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PART 1: IMPORTANT TAX SAVINGS STRATEGIES TO CONSIDER

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With the end of the year fast approaching, now is the time to start implementing effective tax planning strategies that may help lower your income taxes for 2019 and beyond. The first full filing season under the Tax Cuts and Jobs Act (TCJA) is behind us and our team of tax, accounting and business advisors have been analyzing the complex rules and different scenarios in order to provide clients customized strategies and solutions.

While there is no one-size-fits-all approach to tax planning, we have launched a new Year-End Tax Planning Series in order to address the major areas of consideration and top questions we are receiving from clients. Not all of these scenarios may be applicable, however, you or your business can likely benefit from many of them. **We encourage you to contact us at your earliest convenience so we can help develop a customized strategy that best meets your needs.**

The first part of our Series focuses on **tax planning strategies for individuals** (stay tuned for a forthcoming series that focuses on tax planning strategies for businesses). *Keep in mind many businesses operate as a pass-through entity, which has a significant impact on the owner's individual tax return. Therefore, there may be some crossover of planning techniques.*

Postpone Income or Accelerate Deductions

Throughout our Year-End Tax Planning Series, we will get into specifics on how and when you should postpone income into a future tax year or accelerate deductions into 2019. These types of strategies make sense if doing so will reduce your adjusted gross income (AGI) to take advantage of various tax breaks (ex. Child Tax Credit, Qualified Business Income Deduction, Education Credits etc.) or to simply reduce your overall tax burden. A taxpayer needs to be careful as an effective tax plan does not only look at the current year but also incorporates future tax years.
For instance, a taxpayer might not want to postpone income until 2020 or beyond if it is anticipated that they will be in a higher tax bracket in those years. The same is true for accelerating deductions into 2019 when the deduction may be more valuable in a future year in which the taxpayer is in a higher tax bracket.

Implement a Tax-Loss Harvesting Strategy

As the year-end approaches, a crucial tax planning strategy for many investors is tax-loss harvesting, which involves selling securities at a loss to offset realized gains during the year. This strategy works best when offsetting short-term (ST) capital gains as they are typically taxed at a higher rate than long-term (LT) capital gains. The strategy can also be effective with LT capital gains but a taxpayer needs to be careful that they are not in a 0% tax bracket with regards to their LT capital gains. If a taxpayer is already in the 0% tax bracket, they would essentially receive no benefit for harvesting the loss. Keep in mind you can always buy back the stock you sold at a loss, just be sure not to violate the wash sale rules or the tax planning strategy would become ineffective.

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Invest in a Qualified Opportunity Fund (QOF)

One of the more noteworthy provisions of the TCJA was the tax benefits available for an investment in a QOF. The rules related to these investments are extremely complex but in general the following tax incentives can be obtained:

1) **Defer realized gain** - An original realized gain, receiving capital gain treatment and subsequently invested in a QOF, can be deferred until the earlier of the date on which the QOF investment is sold/exchanged or December 31, 2026.

2) **Partial gain exclusion on the original deferred gain** - As stated above, the original realized gain that was invested in the QOF eventually needs to be recognized on a tax return. If a taxpayer holds their investment in the QOF for at least 5 years, they will receive a 10% step-up in basis. If they hold their investment in the QOF for at least 7 years, they will receive an additional 5% step-up in basis.

3) **Full gain exclusion on an investment in a QOF** - If a taxpayer holds their investment in the QOF for at least 10 years, they will receive a step-up in basis equal to the fair market value of the investment upon disposition.

The best way to understand these tax benefits is through an example:

*Taxpayer G sells Apple stock on December 30, 2019 for a realized capital gain of $100,000. G timely invests $100,000 into a QOF. Therefore, G can defer the $100,000 capital gain on their 2019 return. G ends up holding the investment in the QOF for at least 10 years which allows G to take full advantage of all the tax incentives available. The original realized capital gain will get a 15% step-up in basis which allows G to only have to recognize an $85,000 capital gain (($100,000 - ($100,000*15%)) on their 2026 return. After year 10 if G sells the QOF investment for $250,000 G would pay no tax on the sale as the investment would receive a basis step-up equal to the fair market value of $250,000.*

Exercising Incentive Stock Options (ISOs)

A taxpayer who holds ISOs may want to consider exercising some of those options before the end of the year. Upon exercising an ISO there is typically no regular tax consequence at the exercise date but there is an adjustment in calculating a taxpayer's alternative minimum tax (AMT). The difference between the fair market value of the stock and the option's exercise price is an adjustment in calculating taxpayer's AMT. Under the TCJA, the AMT exemption as well as the phase-out threshold were significantly increased which has resulted in fewer taxpayers being subject to AMT. Therefore, a taxpayer may be able to exercise some of their ISOs and not have a regular or AMT tax liability in the year the options were exercised.

Closing

The TCJA was some of the most significant tax legislation to be introduced in 30 years. Some of the old tax planning techniques are no longer applicable and many CPAs are rethinking their approach to year-end tax planning. Regardless of the changes, it is still important to understand your complete tax situation not only for 2019 but also for future years. **In the next part of our Year-End Tax Planning Series, we will take a look at some tax planning strategies specific to the changes with itemized deductions.**

If you have any questions or would like to discuss how these strategies effect your particular situation, please feel free to reach out to one of our tax specialists at Restivo Monacelli LLP.