

YEAR-END TAX STRATEGIES FROM "THE POWER OF THE DUAL VIEW"

This Tax Newsletter lists some of the "low hanging fruit" tax strategies to consider for the year-end. The 50 *Tax Tips!* herein include some of the annual tried and true and they work the five step tax reduction formula, which is: (1) Exclude from taxation the income and gains that you can; (2) Defer the income that you must report; (3) Reduce the reported income with deductions; (4) Pay taxes on the rest; and (5) Pay a few weeks before the taxes are due to avoid penalties and interest. We first start with two IRS cases to help implement the five step strategy.

I. IRS CASES – USE YOUR COMPUTER

\* In *Patitz vs. [IRS]*, the Tax Court denied moderate business deductions when a couple claimed their documentation was lost in a hurricane. However, their automobile expenses stored on an *electronic* log were allowed. **Tax Tip!** With the ease of electronically saving and storing documents, use your computer, such as its pdf capabilities, to guard your tax records against physical destruction.

\* In the *Estate of DeMuth vs. [IRS]*, a few days prior to the taxpayer passing away, his POA mailed 11 checks to friends and relatives in an attempt to utilize the annual gift tax exclusion. But, only one check cleared prior to the taxpayer passing. The Court held the other 10 checks cashed after the taxpayer passed were *incomplete* gifts. The adverse ruling increased Mr. DeMuth's estate's taxes by \$179,000! **Tax Tip!** Fund gifts with online payments to immediately "complete the gift."

II. BUSINESS TAX TIPS

✓ Tax Liability Insurance (TLI) - An emerging tax product is Tax Liability Insurance (TLI). In certain circumstances TLI will pay the extra taxes to the IRS or a state if they successfully challenge the original filing. For example, when a company is sold, many times the Seller has to wait to receive some of its money until certain tax issues are resolved, including waiting years for the statute of limitations to expire. Instead of waiting for its money, a Seller can buy TLI to cover the possible future problem. TLI can also be used in lieu of relying on a law firm's opinion about a tax position. TLI is further an alternative to waiting for an IRS Private Letter Ruling (PLR). A PLR is a procedure asking the IRS for its position prior to completing a transaction. The request can take months though and the IRS might

decline to rule anyway. Similarly, TLI can also be used when a *possible* tax problem is discovered while a Purchaser is investigating a business.

✓ Business Credit Card: A cash basis business can charge its business credit card in late December to pay January 2023 business expenses to procure a 2022 deduction even though it does not make the credit card payment until 2023.

✓ Business Vehicles: December vehicle purchases usually will reduce taxable income. The maximum first year automobile depreciation for 2022 is \$19,200. For 2022 the larger SUVs (over 6,000 lbs.) and Trucks enjoy up to a 100% first year deduction! Its 80% next year.

✓ Employee Office Rents or Accountable Plan? Consider paying rent to an employee for the business use of their home. A better approach might be is for the employee to submit a reimbursement report for the allocable portion of the home operating expenses. Depending on the circumstances the allocable portion is around \$1,500 to \$5,000 annually and *reimbursements* are not subject to employment taxes, the business can deduct it, and the employee does not report it as income. Rents are different though.

✓ A Last Vestige of the Covid Deductions - §139 or Qualified Disaster Relief (QDR) Exclusions. An employee may exclude from taxable income certain payments or reimbursements received in relation to "personal, family, living, or funeral expenses" incurred as a result of Covid, including medical expenses or equipment and supplies for a remote office. Employers who make QDR payments can generally deduct these expenses and avoid payroll taxes on the non-compensation payments.

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✓ Bonus Depreciation is Changing: For 2022 Bonus Depreciation is 100% of the cost of most business personal (as opposed to real estate) tangible property. Bonus depreciation decreases to 80% starting in 2023. Thus, it might make sense for a business to make a 2022 purchase instead of a 2023 acquisition to take advantage of the 20% spread.

✓ Tax Planning with Depreciation: Usually, maximizing current depreciation deductions decrease taxes. But deferring depreciation deductions (DDD) can sometimes yield better tax results. DDD methods include: (a) electing out of bonus depreciation; (b) electing Sec. 179 expensing; (c) electing straight-line depreciation; or (d) taking advantage of certain longer tax life alternatives.

✓ Mileage Deduction v. Depreciation: Often it is better for a business to use the Mileage Per Diem Method of 58.5¢ per mile (January through June 2022) and 62.5¢ per mile (July through December 2022) instead of using depreciation plus operating expenses. Generally, lower priced vehicles with significant business miles yield a better tax result using the Mileage Deduction.

