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To Our Clients and Friends:

Another challenging year has just passed. While the COVID-19 crisis has lessened, international events have led to supply chain issues and inflationary prices. Since income may not rise at the same rate as expenses, saving on income taxes can help keep you in the black. There is still uncertainty over whether any pieces of President Biden's tax plan will be implemented. If legislation does occur, there could be higher tax rates for both individual and corporate taxpayers. The results of the midterm elections will most likely have an effect on whether this legislation moves forward. As always, we are monitoring these developments and will alert you as soon as any legislation is signed into law. For now, it's a good time to get a handle on what your 2022 income might look like so that, if legislation is passed, we will be able to project how it affects you.

Here are some ideas to think about over the summer.

Individual Income Tax Opportunities

Here are some strategies that may lower your individual income tax bill for 2022.

- *Consider Adjusting Your Tax Withholding or Estimated Payments*. If you owed taxes for 2021, you may want to revise your Form W-4. To help you do this, consider using the IRS's "Tax Withholding Estimator," available at **www.irs.gov/individuals/tax-withholding-estimator**. If you make estimated tax payments throughout the year (which is likely the case if you are self-employed, for example), we can take a closer look at your tax situation for 2022 to make sure you're not underpaying or overpaying.
- *Take Advantage of Lower Tax Rates on Investment Income*. Gains from the sale of an investment held for more than one year (as well as dividends on certain stocks) are generally taxed at preferential capital gains rates. Those rates are 0%, 15%, and 20% for most investments. The applicable rate depends on your taxable income. If your income is too high to benefit from the 0% or 15% rates, try gifting investments (like appreciated stock or mutual fund shares) to children, grandchildren, or other loved ones. If these individuals are in the 0% or 15% capital gains tax bracket when they later sell the investments, any gain will be taxed at the lower rates if you and your loved one owned the investments for more than one year. Dividends from any gifted stock also may qualify for the lower rate. However, beware of the "Kiddie Tax," which applies to all children under age 18 and most children age 18 or age 19–23 who are full-time students. It may limit your opportunity to take advantage of this strategy. Also, beware of a potential increase in both long-term capital gains rates and ordinary income tax rates heading into 2023.
- *Time Investment Gains and Losses*. As you evaluate investments held in your brokerage accounts, consider the tax impact of selling appreciated securities before the end of the year. President Biden has proposed a plan that would increase long-term capital gains rates to 39.6% for taxpayers making over $1 million. Combined with the Net Investment Income Tax (NIIT) of 3.8%, affected taxpayers could see a 43.4% marginal long-term capital gains rate, which is quite an increase from the current combined rate of 23.8%. Selling securities that have declined in value may need to wait until 2023 to offset the potential higher tax rate. Losses realized will offset any gains you may have realized. Your net capital loss is limited to $3,000 of ordinary income annually, but any excess carries over indefinitely.
- *Check Your Deduction Strategy*. Generally, it's best to itemize your deductions if your personal expenses, such as mortgage interest, charitable contributions, medical expenses, and taxes, exceed the standard deduction. For 2022, joint filers can enjoy a standard deduction of $25,900. The standard deduction for

heads of household is $19,400, and single taxpayers (including married taxpayers filing separately) can claim a standard deduction of $12,950. However, "bunching" your deductions may offer the best of both worlds. For example, you can pay two years' worth of property taxes in a single calendar year, or double up on charitable giving every other year. If that is enough to get over the standard deduction amount, you'll get a bigger deduction every other year, yet part with the same amount of cash.

