PNC CENTER FOR FINANCIAL INSIGHT

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Nine Year-End Tax and Financial Planning Ideas

There's still time to address year-end tax and financial planning. Here are nine possible tax-saving actions you can address now.

This article includes items for you to consider with your tax, legal, and accounting advisors. PNC does not provide legal, tax, or accounting advice unless, with respect to tax advice, PNC Bank has entered into a written tax services agreement.

Family happens, business happens, life happens. We recognize sometimes you don't get to your financial planning as early as you would have liked. The good news is, it's not too late to take some action. Here we provide a quick review of a few valuable income tax and estate planning strategies you might still use before year end.

As this article went to press, Congress and the President are engaged in negotiating changes to the U.S. tax code that could, if enacted, affect the efficacy of any one or more of the tactics presented in this article. Consult with your advisors to guide you on the most up-to-date tax code status and how it affects planning decisions.

Idea 1: Explore Tax-Loss Harvesting

The stock market has generally experienced strong gains this year, resulting in new all-time highs for the Dow Jones Industrial Average and the S&P 500® and significant increases in many investment holdings. Still, many individuals also have holdings that have declined in value and have the opportunity to take advantage of tax-loss harvesting.

Tax-loss harvesting means deliberately recognizing a capital loss by selling assets currently worth less than you paid for them. The harvested losses can then be used to offset capital gains realized on other assets. You may have already recognized capital gains this year, or perhaps will do so before year end.

- ⇨ *Planning Point*—Generally, you should consider recognizing capital losses to the extent of your capital gains plus $3,000. Why? Because you can offset all of your capital gains and create a loss to offset up to $3,000 of current ordinary income, or the loss can be carried forward indefinitely to be used in future tax years.[1]
- ⇨ *Planning Point*—After a sale to recognize capital losses, taxpayers must wait 31 days to acquire the same or substantially identical security. This is known as the "wash sale rule."[2]

Idea 2: Consider Paying Taxes Prior to Year End

In some cases, paying your state and local income taxes or real estate taxes before December 31 could be beneficial. Additionally, it might make sense to accelerate deductible

[1] I.R.C. § 1211(b)(1).

[2] I.R.C. § 1091(1)(a).

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expenses into this year if you had been looking at doing so in early 2018. Talk to your tax advisor about your potential exposure to the alternative minimum tax before taking any action.

Idea 3: Weigh Giving to Charity before December 31

If there are charitable contributions you are considering making early in 2018, you may determine that doing so before year end may be advantageous as well.

⇨ *Planning Point*—If the idea of making a charitable contribution prior to the end of the tax year is appealing, but you would like more time to make a decision on which charitable missions to support, consider making your charitable contribution to a donor-advised fund. This will allow you to receive an income tax deduction in 2017 while delaying your decision on which charitable causes to support.[3]

⇨ *Planning Point*—There is often a time lag between when a gift to charity is made and when the charity sends an acknowledgment thank you. When making year-end gifts, it is important to verify that the charity will supply a written acknowledgement showing receipt of the gift in 2017. This is necessary to claim a 2017 income tax deduction for any single contribution of $250 or more.[4]

Idea 4: Examine Discretionary Trust Distributions

Many taxpayers are unaware that some trusts that accumulate income pay top-rate income taxes much sooner than individuals.

A taxable trust will reach the top rate of 39.6% if it retains more than $12,500 of accumulated income in 2017.[5] In contrast, the 39.6% rate applies to single filers with more than $418,400 in income and to married couples filing jointly with more than $470,700.

Like you, some taxable trusts are also potentially subject to the 3.8% net investment income tax (NIIT), depending on the level and source of the accumulated income. But a trust subject to the NIIT will pay it on all accumulated income greater than $12,500.[6] The NIIT is encountered at $200,000 for single filers and

Nine Tax-Saving Ideas

- Explore tax-loss harvesting.
- Consider paying some taxes before year end.
- Weigh making charitable contributions before year end.
- Examine discretionary trust distributions.
- Remember to take required minimum distributions.
- Mitigate net investment income tax/Medicare surtax.
- Look at gifting appreciated securities.
- Consider making gifts that qualify for the annual exclusion.
- Consider gifts in trust rather than outright gifts.

[3] Refer to the articles, “Charitable Giving Strategies” and “Donor Advised Funds,” produced by the PNC Center for Financial Insight, for additional details.

[4] I.R.C. § 170(f)(8).

[5] I.R.C. § 1(e)(2).

[6] I.R.C. § 1411(a)(2).

$250,000 for married taxpayers filing jointly.[7]

Nontax considerations may outweigh these options, but the tax savings can be significant.

⇨ *Planning Point*—If the trust permits, the trustee might consider making discretionary distributions of income to beneficiaries at the end of 2017, especially if the trust income would be subject to the NIIT. Such a distribution might be taxed at the beneficiary's lower rate and potentially not be subject to the NIIT at all.

Idea 5: Remember Required Minimum Distributions

Are you 70 ½ or older? Did you remember to take your required minimum distribution (RMD) from your retirement accounts? If you have not and do not take action now, you could be subject to an onerous excise tax.[8] The Internal Revenue Code and regulations require retirees to begin taking RMDs by April 1 of the year after the year in which they attain age 70 ½; thereafter, the RMD must be taken each year by December 31. You can take more than the required amount, but the minimum must always be taken. If you fail to take the minimum you could suffer a steep 50% penalty on the amount that should have been withdrawn.

