As the end of 2020 approaches, several tax planning opportunities may be available to help reduce your tax burden, especially as Congress enacted various provisions designed to help taxpayers during the COVID-19 pandemic. To take advantage of any such strategy, implementation must be completed by year's end, as the tax year closes December 31, 2020. This planning letter highlights several potential tax-saving opportunities for individual taxpayers to consider.

What are the Filing Status and Return Options for the Taxpayer?

As a general reminder, there are several ways in which taxpayers can file an income tax return: married filing jointly, head of household, single, and married filing separately. A married couple, which includes same-sex marriages, may elect to file one return reporting their combined income, computing the tax liability using the tax tables or rate schedules for "Married Persons Filing Jointly." If a married couple files separate returns, in certain situations they can amend and file jointly, but they cannot amend a jointly filed return to file separately once the due date has passed. A joint return may be filed even though one spouse has neither gross income nor deductions. If one spouse dies during the year, the surviving spouse may file a joint return for the year in which his or her spouse died. Generally, married filing jointly will yield a lower overall tax liability than married filing separately for most couples. In addition, for tax years 2020–2025, the so-called "marriage penalty" only applies to couples whose combined taxable income exceeds approximately $600,000.

Certain married persons who do not elect to file a joint return may be entitled to use the lower head of household tax rates. Generally, to qualify as head of household, the taxpayer must not be a resident alien, must satisfy certain marital status requirements such as living apart, and must maintain a household for a person who is their dependent, and must be entitled to a dependency deduction for that person.

Consider Adjusting Withholding or Making Estimated Payments to Reduce Underpayments or Reducing Refunds: If, after reviewing the 2019 return, the taxpayer had a balance due, consider adjusting paycheck withholding for the remainder of 2019, and/or make an estimated payment to avoid an estimated tax penalty. An individual may be able to avoid the penalty by paying withholding and/or estimated taxes based on 100% of the tax shown on the 2019 return. However, if an individual's adjusted gross income as shown on the 2019 return exceeds $150,000 ($75,000 in the case of a married individual who files separately), the amount of the required installment generally increases to 110% of the tax shown on the 2019 return.

Also factor in the 3.8% net investment income tax, the receipt of unemployment benefits, and early and COVID-19 distributions from IRAs and 401(k) plans when adjusting withholding or making estimated payments.

With the $10,000 deduction limit on state and local taxes (SALT) in place, the acceleration of the fourth estimated state income tax payment into December 2020 to increase the current-year SALT deduction may be less important. However, accelerating or deferring the state estimated payment may make a difference in being able to claim a higher itemized deduction versus the standard deduction, so the timing of the payment still should be considered.

What Are the Basic Numbers the Taxpayer Needs to Know?

Because many tax benefits are tied to or limited by adjusted gross income (AGI) — IRA deductions, for example — a key aspect of tax planning is to estimate both 2020 and 2021 AGI. Also, when considering whether to accelerate or defer income or deductions (discussed further below), be aware of the impact this may have on AGI and the ability to maximize itemized deductions that are tied to AGI. The 2019 tax return and 2020 pay stubs and other income and deduction-related documents are a good starting point for estimating AGI.

Another important number is a taxpayer's "tax bracket," i.e., the rate at which the last dollar of income is taxed. The tax rates for 2020 are 10%, 12%, 22%, 24%, 32%, 35% and 37%. A "tax bracket" is the range of taxable income to which a particular marginal rate applies. (For example, for 2020, married taxpayers who file a joint return with taxable income of $414,701 to $622,050 have a marginal tax rate of 35% and are said to be in the 35% tax bracket). Although the income thresholds for the tax brackets are indexed for inflation, if income increases faster than the inflation adjustment, the taxpayer may be pushed into a higher bracket, and thus subject to a higher marginal tax rate. If so, the potential benefit from any tax-saving opportunity is increased (as is the cost of overlooking the opportunity).

Another key number is the standard deduction. For 2020, the standard deduction is $24,800 for married filing jointly and surviving spouses, $18,650 for head of household, and $12,400 for all other taxpayers. The standard deduction is important for planning the timing of one's itemized deductions (as discussed further below) as a taxpayer needs itemized deductions that exceed the standard deduction in order to achieve additional tax savings.

How Does Deferring the Receipt of Income Until 2021 Help?

If the taxpayer expects adjusted gross income (AGI) to be higher in 2020 than in 2021, or anticipates being in the same or a higher tax bracket in 2020, he/she may benefit by deferring the receipt of income until 2021. Deferring income is advantageous so long as the deferral does not bump the individual into a higher tax bracket in the succeeding year(s). Deferring income may be disadvantageous, however, if the deferred income is subject to §409A, thus making the income includible in gross income and subject to additional tax. Some ways to defer income include:

Delay Billing: Self-employed taxpayers who file Schedule C (e.g., sole proprietors and single-member LLCs) and who operate on a calendar year, cash basis accounting method, may delay year-end billing to clients so that payments will not be received until 2021.

