



Newsletter

NOVEMBER 2020

Freddi Eberhart & Associates Inc. would like to thank you for selecting our firm for your tax and accounting needs. We appreciate the confidence you have shown in us, and we remain ready to assist you at any time. Also, thank you for recommending us to your family, friends, and associates. We truly appreciate your referrals.

This Month:

November 11

- Veterans Day

November 26

- Thanksgiving

November 27

- Black Friday

Reminder

- Conduct year-end tax and financial planning

Included in this issue are planning strategies and techniques which could be of benefit to you through the end of the year, as well as retirement savings tips for small businesses.

Please call if you would like to discuss how this information could impact your situation. If you know someone who can benefit from this newsletter, feel free to send it to them.

Planning Strategies and Techniques Through the End of Year

2020 has brought along many changes in everyday life and this includes the tax landscape. The ongoing COVID-19 (coronavirus) crisis has caused economic uncertainty and there is major incentive to maximize all tax savings now. Additionally, the Coronavirus Aid, Relief, and Economic Security (CARES) Act enacted many taxpayer-friendly provisions, many of which have a 2020 expiration date. On top of that, 2020 sees a presidential election, which always means that major tax policy changes could be months away.

With so much going on in the world, a logical and reasonable tax plan is very important, and can be integral in helping families and businesses get through this very difficult time.

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Planning Strategies and Techniques Available Through the End of Year (Cont'd)

Much of year-end tax planning for 2020 is subject to the outcome of the elections on November 3. A win by Biden (and Democratic control of Congress), likely increases taxes on higher income individuals and corporations. However, a re-election of President Trump (with or without Democratic control of Congress) means a continuation of current tax policies through 2024 is likely.

Year-end tax planning often means determining whether to accelerate or delay income or deductions between years, it may be a good idea to hold off on any decisions until the outcome of the election is clear. Unfortunately, if the election is close and contentious after November 3, there could be less time to act once the results are official. Therefore, it would be wise to make a plan now for both scenarios and get the pieces into place for quick action.

The key to any year-end planning strategy is to minimize taxes. This is done by either reducing income received or increasing deductions, which is easier said than done. However, there are a few simple things that can be done in the waning weeks of 2020 to accomplish this.

If taxes are higher in 2021 an **acceleration** of income into 2020 might be the best option for reducing taxes.

Delay/Reduce Gains

Ordinary income is taxed at seven rates, depending upon the amount. Taxes on capital gains also apply at different rates depending upon the amount of taxable income. For 2020, the capital gains rates are as follows:

	0%	15%	20%
MFJ	\$0 - \$80,000	\$80,001 - \$496,600	Over \$496,600
MFS	\$0 - \$40,000	\$40,001 - \$248,300	Over \$248,300
HOH	\$0 - \$53,600	\$53,601 - \$469,050	Over \$469,050
SINGLE	\$0 - \$40,000	\$40,001 - \$441,450	Over \$441,450
E & T	\$0 - \$2,650	\$2,651 - \$13,150	Over \$13,150

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Planning Strategies and Techniques Available Through the End of Year (Cont'd)

For taxpayers whose income tends to fluctuate from year to year, it would be prudent to examine the impact of sales of investment items. For taxpayers who expect their 2021 income to be at or near a threshold for a higher capital gains bracket, it would be smart to hold off on a sale of a capital item.

Consideration should also be given to the net investment income (NII) tax. The 3.8% NII tax kicks in at \$200,000 of modified adjusted gross income for single and head-of-household filers, \$250,000 for joint filers, and \$125,000 for married taxpayers filing separately. The NII thresholds fall right in the middle of the 15% capital gains bracket.

Maximizing Deductions

For 2020, the standard deduction amounts are \$24,800 for joint filers, \$18,650 for heads of households, and \$12,400 for all other filers. The standard deduction amounts being so high, combined with the \$10,000 limitation on the state and local tax deduction, it is difficult for many taxpayers to claim enough deductions to make itemizing beneficial. Thus, maximizing deductions may not be beneficial for all taxpayers.

Bunching: This involves accumulating charitable contributions, or even medical expenses (see below), from two or more years into one year. For example, a taxpayer may not make any of their normal charitable contributions in 2019, and then double in 2020 to help surpass the standard deduction amount. This, of course must be considered within the context of the election. It may be more beneficial to minimize deductions in 2020 to maximize them in 2021 if higher taxes are likely under a new administration.

Note: The CARES Act does allow an above-the-line charitable contribution deduction up to \$300 for individuals who do not itemize deductions for 2020 **only**. This special deduction applies regardless of the individual's income level.

The same strategy is applicable for deductible medical expenses where the timing can be somewhat flexible, such as for elective procedures (remember, purely cosmetic procedures are not deductible). However, the floor for deductible medical expenses in 2021 is 10%, whereas the floor is 7.5% in 2020. The increase in the floor for deductible medical expenses in 2021 makes it tricky for planning. A potential tax increase in 2021, (hinging on the election results) would mean a taxpayer would generally want to push more deductions to 2021, but the higher floor on the deduction for medical expenses in 2021 could reduce or eliminate the benefits of a delay.