✓ Oklahoma Pass-Through Entity (PTE) Election: If your profitable Oklahoma PTE (S corporation or LLC partnership) has not elected to deduct its Oklahoma income taxes at the business level, consider it. Our tax preparation business checklist includes a due diligence provision that, in short asks, if the taxpayer has not made the election, "why not?" The election is due March 15, 2023, and it usually converts a non-deductible state income taxes into a deduction. For every \$100,000 of income, this deduction can save about \$1,250+ in taxes.

✓ Qualify for Oklahoma PTE Election: Yield a better tax result by converting certain sole proprietorships or rental operations to a flow-through entity such as a partnership or S-corporation. For example, consider adding a spouse as a partner of a sole proprietorship to create a PTE, or in some cases S-elect a single member LLC.

✓ Maximize the Oklahoma PTE Election: If your cash basis business has elected to pay its Oklahoma income taxes, calculate its 2022 estimated taxable income, and pay the taxes in December 2022 even if they are not due until January or April 2023.

✓ Restaurant Meals: Food and Beverages are 100% deductible for 2022 if purchased from a restaurant. Perhaps the owner attend and plan a business Christmas Party at a restaurant. The deduction will be curtailed back to 50% in 2023.

✓ Tax Basis: IRS is requiring more verification for tax basis. Make sure you have tax basis in your partnerships and S corporations to deduct any losses. Increasing your tax basis can be accomplished by several methods including loans, and capital investments. If you need help increasing your tax basis for your business, our office can assist you.

✓ Specified Service Businesses (SSB): For doctors, lawyers, accountants, consultants, etc. that own their practices as a business (not solely a W-2 employee), consider maximizing contributions to traditional IRAs, §401(k)s, and others pension plans to help qualify for the 20% business income deduction that can be and is limited for SSBs.

✓ Business Losses: You are not in business to generate losses, but they do happen. This is a list of possible business loss deductions:

- (1) Business Bad Debts
- (2) Casualty and Theft Losses
- (3) Capital Loss/Worthless Investments
- (4) Losses on Sales of Business Assets

Sometimes it can be difficult to ascertain what year a business or investment loss should be written off. The general rule is to deduct the loss in the earliest year possible.

✓ Pension Plans: Set up pension plans before year-end and fund in 2023. In many cases, if a plan is set up by December 31, you can contribute to the plan as late as October 15, 2023 for a 2022 tax deduction. A small employer can claim up to a \$5,000 credit for administration costs for pension plans.

✓ Pre-Paid Expenses & the 12 Month Rule: A cash basis business can typically deduct any amounts paid for a right or benefit that does not extend beyond 12 months after the date of the payment. Thus, a business can pre-pay expenses in December 2022 that are for 2023. For example, pre-paying rent, health insurance, etc. can yield sizable deductions.

✓ Leasing Vehicles & the 12 Month Rule: In December, make a one-time lump sum payment on a 36-month auto lease and deduct one-third of it in December under the 12-month rule.

### III. INDIVIDUAL TAX TIPS

✓ Increase December W-2 Withholdings: Avoid underpayment penalties by increasing your withholdings from your December paychecks.

✓ Employer Flexible Spending Accounts (FSAs): Increase the amount you set aside in your Health FSA account if you have set aside too little for the year. The 2022 maximum is \$2,850, and for 2023 it's \$3,050.

✓ Health Saving Accounts (HSAs): If you become eligible in December 2022 to make HSA contributions, you can contribute a full year's worth by the end of 2022. Nevertheless, this year's maximum is \$3,650 for self-only, and \$7,300 for family plan, and an additional \$1,000 if age 55 or over.

✓ Maximize Pension & IRA Contributions: Increase your retirement plan contributions to take the maximum write-offs. If applicable, take full advantage of employer matching. For 2022: (1) the IRA contribution limits are \$6,000 (\$6,500 for 2023) and \$1,000 more if age 50 or older; (2) the SIMPLE Plan limits are \$14,000 (\$15,500 for 2023) and \$3,000 extra (\$3,500 for 2023) for age 50 or over; and (3) the §401(k) contribution limit is \$20,500 (\$22,500 for 2023), and if age 50+ add an additional \$6,500 (\$7,500 for 2023).

✓ Sale of Loss Entities: Dispose of your interests in those flow-through entities in which you have "suspended" loss carryforwards.

✓ IRA Charity Distributions: At age 70 ½+, you can donate up to \$100,000 of your IRA and: (1) it is not included in your income, (2) it counts toward the RMD, and (3) although not deductible, it usually more advantageous than withdrawing and donating.

✓ Charitable Stock Donation: Consider gifting appreciated property, typically publicly traded stock, to a charitable organization for a deduction equal to its fair market value without reporting the gain.