Interest and Dividends: Interest income earned on Treasury securities and bank certificates of deposit (CDs) with maturities of one year or less is not includible in income until received. To defer interest income, an individual should consider buying short-term bonds or certificates that will not mature until 2021. If there is a possibility of receiving dividends from a closely held company, the individual should weigh the timing of receipt of those dividends.

Capital Gains: The timing of transactions generating capital gains and losses should be considered whenever possible. Attention should also be paid as to the holding period of the investment as long-term capital gains (i.e., gains from assets held for more than one year) are taxed at preferential rates not exceeding 20% whereas short-term capital gains are taxed as ordinary income tax rates.

To avoid recognizing capital gains altogether, an individual should consider donating appreciated property to charity rather than selling it, especially if doing so may result in overall itemized deductions exceeding the individual's standard deduction for 2020.

What Benefits Arise from Accelerating the Receipt of Income into 2020?

In limited circumstances, taxpayers may benefit by accelerating income into 2020. For example, if the taxpayer anticipates being in a higher tax bracket in 2021 than in 2020 or may need additional income to take advantage of an offsetting deduction or credit that will not be available in future tax years, it may make sense to accelerate the receipt of income. However, accelerating income into 2020 may be disadvantageous if the taxpayer expects to be in the same or lower tax bracket for 2021.

If self-employed, it could be disadvantageous to accelerate income, even if the individual will be in a higher bracket in 2020, if the acceleration causes the individual to cross a threshold that would result in an offsetting reduction in the §199A qualified business income deduction. The §199A deduction phase-out thresholds for 2020 are $326,600 for joint filers and $163,300 for all other taxpayers.

If accelerating income will be beneficial, ways to accomplish this include:

Year-End Bonuses: If the individual's employer generally pays year-end bonuses early in 2021, ask to have the bonus paid before the end of 2020.

Retirement Plan/IRA Distributions: For taxpayers that are over age 59 1/2 that participate in an employer retirement plan or have an IRA, consider taking any taxable withdrawals before 2021. Taxpayers also may also want to consider making a Roth IRA rollover distribution, as discussed below.

2020 also presents a special opportunity for taxpayers to take distributions from §401k plans and IRAs due to COVID-19. If the taxpayer meets certain requirements, " coronavirus-related distributions" up to an aggregate limit of $100,000 from all plans and IRAs:

• Are included in taxable income over a three-year period, one-third each year, beginning in the year you receive the distribution, or, if elected, in the year you receive the distribution.

• Are not subject to the 10% additional tax on early distributions (including the 25% additional tax on certain SIMPLE IRA distributions) that may otherwise apply to most withdrawals before age 59 ½.

• Are not subject to mandatory tax withholding, and

• May be repaid to an IRA or workplace retirement plan within three years, if eligible for tax-free rollover treatment.

To be eligible for COVID-19 relief, coronavirus-related withdrawals or loans can only be made to an individual if:

• The individual (or the individual's spouse or dependent) is diagnosed with the virus SARS-CoV-2 or with coronavirus disease 2019 (collectively, COVID-19) by a test approved by the CDC (including a test authorized under the Federal Food, Drug, and Cosmetics Act);

• The individual experiences adverse financial consequences as a result of: (1) the individual being quarantined, being furloughed or laid off, having work hours reduced, being unable to work due to lack of childcare, having a reduction in pay (or self-employment income), or having a job offer rescinded or start date for a job delayed, due to COVID-19; (2) the individual's spouse or a member of the individual's household (that is, someone who shares the individual's principal residence) being quarantined, being furloughed or laid off, having work hours reduced, being unable to work due to lack of childcare, having a reduction in pay (or self-employment income), or having a job offer rescinded or start date for a job delayed, due to COVID-19; or (3) closing or reducing hours of a business owned or operated by the individual, the individual's spouse, or a member of the individual's household, due to COVID-19.

Note that you may re-contribute all or part of certain coronavirus-related distributions to an eligible retirement plan (including an IRA) within three years beginning on the day after the date you received the distribution. Repayments will be treated as though they were eligible direct rollovers. Amounts repaid are not subject to any contribution or rollover limits.

A special provision gives taxpayers the ability to distribute tax-free to charity up to $100,000 from a traditional or Roth IRA maintained for an individual who has reached age 70 1/2.

How Can an Individual Plan His/her Itemized Deductions?