⇨ *Planning Point*—You can have taxes withheld from your RMD. Taking a distribution and having some or most of it withheld for taxes may be beneficial in certain circumstances.

⇨ *Planning Point*—For taxpayers who are charitably inclined and have an individual retirement account (IRA), a valuable planning tool called the qualified charitable distribution was recently made permanent by Congress. It allows a taxpayer to have their IRA send up to $100,000 of their RMD directly to a qualified charity.[9] The gift to charity will count as the taxpayer's RMD for the year, but the taxpayer does not include the distribution as income. So if you use this feature, you will not receive a charitable deduction for the amount contributed. However, by making the distribution directly to the charity, you do not recognize the income, which produces a favorable tax result alongside the benefit to the organization you choose for the gift.

Idea 6: Four Strategies to Mitigate NIIT/Medicare Surtax

The 3.8% Net Investment Income Tax and Medicare surtax of 0.9% on wages apply to taxpayers with $250,000 of adjusted gross income (AGI) for married couples and $200,000 for single taxpayers.[10] Here are four strategies to lessen AGI:

- the qualified charitable distribution (see Idea 5);
- tax-loss harvesting to offset capital gains (see Idea 1);
- postpone the sale of investments that would generate large capital gains as long as this does not conflict with your overall investment strategy and goals; and
- contribute the maximum amounts to retirement accounts, including

[7] I.R.C. § 1411(b)(1).

[8] Refer to the article, "Required Minimum Distributions," produced by the PNC Center for Financial Insight, for additional details.

[9] I.R.C. § 408(d)(8).

[10] I.R.C. §§ 1411(b)(1) and 1401(b)(2).

- contributions to a Simplified Employee Pension plan (20% of net self-employment income, up to $54,000) and 401(k) contributions ($18,000 for 2017 and $24,000 for age 50 or over).[11] Also, increase contributions to health savings accounts.

If you do happen to be over the $250,000 AGI threshold, remember that investment expenses and state taxes that are derived from investment income are deductions against the net investment income tax.[12] Even if you do not receive a benefit because of the alternative minimum tax, you may want to make these payments before the end of the year to save on the net investment income tax.

Your trust might be in a higher tax bracket than you are. Ask the trustee if a distribution this year might be advantageous.

Idea 7: Look at Gifting Appreciated Securities

In lieu of cash, consider gifting appreciated securities to a qualified charity. This gives you the ability to take a deduction for the full fair-market value of long-term securities, those held for more than one year, without incurring the capital gains income tax. Remember that the deduction for gifting appreciated securities to a public charity is capped at 30% of the donor's adjusted gross income. Please see your professional tax advisor for deduction limitation details on gifts of various other types of assets to public charities and to other types of charitable entities.

Unlike appreciated securities, a charitable donation of investments that have declined in value is not as advantageous. Rather, you should consider selling the assets first and donating the proceeds. Why? Selling a depreciated asset generates a capital loss (see tax-loss harvesting, Idea 1) that can be used to offset capital gains, and the proceeds from the sale can then be donated to obtain a charitable deduction.

Idea 8: Consider Gifts that Qualify for Annual Exclusion

The $14,000 annual gift tax exclusion is entirely lost if not used by December 31. For those who possess a taxable estate, annual exclusion gifts can be a powerful tax reduction tool. Each taxpayer can make a gift of $14,000 or less to anyone they choose—and to as many people as they choose without paying gift taxes or using any of the lifetime exemption amount.[13] This means a married couple can make gifts of up to $28,000 per year per person, and to as many people as they want, without incurring any gift tax.

⇨ *Planning Point*—One unique option to consider for maximizing the annual gift tax exclusion prior to the end of the year would be to make a lump sum gift to a 529 college savings plan and take advantage of the special five-year acceleration provision.[14] This provision allows you to make a gift up to $140,000 for joint gifts, and avoid federal gift tax by making a special election to treat the gift as if it were made evenly over a five-year period.

Idea 9: Would You Prefer a Gift in Trust?

For any number of reasons, some people would rather make gifts that have some guardrails around

[11] I.R.C. § 414(v).

[12] I.R.C. § 1411(c)(1).

[13] I.R.C. § 2010–unified credit against estate tax; I.R.C. § 2505–unified credit against gift tax.

[14] I.R.C. § 529(c)(2)(B).

them. In order for a gift to qualify for the $14,000 annual exclusion, or $28,000 if your spouse makes a gift to the same person, it must satisfy the present interest requirement.[15] That is, the person receiving the gift must have an unrestricted right to the immediate use, possession, or enjoyment of the property. Transfers in trust are, by design, used to restrict access to property and generally do not qualify as a present interest gift. But there is one path that gets it done, a Crummey trust. Annual exclusion gifts in trust satisfy the present interest requirement when the donee is given notice of a limited window to withdraw the gifted amount from the trust. The right typically lapses after 30 days, after which the donee can no longer access the funds.

⇨ *Planning Point*—While we do not recommend delaying annual exclusion gifts, a transfer can be made on December 31, 2017, and still qualify for the annual exclusion in tax year 2017 even if the donee is not notified of the transfer until 2018. This may be useful if you need to create a brand new trust to receive your gift.

[15] I.R.C. § 2503(b)(1).

For more information, please contact your PNC advisor.

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