Year-End Tax Planning
What to Consider Post-Election

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Year-end tax planning has an added layer of complexity in 2020—weighing the known vs. the unknown. Do you take certain actions before December 31 to "lock in" under current tax laws? Or do you wait for the results of the run-off Senate races in January? (If Republicans retain control of the Senate, President-elect Biden may have difficulty enacting many of his proposed tax policies.)

There is no right or wrong answer. Your choice will ultimately depend on many factors particular to your tax situation, including your anticipated income and expenses for 2021, your outlook for the coming year, and your goals. It's also not an all or none decision. You might decide to take certain steps now and wait on others.

To help you with your year-end tax planning, we've outlined a few key areas you may want to focus on. We encourage you to work closely with your Cerity Partners advisor to gain a deeper understanding of what the 2021 political landscape could mean for your financial situation. They can simulate different scenarios based on your unique circumstances to show the potential impact on your current and future tax liabilities.

Individual Income Tax Rates

The current top marginal tax rate is 37% for individuals earning more than $523,600 in 2021 ($628,300 married filing jointly). On the campaign trail, President-elect Biden discussed raising the top rate to 39.6% for anyone earning more than $400,000.

Planning Considerations

If you think your tax rate may go up in 2021, look for ways to accelerate your income (receive in 2020 instead of 2021) to reduce your taxable income for the coming year. For example, can your bonus be paid by December 31? Can you receive January royalties or rental income in December?

Self-employed business owners may have other avenues to accelerate their income and expenses. Additionally, if you are an employee, check to see if your employer offers a nonqualified deferred compensation plan and if you're eligible to participate. Deferring income can help offset any potential increase in your tax rate.

Capital Gains Tax

The proposed 39.6% rate would also apply to capital gains and qualified dividends for individuals with more than $1 million in income. Currently, the maximum tax rate for capital gains is 20%.

Planning Considerations

Do you have any appreciated assets that you've been contemplating selling? Does it make sense to sell now, so you pay the capital gains tax in 2020? Do you have any carryover losses that would help offset the capital gains?

Estate and Gift Taxes

The lifetime estate-tax exemption is currently $11.58 million per person, and there's a step-up in basis to fair market value of appreciated property at death. President-elect Biden has proposed lowering the lifetime exemption to $3.5 million - $5 million per person and eliminating the step-up in basis. It's worth noting the lifetime exemption is set to drop back to approximately $5 million (2017 level) at the end of 2025 if there are no tax law changes before then.

Planning Considerations

You can implement several planning strategies to reduce your taxable estate and take advantage of the more generous lifetime exemption, such as making gifts to certain types of trusts, making outright gifts to your loved ones, or creating Grantor Retained Annuity Trusts (GRATS). The IRS has stated it won't "claw back" any of the exemption if you make a gift now, and the exemption amount drops in the future. For example, suppose an individual makes an $11.58 million gift in 2020 and dies in 2026. In that case, the exclusion used in calculating the unified gift and estate tax in 2026 would be $11.58 million, not $5 million, adjusted for inflation.

Charitable Deductions

The high standard deduction limit ($12,400 for 2020/$12,550 for 2021) and the $10,000 deduction limit for state and local taxes (SALT) have made claiming itemized deductions more challenging. As a result, many people have begun to "bunch" their charitable donations (aggregate multiple years of gifts into one year) to maximize their charitable deduction. But when should you bunch—2020, 2021, or not at all?

Planning Considerations

If you decide to accelerate your income, you may also want to "front load" your Donor Advised Fund or bunch your charitable gifts this year to help offset your higher taxable income. If you don't accelerate and think your tax rate will be higher in 2021, you might hold off on your donations until next year to boost your deductions. Note: President-elect Biden has discussed limiting itemized deductions to 28% of adjusted gross income for individuals earning more than $400,000.

Depending on your gifting philosophy, you might also consider establishing a foundation, a charitable lead annuity trust (CLAT), or charitable remainder unitrust (CRUT). Perhaps the most important factor that will influence your decision is how much you can afford to give in any one year.

Retirement Planning

Deferring income is another strategy that can help you effectively navigate current tax laws and any potential changes. It pushes some of your tax liabilities down the road, giving you more time to plan.

Planning Considerations

Are you contributing the maximum amount to your employer's 401(k) plan and your IRA, including catch-up contributions if eligible? If not, consider increasing your contributions from both your salary and any bonus. Do you have equity compensation that you can defer receiving? Business owners might also consider establishing a deferred compensation plan for their key employees.

Nothing is Certain

At first blush, it may seem obvious that you want to act now before President-elect Biden takes office. But taxpayers need to exercise caution and not make hasty decisions. Proposed policies are just that—proposals. There is no guarantee that any of them will become law. And if enacted, they could be in a modified form. You should look at all possible scenarios and evaluate which one aligns best with your goals and circumstances, and will help move your financial life forward.

We're Here to Help

We recognize this information is a lot to absorb, especially considering everything else that is going on. Our in-house tax and planning professionals have extensive knowledge of tax laws and advanced-planning strategies. Contact us to discuss how we can help you reduce your 2020 tax liabilities and beyond.

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