Deduction timing is an important element of year-end tax planning. However, deduction planning is complex, due to factors such as AGI levels, AMT, filing status, and the increased standard deduction. Cash-method taxpayers should keep the following general principles in mind:

Deduction in Year Paid: An expense is only deductible in the year in which it is actually paid. Under this rule, if the taxpayer's tax rate is going to increase in 2021, it may be a good strategy to postpone spending until after 2020 to take the deduction in 2021.

Payment by Check: Date checks before the end 2020 and mail them before January 1, 2021.

Promise to Pay: A promise to pay or providing a note does not make the expense deductible. But a deduction can be taken if the taxpayer pays with money borrowed from a third party. For example, paying by credit card in 2020 allows the taking of a deduction even though the credit card bill won't be paid until 2021.

Standard Deduction versus Itemized Deduction Planning: Deduction planning is also affected by the standard deduction. As noted earlier, for 2020 returns, the standard deduction is $24,800 for married filing jointly and surviving spouses, $18,650 for head of household, and $12,400 for all other taxpayers.

If itemized deductions are relatively constant and are close to the standard deduction amount, little or no benefit will be gained from itemizing deductions each year. But simply taking the standard deduction each year means the loss of the benefit of itemized deductions that exceed the standard deduction. To maximize the benefits of both the standard deduction and itemized deductions, consider adjusting the timing of deductible expenses, i.e., " bunching," so that they are higher in one year and lower the following year. This can be accomplished, for example, by paying deductible expenses in 2020, such as mortgage interest due in January 2021, and state estimated tax payments due in early 2021, or doubling up on charitable contributions every other year.

Medical Expenses: For 2020, medical expenses, including amounts paid as health insurance premiums, long-term care insurance premiums, and dental insurance premiums are deductible only to the extent that the total medical and dental expenses exceed 10% of AGI for all taxpayers. Bunching medical and dental expenses in one calendar year can help maximize the allowable deduction.

State and Local Income Taxes and General Sales Taxes (SALT): If the taxpayer anticipates a state income tax liability for 2020 and plans to make an estimated payment typically due in January 2021 consider making the payment before the end of 2020. Taxpayers may elect to itemize and deduct state and local general sales taxes in lieu of the itemized deduction for state and local income taxes. In either case, the $10,000 ($5,000 if married filing separate returns) SALT deduction limitation may significantly impact this type of deduction planning.

Charitable Contributions: For 2020, two special rules apply to charitable contributions. First, for taxpayers that do not itemize deductions, a $300 above-the-line deduction in addition to the standard deduction is available, but only for cash gifts to public charities. For taxpayers that itemize deductions, the general 60% of AGI deduction limit for cash gifts to public charities has been increased to 100% of AGI, i.e., there is no limit for 2020.

Consider making charitable contributions by the end of 2020 using a credit card if the bill will not have to be paid until 2021. A mere pledge to make a donation is not deductible, however, unless it is paid by the end of the year. When claiming a deduction for donations of cars, boats and airplanes of more than $500, the amount available as a deduction depends on what the charity does with the donated property, not just the fair market value of the donated property. If the organization sells the property without any significant intervening use or material improvement to the property, the amount of the charitable contribution deduction cannot exceed the gross proceeds received from the sale.

What Tax Benefits are Available for Taxpayers with Children?

Child Tax Credit: A tax credit of $2,000 per qualifying child under the age of 17 is available for 2020, but a child must qualify as a dependent of the taxpayer, and the qualifying child must be younger than the taxpayer. The credit phases-out for higher earning individuals and couples. A portion of the credit is refundable.

A $500 nonrefundable credit for dependents other than qualifying children (e.g., a child over the age of 17 or an elderly parent living with you who qualifies as a dependent) also is available in 2020. There is no age limit, but the dependency test must be satisfied.

Credit for Adoption Expenses: For 2020, the adoption credit limitation is $14,300 of aggregate expenditures for each child. Families who finalize the adoption of a child with special needs in 2020 and fulfill the eligibility requirements can claim the full credit of $14,300, regardless of whether they had any expenses. The credit phases out ratably down to $0 for taxpayers whose income is between $214,520 and $254,520.

Education Credits: The American Opportunity Tax Credit (AOTC) is available for qualified tuition and fees paid on behalf of a student (i.e., the taxpayer, the taxpayer's spouse, or a dependent) who is enrolled on at least a half-time basis. The maximum credit is $2,500 (100% of the first $2,000, plus 25% of the next $2,000). The credit is available for the first four years of the student's post-secondary education.

The AOTC is phased out at modified AGI levels between $160,000 and $180,000 for joint filers, and between $80,000 and $90,000 for other taxpayers. Forty percent of the credit is refundable, which means that a taxpayer can receive up to

$1,000 even if no taxes are owed. “Qualified tuition and related expenses” include expenditures for “course materials” (i.e., books, supplies, and equipment needed for a course of study whether or not the materials are purchased from the educational institution as a condition of enrollment or attendance).

