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TAX ADVANTAGE

Six Ways to Save on Taxes This Year

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Throughout 2021, clients have expressed uncertainty and anxiety regarding possible changes to rules governing federal income and estate taxes. While this anxiety is typical with a transition of power in Washington, we believe in planning according to the rules that exist, not those that may exist. Regardless of pending legislation, there are several tax planning opportunities you may wish to discuss with your tax advisor.

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Compare Itemized Deduction and Standard Deduction

Each year, you may deduct the larger of your itemized deductions (taxes, mortgage interest, charitable contributions, etc.) or the appropriate standard deduction based on your age and filing status. If the total of your itemized deductions is close to the standard deduction amount, you may consider bunching itemized deductions into one year and then taking the standard deduction the next year. One way of doing this is to make your charitable contributions in the years that you plan to itemize rather than giving equally each year.

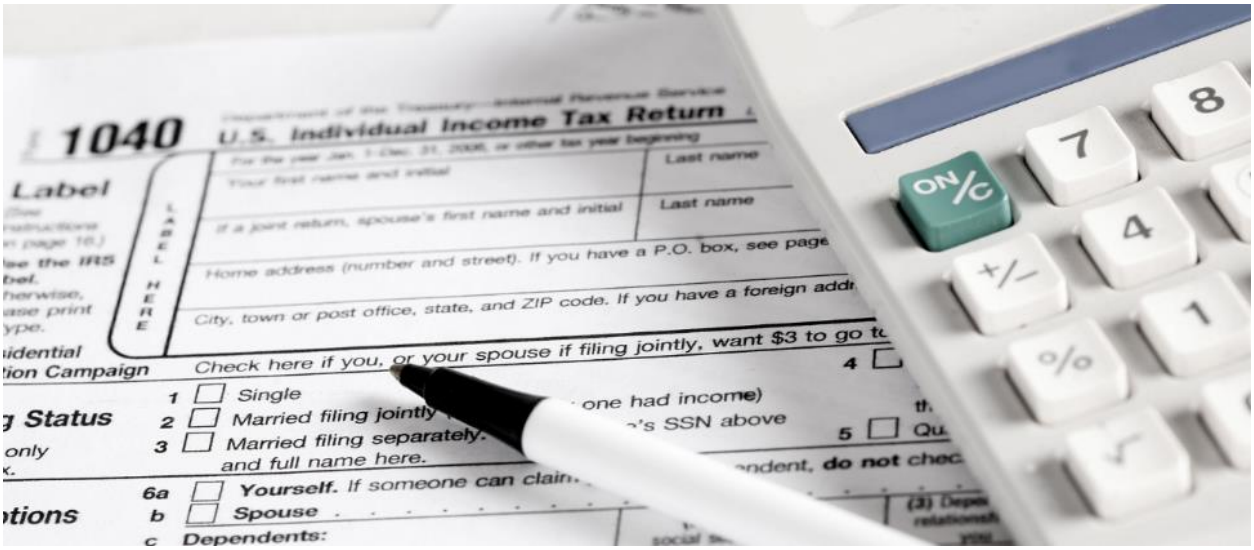
Give Strategically to Charity

For taxpayers who itemize their deductions, there may be an advantage to donating appreciated stock to charity. The value of the donation for the tax deduction is based on the fair market value of the donated shares. For stocks with a low tax basis, this technique allows the taxpayer to not only have the advantage of a larger deduction but also to avoid capital gains tax.

Taxpayers may also want to consider making donations to a donor advised fund. This technique allows you to contribute cash or appreciated securities to a charitable fund and receive a current year tax deduction for the donation. The transfer to the donor advised fund is an irrevocable donation for charitable purposes; you as the donor may direct the fund's holdings to be transferred to qualified charities of your choice, either in the current year or in future years.

For example, a taxpayer who would normally give $20,000 each year may not have enough additional deductions to benefit from the charitable gifts and would instead claim the standard deduction each year. However, if that same taxpayer donated $100,000 to a donor advised fund in year one, and then granted $20,000 of that fund for each of the next five years, they may not only be able to reduce their taxable income by $100,000 in year one, but in years two through five, they would also receive the benefit of the standard deduction. Plus, donor advised funds can be invested and grow without tax impact, which may extend the funds even further than the five-year period in this example.

If you have an IRA and are taking Required Minimum Distributions (RMDs), you may want to consider making a charitable donation directly from your IRA. This technique, called a Qualified Charitable Distribution (QCD), allows for all or a portion of your RMD (up to $100,000) to be transferred directly to a qualified charity. Rather than reporting the income from the IRA withdrawal and a subsequent deduction for a contribution to charity, the QCD is excluded from your income all together. In addition to the income tax benefit, you also reduce your modified adjusted gross income used for determining Medicare premiums.



Make Your Retirement Contributions

Every year, you should think about what retirement contributions you may be eligible to make. Take advantage of deferrals offered through your employer's 401(k) plan. If you are self-employed, consider whether an IRA, SEP IRA, or individual 401(k) is an option for your retirement funding. You may also be eligible to make contributions to an IRA or Roth IRA.

Take Advantage of Low Tax Brackets

It is always a good idea to review your expected tax bracket and think about tax planning opportunities. If you are expecting to be in a lower tax bracket in the current year, you might consider taking an IRA distribution or converting funds from your traditional IRA to a Roth IRA.

You may also want to realize capital gains on appreciated securities in a low-income year to benefit from a lower rate or in a year when you are not subject to the Net Investment Income Tax. Conversely, if you hold securities that have declined in value, you may want to realize those losses, which can be carried forward and used to offset current or future capital gains and up to $3,000 of ordinary income annually.

Max Out Your Gifts

You and your spouse are each allowed to gift up to $15,000 per recipient annually, without using any of your lifetime gift and estate exemption. In addition to the $15,000 cap, you may also make health care and education payments directly to the provider. According to a recent IRS announcement, in 2022, the gift limit will rise to $16,000 per donor.

Keep Up with State Tax Regulations

Here in Colorado, several changes in state tax rules are going into effect. Careful planning now may allow you to take advantage of these new rules or at least limit your exposure to their effects. Among the changes Colorado has recently enacted:

- Starting in 2022, high income taxpayers (those with federal adjusted gross income over $400,000) will be subject to a cap on itemized deductions of $30,000 for single filers and $60,000 for married filers. If you will be subject to this limitation, you might consider accelerating charitable contributions or other itemized deductions into tax year 2021 to avoid the impact in 2022.
- High income taxpayers (in this instance, defined by federal adjusted gross income of $500,000 for single filers and $1,000,000 for married filers) will be required to add back the Qualified Business Income Deduction taken on their federal tax return in calculating their Colorado taxable income.
- Starting in 2022, Colorado will limit the qualified tuition program subtraction to $20,000 per taxpayer per beneficiary single filers and $30,000 per taxpayer per beneficiary for married filers.

The Bottom Line

Consult with your tax professional if you think the above opportunities or others may apply to you. For GHPIA clients who would like more information, our Financial Concierge team can help coordinate a discussion with your tax professional.

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