- *Virtual Currency*. For federal tax purposes, virtual currency is treated as property, not currency. Basis in virtual currency is the Fair Market Value (FMV) of the currency on the date it is received. If you receive virtual currency as payment for services, it is considered taxable income and will be subject to both income and Social Security taxes. Also, using virtual currency to obtain cash or purchase goods is a recognizable transaction. If the FMV of property you receive for the virtual currency exceeds your adjusted basis in the currency, you will have a taxable gain. A loss will occur if the FMV is less than your basis. The character of the gain or loss depends on whether the virtual currency is considered your capital asset. Using the Highest-in, First-out (HIFO) accounting method, by which you specifically identify which units you are transferring in any transaction, can reduce your 2022 tax liability and defer the higher gain on lower basis units to a later tax year.
- *Reverse Mortgages*. Due to current inflation rates, some individuals are suffering from cash flow issues. If you are age 62 or older and have substantial equity in your residence, a reverse mortgage may be one way to meet current cash flow needs. A reverse mortgage allows you to receive loan proceeds over a certain period (by borrowing against equity in the home) while continuing to live in the house. While a reverse mortgage can help with cash flow issues, it does not allow a current tax deduction for the interest that accrues on the loan. However, starting in 2026, accrued interest may be deductible (subject to limitation) when the loan is repaid. The repayment (and tax deduction for mortgage interest) generally occurs when you are no longer using the home as your principal residence, you refinance the property, you sell the home, or the home becomes part of your estate.

Planning for Small Businesses

If you own a business, consider the following strategies to minimize your tax bill for 2022.

- *Section 179 Expense and Bonus Depreciation*. If your business plans to purchase new or used machinery or equipment prior to year end, you may be able to expense the entire cost in 2022. Under Section 179, taxpayers can elect to expense up to $1,080,000 of qualified purchases, subject to taxable income limitations. Alternatively, your business can take advantage of 100% first-year bonus depreciation. Unlike the Section 179 deduction, claiming 100% bonus depreciation is not limited to taxable income, although another limitation could apply. Many factors can influence this decision, including current and future tax rates. With the possibility of higher rates in 2023, the best choice may be to wait and see if you are going to be subject to a higher tax rate before you acquire assets, if it is feasible to hold off. Also, under current law, 100% bonus depreciation is scheduled to be reduced to 80% for property placed in service in 2023. If you're thinking of acquiring business property between now and the end of the year, we can help you navigate that decision.
- *Retirement Plan Contributions*. Setting up a qualified retirement plan for your business allows you to make deductible contributions for 2022 while allowing the earnings in the plan to build up without taxation until the funds are withdrawn. Selecting the best qualified retirement plan will depend on the facts and circumstances of your business, including your level of income and whether you have employees. Types of available plans include defined benefit, defined contribution, one-person 401(k), Simplified Employee Pension (SEP), and SIMPLE IRAs. Each type of plan has advantages and disadvantages that we will gladly discuss with you to determine which plan is the right fit for your business. In addition, you may be eligible for two tax credits related to establishing and operating a small business retirement plan.
- *Employing Family Members*. Employing family members can be a useful strategy to reduce overall tax liability. If the family member is a bona fide employee, the taxpayer can deduct the wages and benefits, including medical benefits, paid to the employee on Schedule C or F as a business expense, thus reducing the proprietor's self-employment tax liability. In addition, wages paid to your child under the age of 18 are

not subject to federal employment taxes, will be deductible at your marginal tax rate, are taxable at the child's marginal tax rate, and can be offset by up to $12,950 (your child's maximum standard deduction). However, your family member must be a bona fide employee, and basic business practices, such as keeping time reports, filing payroll returns, and basing pay on the actual work performed, should be followed.

- *Business Meal Expenses*. Normally, business meal expenses are limited to a deduction of 50% of the total costs. However, for 2022, food and beverages provided by a restaurant are allowed a 100% deduction. Taxpayers who use the per diem method may treat the entire meal portion of the per diem rate paid or incurred in 2022 as being attributable to food or beverages provided by a restaurant, making the meal per diem 100% deductible. As such, you may want to move any business meals originally planned for early 2023 into late 2022 in order to obtain the higher deduction.

If you have any questions please reach out to your tax professional for more information.

Sincerely,

Wicks Emmett LLP