One way to take advantage of the AOTC for 2020 is to prepay spring 2021 tuition. In addition, if it is known what books the student will need for the spring 2021 semester, those can be bought in 2020 and the costs qualify for the credit for 2020.

The Lifetime Learning Credit (LLC) is available for qualified tuition and related expenses paid for eligible students enrolled in an eligible educational institution. This credit can help pay for undergraduate, graduate and professional degree courses — including courses to acquire or improve job skills. There is no limit on the number of years you can claim the credit. For 2020, the maximum credit is $2,000 (20% of qualified tuition and fees up to $10,000). A student need not be enrolled on at least a half-time basis so long as he or she is taking post-secondary classes to acquire or improve job skills. As with the AOTC, eligible students include the taxpayer, the taxpayer's spouse, or a dependent. For 2020, the LLC begins to phase out at modified AGI levels of $59,000 for single taxpayers and $118,000 for joint filers. The LLC is not a refundable credit.

Coverdell Education Savings Account: The aggregate annual contribution limit to a Coverdell education savings account is $2,000 per designated beneficiary of the account. For 2020, the limit is phased out for individual contributors with modified AGI between $95,000 and $110,000 and joint filers with modified AGI between $190,000 and $220,000. The AGI amounts are not indexed for inflation. The contributions to the account are nondeductible but the earnings grow tax-free. Coverdell account holdings can be distributed tax-free if used for qualifying expenses (higher education expenses, along with elementary and secondary education expenses).

Student Loan Interest: Taxpayers may be eligible for an above-the-line deduction for student loan interest paid on any “qualified education loan.” The maximum deduction is $2,500. The deduction for 2020 is phased out at a modified AGI level between $140,000 and $170,000 for married taxpayers filing jointly, and between $70,000 and $85,000 for individual taxpayers.

Kiddie Tax: For 2020, the amount that is used to reduce the net unearned income reported on the child's return that is subject to the “kiddie tax,” is $1,100. The same $1,100 amount is used to determine whether a parent may elect to include a child's gross income in the parent's gross income and to calculate the “kiddie tax”. For example, one of the requirements for the parental election is that a child's gross income is more than $1,100 but less than $11,000. The kiddie tax applies to: (1) children under 18 who do not file a joint return; (2) 18-year-old children who have unearned income in excess of the threshold amount, do not file a joint return, and who have earned income, if any, that does not exceed one-half of the amount of the child's support; and (3) children between the ages of 19 and 23 if, in addition to the above rules, they are full-time students.

Note that including a child's income on the parent's return will increase the parent's AGI and taxable income, thus resulting in a higher tax and possible reductions in credits and other amounts that are tied to AGI.

Achieving a Better Life Experience (ABLE) Accounts: This is a type of savings account for individuals with disabilities and their families. For 2020, taxpayers can contribute up to $15,000 (tied to the annual gift tax exclusion). Distributions are tax-free if used to pay the beneficiary's qualified disability expenses.

What IRA/Retirement Savings Rules Can Lower Taxes?

Maximize Retirement Savings: If the maximum §401(k) contribution for 2020 was not selected, a taxpayer may be able to increase contributions for the remainder of 2020 to lower AGI in order to take advantage of some of the tax breaks described herein. Maximizing pre-tax retirement contributions generally is a good tax-saving move.

Traditional IRAs: Individuals who are not active participants in an employer pension plan may make deductible contributions to an IRA. The deadline for 2020 contributions is April 15, 2021. The annual deductible contribution limit for an IRA for 2020 is $6,000. A $1,000 "catch-up" contribution is allowed for taxpayers age 50 or older by the close of 2020, making the total limit $7,000 for these individuals.

Individuals who are active participants in an employer pension plan also may make deductible contributions to an IRA, but their contributions are limited in amount depending on their AGI. For 2020, the AGI phase-out range for deductibility of IRA contributions is between $65,000 and $75,000 of modified AGI for single persons (including heads of households), and between $104,000 and $124,000 of modified AGI for married taxpayer filing jointly. Above these ranges, no deduction is allowed. A married taxpayer filing a separate return may not deduct IRA contributions if his/her modified AGI is $10,000 or more.

In addition, an individual will not be considered an "active participant" in an employer plan simply because the individual's spouse is an active participant for part of a plan year. The taxpayer may be able to take the full deduction for an IRA contribution regardless of whether their spouse is covered by a plan at work, subject to a phase-out if their joint modified AGI is $196,000 to $206,000 ($0 – $10,000 if married filing separately) for 2020. Above this range, no deduction is allowed.

