Six tax-saving tips to consider by year-end

Key takeaways

- To help reduce taxable income, considering increasing your contributions to tax-deferred retirement accounts or a health savings account.

- Charitable giving can potentially be a great way to lower taxes, while also contributing to worthy causes. Consider such options as a Donor-Advised Fund or a Qualified Charitable Distribution.

- To reduce capital gains, consider a tax-loss harvesting strategy, which offsets realized taxable gains on your investments (capital gains) with realized losses (capital losses).

When it comes to taxes, the filing deadline of April 17, 2018, tends to get all the attention. But this year, December 29 may be more important. That's the deadline for many moves that could reduce what you owe—or increase what you get back—when you file your 2017 income tax return.

This year, planning for those deadlines may seem trickier than usual, as a debate plays out in Washington about the future of tax law. House Republicans released a proposed tax plan that offers the first detailed look at the most ambitious tax reform proposal since 1986. The plan calls for changes to income tax rates, estate taxes, deductions, and some retirement rules—and if even parts of the proposal become law it would be a significant event for investors.

"The New Tax Bill is sweeping, which means major changes for businesses and individuals," says Glenn Goldsmith, president and principle consultant Goldsmith & Goldsmith Management Company. “People should be cautious about making planning decisions based on a hearsay, and in general should not make consequential decisions based primarily on tax law."

“Regardless of the current ambiguity, you still have to pay taxes; but there may be ways to ease the pain. You have until the end of the year to implement some tried-and-true strategies, such as contributing to a 401(k) plan at work or donating to charity, but the clock is ticking on how effective those strategies can be. The longer you wait, the more difficult it may be to take full advantage of the potential tax savings.”

"Most tax strategies take time to be fully effective," Goldsmith notes. "You can't wait until December 31 and click a button. You need to get started as soon as possible." With that in mind, here are some possible year-end tax moves, combined with planning tips that could help you be more strategic about your taxes next year and beyond.

1. **Contribute to a tax-advantaged retirement plan or health savings account**

Pretax contributions to a traditional 401(k), 403(b), or similar workplace retirement plan could reduce your taxes by the amount of your total contribution for the year multiplied by your marginal tax rate. If you're in the 28% tax bracket, for example, you could save $280 in current-year federal taxes for every
$1,000 you contribute, up to the 2017 limit of $18,000. However, you have only until December 29, 2017, to make the contribution count for this year, so now is the time to contact your employer to bump up your contributions for this year. The maximum you can contribute to a 401(k) for 2017 is $18,000. If you're age 50 or older, you can contribute an extra $6,000, for a maximum contribution of $24,000.

**Plan ahead:** With the end of the year approaching, you may not be able to increase your 401(k) contributions sufficiently to maximize your tax savings. The best way to avoid having the same thing happen next year is to notify your employer now that you want to increase your automatic deferral percentage for 2018.

A traditional IRA and a Simplified Employee Pension (SEP) IRA offer potential tax breaks similar to those of a 401(k); however, you have until **April 17, 2018**, to make a contribution that applies to your 2017 tax return. The maximum IRA contribution for this year is $5,500 for eligible taxpayers under age 50, and $6,500 for those 50 and older. SEP contributions by self-employed individuals are limited to $54,000 or 25% of eligible income, whichever is less.

**Plan ahead:** If you expect to be in a higher bracket in retirement, you may want to consider whether converting all or a portion of a traditional IRA to a Roth IRA makes sense. Generally, you'll have to pay current-year tax on the converted amount. But if the conversion won't push you into a higher tax bracket, the potential benefit of tax-free withdrawals from a Roth IRA1 when you retire might make the one-time higher tax payment this year worth it. Contact your tax advisor regarding your individual situation.

Another option for reducing taxable income is a health savings account (HSA). An HSA has triple tax benefits. Your contributions are made with pretax dollars so you reduce your federally taxable income; earnings are federal and potentially state-tax free, as are withdrawals used to pay for HSA-qualified medical expenses. If you are enrolled in a high-deductible health plan (HDHP), see if you are contributing the max $3,400 for an individual and $6,750 for a family, plus an extra $1,000 if you are age 55 or older.

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**2. If you've reached age 70½, remember to take required minimum distributions**

The penalty for failure to take your required minimum distribution (RMD) from tax-deferred retirement accounts like a traditional IRA and 401(k) can be up to 50% of the shortfall. The deadline for taking your 2017 RMD is December 31, unless you turned 70½ this year, in which case you get a grace period until April 1 of next year to make your first withdrawal.

Keep in mind, however, that if you turned 70½ this year and wait until next year to take your 2017 RMD, you'll owe taxes on two RMDs, the one for 2017 and the one you need to take by the end of 2018—consider the effect this double RMD may have on your 2018 income taxes. Because December 31, 2017, falls on a Sunday, if you need to sell securities to raise cash for your RMD, plan to have the trades settled and RMD completed by Friday, December 29, 2017. This transaction will take at least a couple of days, so be sure to give yourself enough time.

