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Smart Tax Strategies for Now ... and Later

It's fair to say that the topic of taxes has been on the minds of many in recent weeks. Just before the end of 2017, President Trump signed into law the most sweeping overhaul of the federal income tax code since 1986. Before the ink was dry on his signature, however, tax experts and financial planners were busily poring over the text of the new legislation, looking for ways to help their clients take advantage of the law's new provisions or to avoid any unpleasant surprises that might be in store.

Without question, the new law will change assumptions and planning for many wealthy individuals, retirees, business owners, and even high school and college students. And though the returns due by April 15, 2018, are still subject to the former rules, there are a number of strategies available now that should be carefully considered as we move forward.

In this article, we'll highlight a few of the more important changes and briefly discuss some tax strategies that could make a big difference in both short- and long-term scenarios.

Assess taxation of your Social Security income. Social Security income is not taxed if a single taxpayer makes $25,000 or less per year ($32,000 for married filing jointly). From that base level up to $45,000 (married filing jointly), 50 percent of Social Security benefits may be taxable at your ordinary income rate. Above $45,000, 85 percent of Social Security benefits are subject to income tax. On the more positive side, the lower nominal rates of taxation indicated by the new tax brackets mean that any Social Security income that is taxed will be assessed at a lower rate than in the past. Also, for those who have traditional IRAs, it can make sense to convert to a Roth IRA; you'll pay some taxes now on the conversion (albeit at lower rates than previously, because of the new, lower tax brackets), but the income you take from the account in retirement will be tax-free, reducing the amount of taxable income that can push more of your Social Security benefits into the taxable category. You can also exercise optimal timing on taking distributions from retirement savings accounts and also for realizing taxable gains and losses on investments; both of these strategies can help limit the amount of your SSI benefits that become taxable.

"**Bundle" deductions now, take larger standard deduction later.** The new law has dramatically decreased the number and availability of many personal deductions, such as investment and tax preparation expenses, some state and local taxes, and others. If you haven't already filed your return for 2017, you may wish to "double up" on some of these deductions on your current return (subject to some limits imposed by the new law), maximizing tax savings available under the "old rules." Though you won't be able to claim these on your 2018 return, there is some good news: the standard deduction has been nearly doubled. So, instead of a standard deduction of $6,500 for a single taxpayer ($13,000 for married filing jointly), next year you'll be able to deduct $12,000 ($24,000 MFJ). And this can also apply to future tax years. You may wish to consider "doubling" charitable donations in one year, then taking only the standard deduction the next. Doubling up on deductions can also help place your taxable income in a lower bracket for capital gains taxes, in which case you might wish to "harvest" capital gains and pay taxes on them at a reduced rate.

Move your residence to a low-tax state. One of the most-debated changes in the new tax law was its large reduction in the deductibility of state and local taxes. For residents in low-tax states like Texas, Florida, and Tennessee (where there is no state income tax, for example), this provision was less important. But for those living in places like New York, California, and Illinois, losing the ability to deduct state income taxes and 100 percent of the property taxes on expensive homes creates potential for some tough decisions. Some high-net-worth individuals may opt to relocate their primary residence to a low-tax state and maintain a much smaller residence in the high-tax location. Especially for those who already split their time between two locations, this strategy could make a lot of sense. It is very important to be familiar with both states' requirements for full-time residency, as high-tax states, especially, may be expected to be extra vigilant in this regard. Kiplinger.com offers a convenient state-by-state guide to taxes on retirees; utilize this handy resource to begin evaluating whether such a move makes sense for you.

Estate Planning: Both Simpler and More Complicated. Those with substantial estates were cheered by the provision of the new tax law that raised the exemption on the estate tax from just under $5.5 million to $11.2 million per individual. This means that a married couple with an estate valued at up to $22.4 million can now pass their assets on to heirs without incurring estate tax liability. What many are not focused on, however, is that this provision is set to expire in 2026. Unless a future Congress renews or extends it, the old, lower exemption will go back in force in just eight years. This means that persons with estates at or near the new, higher limit should still carefully review their estate planning documents and strategies. If nothing else, appreciation in value may push estates over the limit, so careful planning now can avoid unpleasant surprises for heirs later. Also, the new law retains the rule for a stepped-up cost basis of inherited assets. That means that passing appreciated assets (such as stocks, mutual fund shares, and real estate with capital gains) sooner, rather than later, still permits heirs to receive them with a basis equal to the value at the donor's death. Careful utilization of trusts and other asset-transfer structures can save children and grandchildren significantly when the day eventually arrives for them to take ownership.

As with any plan involving your finances and taxation, you should consult a qualified tax or financial advisor before making any moves. Such strategies should take into consideration not only your present situation, but your future plans and any projected changes in the value of your estate, your heirs, and any other likely shifts in your and your family's situation. But looking ahead can provide some additional peace of mind in the here-and-now.

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