IRA Rollovers: For 2020, taxpayers may make only one IRA-to-IRA rollover per year. (Direct trustee to trustee rollovers are not affected.) A second attempted rollover will be treated as a withdrawal and taxed at regular rates, plus a possible 10% early withdrawal penalty.

Spousal IRA: If an individual files a joint return and has less compensation than his or her spouse, the IRA contribution is limited to the lesser of $6,000 for 2020 plus age 50 catch-up contributions ($1,000 for 2020), or the total compensation of both spouses reduced by the other spouse's IRA contributions (traditional and Roth).

Roth IRA: This type of IRA allows individuals to make nondeductible contributions of up to $6,000 ($7,000 if making an eligible catch-up contribution) for 2020. Earnings grow tax-free, and distributions are tax-free provided no distributions are made until more than five years after the first contribution and the individual has reached age 59 1/2. Distributions may be made earlier on account of the individual's disability or death.

The maximum contribution is phased out in 2020 for persons with an AGI from $196,000 to $206,000 for married taxpayers filing jointly, $124,000 to $139,000 for single taxpayers (including heads of households), and between $0 and $10,000 for a married taxpayer filing separately who lived with the spouse during the year. A Roth IRA must be established and funded by April 15, 2021, for the contribution to be considered a 2020 contribution.

Roth IRA Conversion Rule: Funds in a traditional IRA (including SEPs and SIMPLE IRAs), §401(a) qualified retirement plan, §403(b) tax-sheltered annuity, or §457 government plan may be rolled over into a Roth IRA. Such a rollover, however, is treated as a taxable event, and the taxpayer will pay tax on the amount converted. No penalties will apply if all the requirements for such a transfer are satisfied.

Section 401k Contribution: The §401(k) elective deferral limit is $19,500 for 2020. If the taxpayer's §401(k) allows for catch-up contributions for 2020 and the taxpayer reaches age 50 by December 31, 2020, an additional $6,500 may be contributed to the §401(k) account, for a total maximum contribution of $26,000 ($19,500 in regular contributions plus $6,500 in catch-up contributions).

SIMPLE Plan Contribution: The SIMPLE plan deferral limit is $13,500 for 2020. If the taxpayer's SIMPLE plan has been amended to allow for catch-up contributions for 2020 and the taxpayer will be 50 years old by December 31, 2020, an additional $3,000 may be contributed.

Catch-Up Contributions for Other Plans: If the taxpayer will be 50 years old by December 31, 2020, an additional $6,500 can be contributed to a §403(b) plan, SEP, or eligible §457 government plan.

Saver's Credit: A nonrefundable tax credit is available based on the qualified retirement savings contributions to an employer plan made by an eligible individual. For 2020, only taxpayers filing joint returns with AGI of $65,000 or less, head of household returns with AGI of $48,750 or less, or single returns (or separate returns filed by married taxpayers) with AGI of $32,500 or less, are eligible for the credit. The amount of the credit is equal to the applicable percentage (10% to 50%, based on filing status and AGI) of qualified retirement savings contributions up to a maximum credit of $2,000.

Required Minimum Distributions: For 2020 only, the CARES Act waives required minimum distributions during 2020 for IRAs and retirement plans, including beneficiaries with inherited accounts. This waiver includes RMDs for individuals who turned age 70 ½ in 2019 and take their first RMD in 2020. If an individual has already taken an RMD in 2020, including someone who turned 70 ½ during 2020, the individual may return the distribution to their account or other qualified plan under certain circumstances.

What Tax Savings Are Available for Taxpayers with Investment Income?

The following rules apply for most capital asset transactions in 2020:

• Capital gains on property held one year or less are taxed at an individual's ordinary income tax rate.

• Capital gains on property held for more than one year are taxed depending on the taxpayer's regular income tax bracket.

For 2020, the maximum capital gains rate is 20% for a taxpayer with taxable income above $496,600 (in the case of a joint return or surviving spouse), $248,300 (in the case of a married individual filing a separate return), $469,050 in the case of an individual who files as head of household, or $441,450 in the case of any individual. For taxpayers in the lower tax brackets, the capital gains rate is 0% or 15% (depending on the taxpayer's income).

An additional 3.8% tax is levied on certain unearned income for higher-income taxpayers. The net investment income tax (NIIT) is levied on the lesser of net investment income (NIIT) or the amount by which modified AGI (MAGI) exceeds certain dollar amounts - $250,000 for married taxpayers filing jointly, $125,000 for married taxpayers filing separate returns, and $200,000 for single individuals. Investment income is: (1) gross income from interest, dividends, annuities, royalties, and rents (other than from a trade or business); (2) other gross income from any business to which the tax applies; and (3) net gain attributable to property that is not attributable to an active trade or business. Investment income does not include distributions from a qualified retirement plan or amounts subject to self-employment tax. This rule applies mostly to passive businesses and the trading in financial instruments or commodities. With this additional tax, the maximum net capital gains rate is 23.8% in 2020.

