FRADIN & COMPANY LTD

2020 YEAR-END TAX PLANNING FOR INDIVIDUALS

COVID-19 and IRS and State Delays

2020 has been a challenging year for many of us. The Cares Act was enacted in early 2020 and most **taxpayers received an Economic Impact Payment if they were eligible**. The IRS offices were closed for three months during the spring, due to the pandemic. This created a **large backlog of work**. IRS employees are also drafted to handle FEMA calls and claims in national disasters, and this has created more delay because of the high number of wildfires, hurricanes and floods this year. The Rhode Island Division of Taxation offices were closed for a period in June due to riot damage.

Due to these closings and delays, many taxpayers are still waiting to receive refunds and stimulus checks, and many manual checks sent for tax payment have not been processed. The IRS is still processing manually filed returns, including Amended returns from as far back as March.

Our office has been working with IRS and State Revenue offices to assist our clients in getting their refunds and resolving issues with returns and notices.

Possible Changes for 2020 and 2021 Taxes

With all the uncertainty, we do not know if there will be changes in the filing of 2020 tax returns, as there were for 2019 filing. As always, we strongly encourage you to **efile your tax return** and set up **direct deposit for your refund**.

With changes in Washington, there most likely will be changes in taxes for 2021. We will be watching what Congress will do and get you that information as soon as it is available.

2020 TAX SAVING OPPORTUNITIES

There is still time to reduce your 2020 tax bill and plan ahead for 2020 if you act soon. This letter highlights several potential **tax-saving opportunities** for you to consider. We would be happy to discuss specific strategies for your situation.

2020 Tax Rates

Tax Rates: The **tax rates for 2020** are as follows: 10%, 12%, 22%, 24%, 32%,35% and 37%. You can view a full table of 2020 tax brackets and rates on the Tax Center page of our website at www.fradincpa.com/taxrates2.php.

Adjusted Gross Income*:* For 2020 tax planning, you will want to **estimate your 2020 taxable** income (Adjusted Gross Income or AGI). Your 2019 tax return and your 2020 pay stubs and other income- and deduction-related materials are a good starting point for estimating your 2020 AGI.

State Response to Tax Reform

States react differently to changes to federal tax law. Many states are picking and choosing which federal provisions to adopt and at different times then the federal. Because of this, **your state income tax rules may be drastically different** from the federal income tax rules.

Standard Deduction and Personal Exemptions

The Standard Deduction for 2020 is $12,400 for individuals, $18,650 for Head of Household and $24,800 for married filing jointly. Senior citizens will be allowed additional deduction amounts.

Accelerate or Defer Income

You may benefit by **accelerating income into 2020**, if you anticipate being in **a higher tax bracket in 2021**, or if you need additional income to take advantage of an **offsetting deduction or credit** that will not be available in future tax years.

You may also benefit by **deferring income into 2021**, if you expect to be in **a lower or the same tax bracket in 2021.**

Delay Billing: For self-employed taxpayers using the cash-basis of accounting, you can **delay year-end billing** to clients so that payments will not be received until 2021.

Accelerate Collection of Accounts Receivable: Self-employed taxpayers reporting income and expenses on a cash basis method can **issue invoices and attempt collection before the end of 2020**. If some clients or customers are willing to pay for January, 2021 goods or services in advance, invoice them and collect before year end. Any income received using these steps will shift income from 2021 to 2020.

Retirement Plan Contributions

Maximize Retirement Plan Contributions. If you own an incorporated (S Corp or LLC) or unincorporated (Schedule C Sole Proprietorship) business, consider **setting up a retirement plan** if you don't already have one. It doesn't actually need to be funded until you file your taxes, but **allowable contributions will be deductible on this year's return**. If you are an employee and your employer has a 401(k), **contribute the maximum amount** ($19,500 for 2020), plus an additional **catch-up contribution of $6,500 if age 50 or over**, assuming the plan allows this and income restrictions don't apply.

If you are employed or self-employed with no retirement plan, you can make **a deductible contribution of up to $6,000 a year to a traditional IRA** (deduction is sometimes allowed even if you have a plan). Further, there is also an additional catch-up contribution of $1,000 if age 50 or over.

Deductions

Planning year-end deductions can be complex depending on your individual circumstances. We recommend that you discuss these deductions with us in advance.

If **itemized deductions** are relatively constant and **are close to the standard deduction amount**, little or no benefit will be gained from itemizing your deductions each year. But simply taking the standard deduction each year means you may **lose the benefit of itemized deductions that exceed the standard deduction.** Try to **bunch itemized deductions and "threshold" expenses**, such as medical and dental expenses, every other year. For example, you might pay medical expenses, charitable donations, and real estate taxes in whichever year will do the most good.

Deduction in Year Paid: An expense is **only deductible in the year in which it is actually paid**. Under this rule, if your tax rate is going to increase in 2021, it is a smart strategy to postpone spending until after year end to take the deduction in that year.

Moving Expenses: Moving expenses are no longer tax deductible as of 2018, **unless** you are an active duty member of the armed forces.