Bunching can be a very effective strategy, but it has to be effectively used, and potentially planned out two or three years in advance to maximize the benefit, while also taking into account shifts in tax policies as a result of political change.

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Planning Strategies and Techniques Available Through the End of Year (Cont'd)

Other Year-end Strategies

Other traditional year-end strategies may still apply including:

- **Maximizing Education Credits and Deductions** – Individuals can claim a credit or a deduction for tuition paid in 2020 even if the academic period begins in 2021, so long as the period begins by the end of March. This is especially important because, absent legislation, the tuition and fees deduction will not be available in 2021.
- **Increasing 401(k) Contributions** – Adjusted gross income (AGI) can be reduced if individuals increase the amount of their 401(k) contributions. As a side note, if a taxpayer has an employer matching program, even if money is tight, they should strive to contribute at least enough to maximize the employer match.
- **IRA Contributions** – Individuals eligible for deductions for IRA contributions can claim deductions, and thus reduce AGI, for amounts contributed through April 15, 2021.

Teacher deductions – Educators can claim a deduction for up to \$250 of classroom expenses (like books, supplies, computer equipment), and should maximize those expenses by year-end

Stimulus Payment

The CARES Act included a \$1,200 credit for the 2020 tax year that was paid to individuals in advance during the spring of 2020 as economic income payments. The amount of the credits was subject to phase-out based upon individual income amounts for 2019 (or 2018 if taxpayers had not yet filed returns for 2019).

As the crisis continues, politicians across the political spectrum have called for a second round of stimulus payments. If legislation were to be passed now it is likely the phase-out would be based on 2019 income amounts. It is possible however, that legislation could be delayed far enough into 2021 that the phase-out would be based on 2020 income amounts. Thus, it may be smart to delay income to 2021 to maximize the amount of a potential second round of economic income payments. While this strategy would seem to run counter to the theory that income should not be delayed to 2021 because taxes could increase, taxes will likely only increase in the event of a Biden victory, and he has stated that he will only increase taxes on incomes above \$400,000. The first round of economic impact payments phased out well below this level, thus there would be no risk of higher taxes.

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Planning Strategies and Techniques Available Through the End of Year (Cont'd)

Required Minimum Distributions

Individuals who have reached age 72 during 2020 (70½ prior to 2020) and are retired generally need to make sure that they are making their required minimum distributions (RMDs) from IRAs. However, the CARES Act eliminated the need to take RMDs for 2020. Despite the CARES Act waiver, it may still be worthwhile to take a distribution in 2020, thereby reducing the size of future RMDs, if it appears that tax rates will go up if Biden wins the election.

Gift Taxes

The TCJA-increased unified exclusion amount for gift taxes is not scheduled to expire until 2026. However, if Biden wins, one possibility is that many of the provisions of TCJA could be rolled back sooner than that. It would be worth considering making any gifts before the end of 2020 to take advantage of the higher exclusion while it is still certain to be available.

Retirement Savings Tips for Small Business Owners

As an owner of a small business, you've proven that you're a self-starter by operating a successful private enterprise. Of equal importance is applying your skills towards saving for your future. Here are some of the most popular tax-advantaged retirement vehicles for small business owners in 2020 and some tips on saving for retirement.

Options if you're not currently enrolled in a plan

For small business owners not currently enrolled in a retirement plan, here are three of the most popular retirement account options:

- **Simplified Employee Pension (SEP) IRA Account.** Contribute as much as 25% of your business's net profit up to \$57,000 for 2020.
- **401(k) Plan.** Contribute up to \$57,000 of your salary and/or your business's net profit.
- **Savings Incentive Match Plan for Employees (SIMPLE) IRA Account.** You can put all your business's net profit in the plan, up to \$13,500 plus an additional \$3,000 if you're 50 or older.

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Retirement Savings Tips for Small Business Owners (Cont'd)

Which plan should you choose? SEP and SIMPLE IRAs are ideal for either sole proprietors or really small businesses (no more than one or two dozen employees). Due to higher administrative costs, 401(k) plans are usually more suited for larger small businesses (more than one or two dozen employees).

Tips to maximize your retirement contributions

For small business owners who are currently enrolled in a retirement plan, here are some suggestions for maximizing your annual contributions into your retirement accounts:

Pay yourself first. Instead of funding your retirement account with whatever is left over after paying your monthly bills, decide at the beginning of each month how much you want to set aside to fund your retirement. Make funding your retirement each month as important as your other bills. Then assume that you pay your retirement bill first. If you run out of money before paying all your bills, decide if there are any expenses that can be pared back for subsequent months so you can meet your monthly retirement savings goal.

List your retirement contributions on your income statement. It is easy to forget about retirement planning when running the day-to-day operations of your business. To keep retirement contributions top-of-mind, record these as a separate line item on your business's income statement.

Review your tax situation at least twice a year. Tax planning is now more important than ever with the uncertainty caused by the recent pandemic. So review your tax situation at least twice every 12 months to see how to maximize each year's retirement contributions.

As always, should you have any questions or concerns regarding your tax situation please feel free to call.

This newsletter provides business, financial, and tax information to clients and friends of our firm. This general information should not be acted upon without first determining its application to your specific situation. For further details on any article, please contact us.