Plan ahead: One way to ensure that you won’t miss an RMD is to instruct your retirement account administrator to process the withdrawal automatically each year. Fidelity will calculate your RMD, and you can choose to take your RMD in a lump sum or in installments throughout the year.

3. Donate to charity

Charitable giving can potentially be a great way to lower taxes, while also contributing to worthy causes. But for your contribution to have a meaningful effect on your taxes, make sure your itemized deductions exceed the standard deduction. For 2017, the standard deduction—the amount you can deduct if you decide not to itemize—is $6,350 for a single taxpayer, $9,350 for a head of household, and $12,700 for a married couple filing jointly or a surviving spouse. The upper limit of charitable deductions is 50% of your adjusted gross income (AGI).

(Note: the new tax reform calls for an increase in the standard deduction to $12,000 for a single taxpayer, $18,000 for single taxpayer with at least one qualifying child, and $24,000 for a married couple filing jointly or a surviving spouse. In addition, the tax reform would raise the upper limit of charitable deductions to 60% of your AGI for tax years after 2017.)

Remember to get a written receipt for every contribution you make worth $250 or more. Be sure to have a record of all contributions, regardless of their amount, in the form of a bank or credit card statement, or a receipt from the eligible organization. Handwritten notes or computer logs that you keep yourself are not acceptable.

Plan ahead: If you want to give to charity but your total itemized deductions are less than the standard deduction—or you expect your income to be higher next year—you might consider waiting until after January 1 to make your contribution. Bunching to 2 "annual" contributions into one year might be the better strategy for tax purposes.

4. Take advantage of a qualified charitable distribution

If you want to donate to charity and you're 70½ or older, you may want to look into a qualified charitable distribution (QCD). It's a direct transfer of funds from your IRA custodian and payable to a qualified charity, which counts toward your RMD for the year, up to $100,000. It's not included in your gross income and does not count against the limits on deductions for charitable contributions. These can be significant advantages for certain high-income earners, but the rules are complex—be sure to consult your tax advisor.

Plan ahead: If your choice for contributing to charity is between cashing in highly appreciated stock or a QCD, evaluate which one will result in the biggest tax break before you decide. Contact your tax advisor to discuss your individual financial situation.

5. Reduce capital gains with tax-loss harvesting
If you invest in stocks, bonds, or mutual funds in taxable accounts—a nonretirement brokerage account for instance—you may be able to reduce taxes on any realized investment gains and distributions from mutual funds. Tax-loss harvesting might sound complicated, but the principle is fairly simple: offset your realized taxable gains on your investments (capital gains) with realized losses (capital losses). That means selling stocks, bonds, and mutual funds that have lost value, to help reduce taxes on gains from winning investments. However, don’t undermine your long-term investing goals by selling an investment just for tax purposes. Tax-loss harvesting needs to be completed by December 29, because that is the last business day of this year.

**Plan ahead:** Taking full advantage of tax-loss harvesting requires having complete and accurate records of what you paid for your investments—the cost basis. Consider choosing the actual cost method of tracking the cost basis of stocks, bonds, and mutual funds in your investment accounts. That way, you can identify specific shares you want to sell that will maximize the loss for tax-loss harvesting purposes.

### 6. Review your deductions to maximize tax savings

Bunching deductions this year, or saving them for next year, may help you maximize their value. There are several reasons to consider this strategy:

- Some potential deductions, such as medical and miscellaneous deductible expenses, can't be claimed until they exceed a certain percentage of income.

- Itemizing deductions is only advantageous when the total amount you can deduct exceeds the standard deduction.

- You want to maximize deductions in a year when you expect higher-than-normal income.

For example, only qualified medical expenses exceeding 10% of your AGI are deductible. To maximize the deductible amount, you could schedule and pay for deductible elective procedures prior the end of the year, or pay next year’s health insurance premium in advance, if possible—as long as you pay the premium yourself, rather than through pretax payroll deductions. Similarly, miscellaneous deductible expenses, such as unreimbursed employee expenses, union dues, and work-related travel, must exceed 2% of AGI to be deductible, so you could, for example, consider bunching these expenses into every other year, when possible.

Bunching can also be an effective strategy for income. If you're close to one of the tax bracket thresholds that would cause your marginal tax rate to be higher, you might consider bumping any discretionary income into next year.

**Plan ahead:** Whether you're bunching deductions or bumping income, be sure to consider what you expect your tax situation to be the following year. If you expect your income to be higher, for example, you might want to bunch your deductions next year instead of this year. Similarly, pushing discretionary income into next year might not make sense.
Planning is key

While these year-end strategies and others may help reduce your tax bill for 2017 the best tax strategy is a comprehensive plan that's implemented year-round. The tax code is complicated, and every strategy you employ needs to be considered bearing in mind how it may affect some other aspect of your financial situation. Comprehensive tax planning is the key.