Self-Employed Health Insurance Premiums: If you are self-employed, you can claim 100% of the amount you paid during the taxable year for **insurance that constitutes medical care for yourself, your spouse and your dependents.**

***Miscellaneous Deductions**:* As of 2018, **all miscellaneous itemized deductions were eliminated**. For example, safe deposit box, investment fees, work uniforms, union dues, unreimbursed employee business expenses, job hunting expenses and home office deductions. However, if you are a **self-employed, 1099, non-W2** taxpayer working from home, you may be entitled to a home office deduction on your Schedule C

***Medical Expenses**:* For 2020, medical expenses, including amounts paid as health insurance premiums, **are deductible only to the extent that they exceed 7½% of your AGI**. If you can bunch medical expenses in one calendar year, that can help maximize the allowable deduction for that year.

***State and Local Income Taxes and General Sales Taxes**:* The **deduction for state and local taxes was capped at $10,000**. This cap applies to the total of all such taxes you pay in the calendar year. That might include state income tax; property taxes on real estate, fire tax, motor vehicles, boats, TDI and perhaps more.

***Charitable Contributions**:* Consider making **charitable contributions at the end of the year**. You can take the deduction for donations charged on a credit card before December 31, even though you will not pay the bill on your card until 2021. Note that a **pledge to make a donation is not deductible**, you must actually make the donation. Be sure to get receipts for all donations. (Remember that non-cash donations in amounts higher than $500 have some special rules to support the deduction.)

For the 2020 tax year, the **deduction percentage limitation of 60% for cash charitable contributions has been removed** for individual taxpayers. This simply means that any qualified contribution is allowed to the extent that the aggregate of such contributions does not exceed the taxpayer's adjusted gross income.

Starting in 2020, eligible taxpayers are entitled to a deduction of up to $300 for qualified charitable contributions, **even if you do not itemize**.

Common Tax Credits

***Child Tax Credit**:* A tax credit of **$2,000 per qualifying child under the age of 17** is available on this year's return. The credit is phased out starting at an AGI of $400,000 for married filing jointly, and $200,000 for all other taxpayers. A $500 nonrefundable credit for dependents other than qualifying children also is available.

***Education Credits**:* The **American Opportunity Tax Credit** is available for qualified tuition and fees paid on behalf of a student (taxpayer, spouse, or a dependent) who is **enrolled on at least a half-time basis** during the first 4 years of post-secondary education. The maximum credit is $2,500, and is phased out starting at an AGI of $160,000 for joint filers, and $80,000 for other taxpayers.

The **Lifetime Learning Credit** is available for **qualified expenses for other post-secondary classes** to acquire or improve job skills. The maximum credit in 2020 is $2,000. This credit begins to phase out at an AGI of $114,000 for joint filers and $57,000 for single taxpayers.

***Residential Energy Efficient Property Credit**:* Tax incentives are now only available to taxpayers who install certain energy efficient property, such as photovoltaic panels and solar water heating property.

Investment Income

***Capital Gains Tax**:* 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 your ordinary income tax bracket. The maximum capital gains tax rate is 20% for taxpayers in the 37% tax bracket. For taxpayers in lower tax brackets, the rates are 0% and 15%. An additional 3.8% tax is levied on certain unearned income.

***Offsetting Capital Gains and Losses**:* Consider timing the sale of assets so as to **offset any capital gains with capital losses.** Capital losses may be fully deducted against capital gains and also may offset up to $3,000 of ordinary income. If you sell a stock at a loss, you can repurchase the same stock, but must wait 31 days or else be subject to the wash sale rules which would disallow the loss.

Health Coverage Issues

Individual Mandate*:* The Affordable Care Act individual mandate, requiring individuals and their dependents to have health insurance or pay a tax penalty, no longer applies for 2020 for federal. **Rhode Island and many other states do have a health care coverage requirement or will impose a penalty.**

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**. Your employer will probably require you to set your 2021 election before December 31. To estimate the best amount to contribute, you will need to identify potential medical expenses for next year.

Other Issues

Alternative Minimum Tax*: I*n 2018, the alternative minimum tax exemption amounts increased. This means that fewer taxpayers will be subject to it.

Estimated Tax Payments*:* If your withholding doesn't match your tax obligations, you may be able to **avoid any underpayment penalties by paying estimated taxes** based on 100% of the tax estimated for this year, or 110% of the tax shown on last year's return.

Annual Gift Tax Exclusion*:* For 2020 the annual gift tax exclusion is $15,000 to each donee. Qualifying tuition payments and medical payments do not count against this limit.

SUMMARY

If you have any questions, please do not hesitate to call. 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.

This publication is not intended to be financial or tax advice, but is intended only to inform the reader of recent developments. If you require financial or tax advice on a particular matter, please contact us directly at (401) 738-2900, or email info@fradincpa.com

A publication of: **FRADIN & COMPANY LTD, INC.**
1000 Greenwich Avenue • Warwick, RI 02886
401.738.2900 • www.fradincpa.com • info@fradincpa.com