YEAR-END FINANCIAL PLANNING PLAYBOOK

With the end of 2021 coming into focus, we have many areas of uncertainty to navigate on the healthcare, economic, and political fronts. As we encourage our clients to continue thinking and acting long term, there are pockets of near-term financial planning opportunities to consider as the calendar rolls toward year-end.

Although no one can predict what our nation's tax policy will be in future years, we do know the tax rates will change with the possible sunsetting of the Tax Cuts and Jobs Act (TCJA) at the end of 2025, if not before then. Therefore, it is inevitable that tax rates only have one direction to go in the coming years.

With these factors in mind, we highlight a few of the common themes, answer some frequent questions, and summarize steps which could be taken by the end of the year.

BDO WEALTH ADVISORS, LLC

2021 Year-End Checklist

The goal of tax-conscious financial planning is to minimize total taxes paid over the short, mid, and long term. With the possibility that future income tax rates could increase, the following is a sampling of issues to consider.

QUALIFIED PLAN/IRA CONTRIBUTION LIMITS

It's important to ensure you are using any qualified retirement plans and/or IRAs to the best of your ability. For 2021, you can contribute $19,500 ($20,500 for 2022) to a qualified retirement plan (plus an additional $6,500 if you are age 50 or over in both 2021 and 2022).

You can contribute $6,000 to an IRA for 2021 ($6,000 for 2022), plus an additional $1,000 catch-up if you are age 50 or older (in both 2021 and 2022). The deductibility of your IRA contributions is subject to income limits.

REQUIRED MINIMUM DISTRIBUTIONS (RMD)

If you're retired and currently required to take an RMD, you may have enjoyed delaying an RMD in 2020. In 2021, that is no longer possible. Speak with your advisor to help calculate your RMD for this year, if you haven't taken it already.

DID YOU MAKE A CHARITABLE GIFT IN 2021?

For tax filers who claim the Standard Deduction, do not file an itemized tax return, and who normally would not receive a tax benefit from a Charitable Contribution, an extension of the CARES Act allows for an "Above the Line" deduction for a $300 cash donation (or $600 if Married Filing Jointly) made direct to a 501(c)3 charity. Please remember to get documentation and report the gift to your tax preparer. Although a relatively small dollar amount, tax aware planning points to every tax dollar saved being a dollar earned.

WHAT IS THE ROTH CONVERSION STRATEGY THAT SEEMINGLY EVERYONE IS TALKING ABOUT, AND DOES IT MAKE SENSE FOR YOUR TRADITIONAL IRA?

Assets in a Traditional IRA are generally funded with pre-tax dollars, grow tax-free over time, and distributions are taxed at ordinary income tax rates. In a Roth IRA conversion, the owner of a Traditional IRA volunteers to pay taxes now on some or all the assets that have grown tax-deferred in the Traditional IRA. Once the assets are converted to the Roth IRA, the assets continue to grow tax-free. While the original conversion amount can be taken out of the Roth IRA at any time, future earnings can also be taken without penalty or taxation as long as certain minimum requirements are met. Roth Conversions are most effective when the assets converted from the Traditional IRA to a Roth IRA increase in value over time, the owner of the account has the ability to pay taxes out-of-pocket, and future personal income tax rates are higher vs. today's personal income tax rates.

DO YOU OR YOUR SPOUSE NOT HAVE A TRADITIONAL IRA?

As discussed, a Roth IRA allows for assets to grow tax-free as well as for distributions to be taken that are not subject to taxation (certain restrictions apply). If either you or your spouse do not currently have a Traditional IRA, but the household will have earned income in 2021, there is a strategy known as a Back-Door Roth conversion that should be explored with your BDO Advisor.

IF YOU BELIEVE CHANGES WILL SOON OCCUR IN TAX POLICY, WILL YOU BENEFIT FROM A DISCUSSION ON SOLUTIONS WHICH WILL HELP TO PRESERVE THE CURRENTLY HIGH LEVELS OF UNIFIED CREDIT/FEDERAL ESTATE TAX EXCLUSION?

There are a myriad of gifting and estate planning techniques which can be implemented now to help preserve the historically high levels of the Unified Credit/Federal Estate Tax Exclusion of $11.7 million per individual, or $23.4 million per married couple for 2022. These current, relatively high thresholds could head lower soon, which would trigger a lost opportunity for those with a meaningful projected taxable estate.

HAVE YOU EXPLORED ANNUAL GIFTS AS AN OPTION TO REDUCE YOUR TAXABLE ESTATE?

As mentioned previously, if the Unified Credit/Federal Estate Tax Exclusion is lowered significantly, your family could soon find itself facing an estate tax. One option to reduce the amount included in your taxable estate is to make living gifts to your loved ones. You can gift $15,000 annually to each recipient without having to file an IRS Form 709 to disclose the gift. Direct payments to qualified institutions for education or medical expenses of your loved ones have an unlimited gift tax exclusion.

HAVE YOU REVIEWED YOUR BENEFICIARY INFORMATION THIS YEAR?

Now is a good time to simply check your primary and contingent beneficiary information. Beneficiary designations on IRAs and 401k accounts supersede your Will, so make sure to review and update appropriately.

Due to changes brought forward by the SECURE Act, a stretch IRA is no longer a viable strategy for a non-spouse IRA beneficiary. After the IRA owner's death, the SECURE Act's implementation of a forced 10-year period withdrawal may run inconsistent with your intended direction for disbursement to non-spouse beneficiaries. It also might make sense to contact your estate planning attorney to check for an existing provision (or to add flexible wording) in the instance where a trust has been named as beneficiary of your IRA.

WHAT IS A DONOR ADVISED FUND (DAF) AND HOW COULD IT HELP WITH YOUR 2021 TAX PLANNING?

A DAF is a low-cost, effective strategy that provides the opportunity for annual charitable gifting and allows the donor to take a full tax deduction in a single year. A unique application of this strategy allows for the "bunching" of a multi-year gift into a single calendar year. On a related topic for tax filers who file an itemized return, the normal maximum deduction for a *cash* charitable donation is limited to 60% of Adjusted Gross Income (AGI), yet an extension of the CARES Act allows for a deduction of up to 100% of AGI in 2021. (This strategy is subject to AGI limitations. Please consult with your tax advisor for details.) Combining the change to the AGI limitation in the same tax year as a Roth Conversion can be a potentially powerful planning strategy.

CONCLUSION

Acting now on creative financial planning opportunities will help you build momentum into the start of 2022. Please reach out to your BDO Wealth Advisor to explore these issues, address any questions, and take the proper action steps in achieving your year-end financial goals.

CONTACTS:

NAME
Title
xxx-xxx-xxxx / email@bdo.com

NAME
Title
xxx-xxx-xxxx / email@bdo.com

NAME
Title
xxx-xxx-xxxx / email@bdo.com

Visit BDO's hub for wealth management resources: www.bdo.com/wealthadvisors