Year-end strategies to reduce exposure to the NIIT would be to exchange real property through a like-kind exchange to defer recognition of any gain until a future year when MAGI may be lower, or, if planning on selling the taxpayer's principal residence that has a gain over the exempted amounts ($250,000/$500,000 depending on filing status), postponing the sale until after the year, if income will be lower in 2021.

Timing of Sales: Consider timing the sale of assets so as to have offsetting capital losses and capital gains. Capital losses may be fully deducted against capital gains and also may offset up to $3,000 of ordinary income ($1,500 for a married individual filing separately). In general, when losses are taken, long-term losses are first matched against long-term gains, and short-term losses against short-term gains. If there are any remaining losses, they may be used to offset any remaining long-term or short-term gains, or up to $3,000 (or $1,500) of ordinary income. When and whether to recognize such losses should be analyzed in light of possible future changes in the capital gains rates.

If a taxpayer sells stock at a loss, he/she must wait 31 days before re-purchasing the same stock or else the wash sale rules apply, which would disallow the loss.

Defer Taxes by Investing in Qualified Opportunity Funds (QOFs): A taxpayer who invests in Qualified Opportunity Zone property through a Qualified Opportunity Fund (QOF) can temporarily defer tax on the amount of eligible gains they invest. A taxpayer can defer tax on eligible gains invested in a QOF until the earlier of (1) an inclusion event, or (2) by December 31, 2026. Eligible gains include both capital gains and qualified §1231 gains, but only if the gains are: (1) recognized for federal income tax purposes before January 1, 2027, and (2) not from a transaction with a related person.

The amount of time you hold the QOF investment determines the tax benefit you receive. When you make an election to defer the gain, the basis in the QOF investment becomes zero. The QOF basis increases the longer you hold your interest in the QOF. If you hold your investment in the QOF for at least 5 years, your basis (the amount of your investment) will increase by 10% of the deferred gain. If you hold your investment in the QO for at least 7 years, your basis (the amount of your investment) will increase by an additional 5% of the deferred gain. If you hold your investment in the QOF for at least 10 years, you may be able to permanently exclude gain resulting from a qualifying investment when it is sold or exchanged. The exclusion occurs if you elect to increase the basis of your QOF investment to its fair market value on the date of the sale or exchange.

Dividends: Qualified dividends received in 2020 are subject to rates similar to the capital gains rates. Therefore, qualifying dividends on stocks held for more are taxed at a maximum rate of 20% (23.8% if subject to the net investment income tax). Qualifying dividends include dividends received from domestic and certain foreign corporations. Non-qualifying dividends are subject to ordinary income rates (up to 40.8% (37% income tax rate plus 3.8% net investment income tax rate)).

Exclusion of Gain Attributable to Certain Small Business Stock: One-hundred percent (100%) of the gain on the sale of "small business stock" under §1202 is excluded from income. The stock must be held for more than five years to qualify for the exclusion. (If the stock was acquired on or before September 27, 2010, other less favorable exclusion rules apply).

Installment Sales: Generally, a sale occurs when property is transferred. If a gain will be realized on the sale, income recognition will normally be deferred under the installment method until payments are received, so long as one payment is received in the year after the sale. Thus, if a taxpayer expects to sell property at year-end, and it makes economic sense, consider selling the property using the installment method to defer payments (and tax) until next year or later. Using the installment sale method also may defer exposure to the 3.8% NIIT.

Qualified Equity Grants: Individuals who work at a start-up company may be able to defer taxation on vested qualified stock while they have insufficient cash flow to cover their tax liability. The employee makes a special election regarding stock attributable to options exercised or restricted stock units settled in 2020 or later, so that no amount will be included in income for the first tax year in which the rights of the employee in the stock are transferable or are not subject to a substantial risk of forfeiture. In many cases, a qualified equity grant defers taxation until five years after the employee vests in the qualified stock.

Are There Energy Incentives to Consider?

Residential Energy Efficient Property Credit: Tax incentives are available to taxpayers who install certain energy efficient property, such as solar electric property, solar water heaters, geothermal heat pumps, small wind turbines and fuel cell property. A credit is available for a percentage of the expenditures incurred for such property. Taxpayers making or planning to make improvements to their home by the end of 2020 should consult their tax adviser to determine the maximum allowable credit.

What Planning Opportunities are Available to Self-Employed Individuals, Sole Proprietors, and Single-Member LLC Owners?