✓ Achieving a Better Life Experience (ABLE) Accounts: This is a savings account for individuals with disabilities and their families. For 2022, taxpayers can contribute up to \$16,000. Earnings are not taxable, and distributions are tax-free if used to pay the beneficiary's qualified disability expenses.

✓ Single and Head of Household: If you are single and assist your parents financially, even if they have a separate home, make sure you meet the support level test to file head of household instead of single.

✓ Gift Tax Strategy: Make up to \$16,000 gift per done before the end of the year to take advantage of the annual gift tax exclusion. Sometimes the transfers may save taxes when a lower bracket family member reports the income the gift generates. The gift tax exclusion is \$17,000 starting next year.

✓ Lower College Tuition by 4.75%: Take advantage of the Oklahoma §529 plans now by contributing to it in December for a 2022 Oklahoma deduction, then use it for the January 2023 tuition invoice.

✓ §529 Plans – Higher Education Costs: Up to \$10,000 can be withdrawn from a §529 plan for tuition paid in connection with enrollment or attendance at a public, private, or religious elementary or secondary school.

✓ Oklahoma Homestead Exemption: Make sure you are getting your homestead real estate tax

reduction. In Tulsa County, check online at [assessor.tulsacounty.org/exemption/homestead](http://assessor.tulsacounty.org/exemption/homestead).

#### IV. INVESTMENT TAX TIPS

✓ Short-Term (ST) vs. Long-Term (LT) Capital Gains – The General Rules: Capital gains on property held one year or less are ST and are taxed as high as 50%. If held over a year it is LT and taxed about half as much. For taxpayers not in the highest tax brackets, the tax rate for LT capital gains can be 15% or as low as zero!

✓ Take some losses in December 2022? If you are a fortunate taxpayer with realized capital gains in 2022, and you have "loss stock positions," sell the losses in December to off-set the capital gains

✓ Crypto Currencies & Wash Sales: Loss positions with Virtual Currencies are good to use to off-set realized capital gains because the 30-day wash sale rules do not apply to Cryptos. If you sell "securities" (typically stocks), you must wait 30 days to buy it back if you want to utilize the loss.

✓ Defer the Sale: If you have a borderline holding period, consider holding the asset a little longer than a year to take advantage of the favorable LT capital gains rates.

✓ Avoid Fluctuations: Realizing net capital gains in 2022 and then suffering net capital losses in 2023 increases the probability of wasting deductions. Thus, a good tax strategy is to try to realize losses in years with gains or sell loss assets in year #1 and sell gain assets in year #2.

✓ Dividend Taxes: Most stock dividends are taxed at LT preferential rates. Thus, dividend paying stocks, and similar stocks held in mutual funds are tax advantageous investments.

✓ Oklahoma Capital Gain Exclusion: If you have appreciated Oklahoma real property or own stock, or LLC membership interests in companies that are located primarily in Oklahoma, the capital gain, under many circumstances, can be totally excluded from Oklahoma taxation.

✓ Gift Appreciated Stock: An excellent tax savings strategies can be for a parent to gift appreciated stock to their lower tax bracket adult child.

✓ Tax Strategy for Pension Plans & Personal Investments - Generally, if possible: (1) Hold capital appreciation stocks personally to take advantage of the lower capital gain rates, and (2) Hold bonds producing interest income in your 401(k) or traditional IRA; (3) typically investing stocks or bonds using a Roth IRA is preferable to a traditional 401(k) or IRA; and (4) utilizing a "Back Door Roth" is an excellent strategy for an otherwise disallowed Roth contribution.

#### V. ORGANIZE YOUR TAX DATA FOR LOWER TAXES & TAX PREPARATION COSTS

✓ Organized tax information allows us to concentrate more quickly on tax savings strategies.

✓ Organized tax documents also reduces the probability of getting caught in the IRS "abyss."

✓ Visit [Paulhburgess.com](http://Paulhburgess.com) for our 10 Tips for Small Business Accountings to complete your business accountings by January/early February time frame.

✓ Use an Excel spreadsheet to summarize your tax information, and update the spread sheet each year.

✓ Start with reviewing the prior year and start procuring the reoccurring tax documents in January.

✓ Have a file folder in January for your typical W-2s, Forms 1099, Schedules K-1, etc.

✓ Obtain payment proof of your estimated tax payment via online receipts or certified mail, return receipt.

✓ If you itemize your deductions, gather your Form 1098 (Home Mortgage Interest), Charitable Donations, State and Local Taxes, Gambling Losses, and sometimes Medical and Dental expenses.