THE ADAMS GROUP, LLC
CERTIFIED PUBLIC ACCOUNTANTS

"Last-minute" year-end 2018 tax-saving moves for individuals

Although there are only about five weeks left to go before the year ends, it's not too late to implement some planning moves that can improve a client's tax situation for 2018 and beyond. This *Practice Alert* reviews some actions that clients can take before Dec. 31 to improve their overall tax picture.

Make HSA contributions. Under Code Sec. 223(b)(8)(A) , a calendar year taxpayer who is an eligible individual under the health savings account (HSA) rules for December 2018 is treated as having been an eligible individual for the entire year. Thus, an individual who first became eligible on, for example, Dec. 1, 2018, may then make a full year's deductible-above-the-line contribution for 2018. If the individual makes that maximum contribution, he or she gets a deduction of $3,450 for individual coverage and $6,900 for family coverage (those age 55 or older also get an additional $1,000 catch-up amount).

Nail down losses on stock while substantially preserving one's investment position. A taxpayer may have experienced paper losses on stock in a particular company or industry in which he wants to keep an investment. The taxpayer may be able to realize his or her losses on the shares for tax purposes and still retain the same, or approximately the same, investment position. This can be accomplished by selling the shares and buying other shares in the same company or another company in the same industry to replace them, or by selling the original holding then buying back the same securities at least 31 days later.

Apply a bunching strategy to deductible contributions and/or payments of medical expenses. Beginning in 2018, many taxpayers who claimed itemized deductions in prior years will no longer be able to do so. That's because the standard deduction has been increased and many itemized deductions have been cut back or abolished. A bunching strategy can help taxpayers get around the new reality-namely accelerating or deferring discretionary medical expenses and/or charitable contributions into the year where they will do some tax good. For example, a taxpayer who expects to itemize deductions in 2018 but not 2019, and usually contributes a total of $1,500 to charities each year, should consider making a total of $3,000 of charitable contributions before the end of 2018 (and skipping charitable contributions in 2019).

Solve an underpayment of estimated tax problem. Employees may discover that their prepayments of tax for 2018 have been too small because, for example, their estimate of income or deductions was off and they are underwithheld, or they failed to make estimated tax payments for unanticipated income, such as gains from sales of stock. Or they may be facing a penalty for underpayment of estimated tax because of the additional 0.9% Medicare tax and/or the 3.8% surtax on unearned income. To ward off or reduce an estimated tax underpayment penalty, employees can ask their employers to increase withholding for their last paycheck or paychecks to make up or reduce the deficiency. Employees can file a new Form W-4 or simply request that the employer withhold a flat amount of additional income tax.

Increasing the final estimated tax payment for 2018 (due on Jan. 15, 2019) can cut or eliminate the penalty for a final-quarter underpayment only. It doesn't help with underpayments for preceding quarters. By contrast, tax withheld on wages can wipe out or reduce underpayments for previous quarters because, as a general rule, an equal part of the total withholding during the year is treated as having been paid on each quarterly estimated payment date.

Retirement plan distribution. An individual can take an eligible rollover distribution from a qualified retirement plan before the end of 2018 if he or she is facing a penalty for underpayment of estimated tax and the increased withholding option described above is unavailable or won't sufficiently address the problem. Income tax will be withheld from the distribution at a 20% rate and will be applied toward the taxes owed for 2018. The individual can then timely roll over the gross amount of the distribution, as increased by the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2018, but the withheld tax will be applied pro rata over the full 2018 tax year to reduce previous underpayments of estimated tax.

Be sure to take required minimum distributions (RMDs). Taxpayers who have reached age 70-½ should be sure to take their 2018 RMD from their IRAs or 401(k) plans (or other employer-sponsored retired plans). Failure to take a required withdrawal can result in a penalty of 50% of the amount of the RMD not withdrawn. Those who turned age 70-½ in 2018 can delay the first required distribution to 2019. However, taxpayers who take the deferral route will have to take a double distribution in 2019-the amount required for 2018 plus the amount required for 2018. This strategy could make sense if the taxpayer will be subject to a lower tax rate next year.

Use IRAs to make charitable gifts. Taxpayers who have reached age 70-½, own IRAs, and are thinking of making a charitable gift should consider arranging for the gift to be made by way of a qualified charitable contribution, or QCD-a direct transfer from the IRA trustee to the charitable organization. Such a transfer (not to exceed $100,000) will neither be included in gross income nor allowed as a deduction on the taxpayer's return. But, since such a distribution is not includible in gross income, it will not increase AGI for purposes of the phaseout of any deduction, exclusion, or tax credit that is limited or lost completely when AGI reaches certain specified level.

A qualified charitable contribution before year end is a particularly good idea for retired taxpayers who don't need all of their as-yet undistributed RMD for living expenses. That's because a charitable contribution distribution reduces the amount of the RMD that must be withdrawn, resulting in tax savings.

Wrap up a divorce. Alimony payments made under a divorce or separation agreement that is executed before Jan. 1, 2019, are deductible by the payor and included in the income of the payee. But if made under a divorce or separation agreement executed after Dec. 31, 2018, the payor can no longer deduct the alimony payments and the payee doesn't include them in income.

Where the payor of alimony is in a higher marginal income tax bracket than the payee, it is beneficial, for the divorcing spouses as a whole, for the alimony to be deductible to the payor and taxable to the payee. And, that benefit can be split between the two spouses by having the payor pay more alimony than the payor otherwise would pay if the alimony were not deductible to the payor. Thus, in most cases, couples in the midst of a divorce involving alimony payments should finalize that agreement by Dec. 31, 2018.

Make year-end gifts. A person can give any other person up to $15,000 for 2018 without incurring any gift tax. The annual exclusion amount increases to $30,000 per donee if the donor's spouse consents to gift-splitting. Anyone who expects eventually to have estate tax liability and who can afford to make gifts to family members should do so. Besides avoiding transfer tax, annual exclusion gifts take future appreciation in the value of the gift property out of the donor's estate, and shift the income tax obligation on the property's earnings to the donee who may be in a lower tax bracket (if not subject to the kiddie tax).

A gift by check to a noncharitable donee is considered to be a completed gift for gift and estate tax purposes on the earlier of:

1. the date on which the donor has so parted with dominion and control under local law so as to leave the donor with no power to change its disposition, or
2. the date on which the donee deposits the check (or cashes it against available funds of the donee) or presents the check for payment, if it is established that:

    . . . the check was paid by the drawee bank when first presented to the drawee bank for payment;

. . . the donor intended to make a gift;

. . . the donor was alive when the check was paid by the drawee bank;

. . . delivery of the check by the donor was unconditional; and

. . . the check was deposited, cashed, or presented in the calendar year for which completed gift treatment is sought and within a reasonable time of issuance.

Thus, for example, a $15,000 gift check given to and deposited by a grandson on Dec. 31, 2018 is treated as a completed gift for 2018 even though the check doesn't clear until 2019 (assuming the donor is still alive when the check is paid by the drawee bank).