

January 2, 2024 – Wealth Planning Commentary

Tax Resolutions Start Now

Start off the new year with some simple tax management items to make the filing process a little easier, minimize income taxes, and avoid penalties.

First, a reminder that Q4 2023 estimated tax payments are due by Tuesday, January 16th. We recommend setting aside cash soon to avoid missing this deadline. Due to rising interest rates, penalties are 8% annually for those who underpay.

For the 2024 tax year, estimated tax payments are due on April 15th, June 17th, September 16th, and January 15th (2025). If most income is from earned wages and the appropriate taxes are withheld, there's likely no need to pay estimated taxes. However, business owners and those with investment income, in addition to salary, should contact their accountant for instructions on paying estimated taxes.

A simple way to avoid underpayment penalties is to follow the safe harbor rules. Safe harbor payments for a taxpayer whose adjusted gross income is above \$150,000 comprise 110 percent of the previous year's tax payments. Safe harbor payments for a taxpayer whose adjusted gross income is lower than \$150,000 equate to 100 percent of the previous year's taxes. Using the safe harbor method to pay estimated taxes ensures that you will avoid penalties, regardless of how much tax is owed upon filing a return. If you expect that 2024 income will be significantly lower than last year's, the required estimated payments are likely lower than the safe harbor amount. Consider working with your accountant to calculate a more precise tax payment to overpaying; this will increase cash flow.

Many have wisely invested in money market funds to take advantage of higher interest rates, but it's important to understand the tax implications. Some money market funds are invested in holdings that are taxable at the state level. States do not tax most income from federal debt, including treasuries, savings bonds, and bonds issued by certain agencies. However, income from treasury repurchase agreements ("repos") is subject to state income tax. Repos are commonly held in money market funds and certain investors may want to steer clear of them, especially if they reside in a high-income tax states such as New York or California.

Those who expect to have a low-income year should take advantage of it. These opportunities arise when taxpayers are in between jobs, taking a sabbatical, in school, or retired. A low-income year is often an ideal time to perform a Roth conversion or contribute directly to a Roth IRA if there is sufficient earned income. Reduced income presents the opportunity to realize long-term capital gains at lower rates. Lucky folks may even fall in the 0% bracket. Former high-income earners who paid a 20% rate on capital gains in the past may be in the 15% capital gains bracket now; that's a 25% reduction in tax rates!

Renovating this year? Taxpayers who are in the process of upgrading their homes should document all home improvements and share them with their accountant. Costs can be added to the purchase price to reduce the amount of taxable gain when a home is sold. Not all renovations increase cost basis, and an accountant can advise on which costs are eligible. There's also the home sale gain exclusion, which reduces the gain by \$500,000 for married couples and half that for individuals. To qualify for the exclusion, the home needs to be the taxpayers' primary residence, and the taxpayers must have lived there for two of the past five years. Unfortunately, this exclusion is not indexed to inflation.

Some over the age of 70.5 may have performed Qualified Charitable Distributions (QCDs) last year. QCDs are distributions that are made from pre-tax accounts and sent directly to charity. They can reduce reportable income and may lower social security taxes and Medicare premiums. It's important to understand that QCDs are not the same thing as taking an RMD and the proceeds must be sent directly from an IRA to the charity.

We recommend notifying your accountant because the tax statements generated by the custodian do not explicitly identify QCDs and they can be easily missed.

Please reach out to your Wealth Manager with questions about income tax for this year.

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