Qualified Business Income Deduction (QBI Deduction): Individual taxpayers with qualified business income from a pass-through entity (partnership, S corporation, LLC or single-member LLC) or a sole proprietorship may be entitled to a 2020 deduction equal to the lesser of the deductible amount of the QBI (generally 20% subject to the W-2 wage basis limit) or 20% of net taxable income from the business. Deductions may also be allowed for 20% of qualified REIT dividends and qualified publicly traded partnership income. Special rules apply for these additional items. The deduction applies to reduce taxable income and is available even if the taxpayer does not itemize deductions. (The QBI deduction does not impact the calculation of the self-employment tax).

For 2020, if taxable income does not exceed a threshold of $326,600 (joint filers), or $163,300 (all other taxpayers), the deduction is generally the lesser of 20% of QBI or 20% of taxable income. If taxable income exceeds the threshold amount, the deduction is subject to a wage basis limit that is phased-in ratably, and only a portion of the income from a specified trade or business is eligible, the W-2 wage limitation applies, and specified service trades or businesses are excluded. However, if taxable income exceeds the threshold amount by $100,000 or more for married taxpayers filing jointly, or by $50,000 or more for other filers, the wage basis limit applies in full, and income from a specified trade or business is not eligible for the QBI deduction. Calculation of the QBI deduction is a fact intensive inquiry. If a taxpayer claims the deduction and understates the amount of tax required to be shown on his/her return by 5% or more, he/she may be to a 40% substantial understatement of tax penalty.

Accelerating Collection of Accounts Receivable: Self-employed taxpayers on a calendar year cash basis accounting method may issue bills and seek payment before the end of 2020 if accelerating the income makes sense. Some clients or customers may be willing to pay for 2021 goods or services in advance, as it generates an additional deduction on their side of the equation.

Limitation on Business Interest: For tax years beginning in 2019 and 2020, the deduction for business interest expense is limited to the sum of (i) business interest income, (ii) 50% of the business's adjusted taxable income (or 30% of ATI, if the taxpayer elects out of the increased limitation), and (iii) floorplan financing interest expense. Taxpayers may elect not to use the increased limitation. A business with average annual gross receipts of $26 million or less is exempt from the limit.

Government Provided Relief Programs: For Paycheck Protection Program (PPP) loans provided to businesses under the CARES Act (Small Business Administration loans), forgiveness or cancellation of all or part of such loans will not be treated as income for tax purposes. Consult your legal and tax adviser for specific program rules.

Home Office Deduction: For self-employed individuals (but not employees), expenses attributable to using the home office as a business office are deductible if the home office is used regularly and exclusively: (1) as a taxpayer's principal place of business for any trade or business; (2) as a place where patients, clients, or customers regularly meet or deal with the taxpayer in the normal course of business; or (3) in the case of a separate structure not attached to the residence, in connection with a trade or business. If a taxpayer uses part of the home as a business office, determining the amount of any deduction available can be tricky, but an IRS-provided safe harbor could be used to minimize audit risk.

Depreciation and Section 179 Election to Expense Equipment Purchases and Certain Real Property Improvements: If the taxpayer is in business and purchases equipment, he/she may depreciate such equipment or make a " §179 election," which allows the taxpayer to expense (i.e., currently deduct) otherwise depreciable business property (but not investment property). For 2020, the allowable deduction is $1,040,000 (with a phase-out beginning at $2,590,000). Qualified improvement property, as well as certain other improvements to nonresidential real property (roofs, heating, ventilation, and air-conditioning property, fire protection and alarm systems, and security systems) that may not be eligible for bonus depreciation, are eligible for expensing under §179.

Bonus Depreciation: Business or investment property placed in service in 2020 including certain used property, may be eligible for a 100% bonus depreciation deduction (separate from §179 expensing). Taxpayers engaged in a business may want to consider accelerating the placing in service of property or the decision to purchase assets for use in the business, in order to take advantage of this deduction. Taxpayers may not take a bonus depreciation deduction for the same expense that is deducted under §179.

NOL Carryback/Carryforward Period: Taxpayers may carryback net operating losses (NOLs) arising in tax years beginning in 2018, 2019, and 2020, to each of the five tax years preceding the tax year of the loss. Alternatively, NOLs arising in these years may be carried forward indefinitely. In addition, for tax years beginning in 2018, 2019, and 2020, the rule limiting the use of NOLs to offset no more than 80% of taxable income (disregarding the NOL deduction itself) does not apply.

Capitalization v. Expensing for Materials and Supplies and Repairs: Under regulations, a deduction is allowed for materials and supplies that have an acquisition or production cost of $200 or less. A de-minimis safe harbor provides that for repairs to be deductible, among other requirements, the unit of property must cost less than $5,000 per invoice or item substantiated by the invoice for taxpayers with applicable financial statements and $2,500 per invoice for taxpayers without applicable financial statements.

Self-Employed Health Insurance Premiums: Self-employed individuals are allowed to claim 100% of the amount paid during the tax year for insurance that constitutes medical care for themselves, their spouses, and their dependents as an above-the-line deduction, without regard to the general 10% of AGI floor.

SEP IRA Contributions: For 2020, self-employed individuals generally can make a SEP contribution that cannot exceed the lesser of 25% of compensation or $57,000. The SEP contribution is an above-the-line deduction that reduces the AGI subject to tax. Note that the self-employment tax is calculated before SEP contributions are calculated. A SEP IRA must be established by the due date of the return (plus any extensions) for the tax year to which the qualifying contribution is made. Thus, an individual can wait until after the close of 2020 to establish and determine their SEP contribution for 2020.

What Health Care Issues Should be considered for Year-End Planning?

Health Care Flexible Spending Accounts: For 2020, cafeteria plans can provide that employees may elect no more than $2,750 in salary reduction contributions to a health FSA. Typically, employers require the following year's election to be set prior to the end of the year. To estimate the best amount to contribute, taxpayers need to identify potential medical expenses.

Health Savings Accounts: A health savings account (HSA) is a trust or custodial account exclusively created for the benefit of the account holder and his or her spouse and dependents, and is subject to rules similar to those applicable to individual retirement arrangements (IRAs). Contributions to an HSA are deductible, within limits. For 2020 the annual limitation on deductions for an individual with self-only coverage under a high deductible health plan is $3,550; for an individual with family coverage under a high deductible health plan is $7,100. For 2020, the annual "catch up" contribution amount for individuals age 55 and older is $1,000.

For 2020, a "high deductible health plan" is as a health plan with an annual deductible that is not less than $1,400 for self-only coverage or $2,800 for family coverage, and the annual out-of-pocket expenses (deductibles, co-payments, and other amounts, but not premiums) do not exceed $6,900 for self-only coverage or $13,800 for family coverage. In computing the annual HSA contribution amount, an individual who is eligible during the last month of a tax year (December) is treated as having been eligible for all prior months during the tax year and, thus, is allowed to make contributions for months before the individual was enrolled in a high deductible health plan.

Is the Taxpayer Subject to the Alternative Minimum Tax (AMT)?

The 2017 Tax Cuts and Jobs Act of 2017 (TCJA) significantly increased the AMT exemption amounts and raised phase-out thresholds for these exemptions, such that the AMT generally impacts fewer taxpayers. For 2020, the AMT exemption amounts are $113,400 for joint returns and surviving spouses; $72,900 for unmarried individuals; and $56,700 for married individuals filing separate returns. The exemption phase-out range for 2020 begins at $518,400 for unmarried individuals and $1,036,800 for married filing jointly.

Also, for 2020, nonrefundable personal credits can offset an individual's regular and alternative minimum tax, and capital gains will be taxed at lower favorable rates for AMT. For 2020, the amount of AMTI above which the 28% rate applies is $197,900 for married individuals filing joint returns and $98,950 for other taxpayers.

If a taxpayer has stock holding due to the exercise of an incentive stock option (ISO) during 2020 that is now below the value at the exercise date (i.e., " underwater"), consider selling the shares before the end of the year to avoid the AMT tax due on the original exercise of the option. Some of the standard year-end planning ideas will not reduce tax liability if the taxpayer is subject to the AMT because different rules apply. For example, state income and property tax deductions are disallowed in calculating AMT.

What Gift Giving Techniques Are Available to Reduce Gift Tax?

Annual Gift Tax Exclusion: The most commonly used method for tax-free giving is the annual gift tax exclusion, which, for 2020, allows a person to give up to $15,000 to each donee without reducing the giver's estate and lifetime gift tax exclusion amount. A person is not limited as to the number of donees to whom he or she may make such gifts. Further, because the annual exclusion is applied on a per-donee basis, a person can leverage the exclusion by making gifts to multiple donees (family and non-family). Thus, if an individual makes $15,000 gifts to 10 donees, he or she may exclude $150,000 from gift tax. In addition, because spouses may combine their exclusions in a single gift from either spouse, married givers may double the amount of the exclusion to $30,000 per donee. For 2020, the first $157,000 of gifts to a noncitizen spouse (other than gifts of future interests in property) are excluded from gift tax. A person may not carry over his or her annual gift tax exclusion amount to the next calendar year. Qualifying tuition payments and medical payments do not count against this limit.

If you have any questions, please do not hesitate to call. I would be happy to meet with you at your convenience to discuss the strategies outlined above. While we are getting very close to the end of the year, there is still time to implement these strategies to minimize your 2020 tax liability.