2023 Year-End Financial Planning Guide

Octavia Group • Ferguson Wellman • West Bearing

AS WE HEAD TOWARD THE END OF THE YEAR,

now is the ideal time to review your financial strategies before certain deadlines.

Here are the top areas we recommend you explore with your tax, legal and investment advisors. Although many deadlines are December 31, addressing them earlier could alleviate any last-minute angst you may encounter.

The SECURE Act 2.0 was passed in 2022 with a number of changes starting in 2024. This icon » represents areas that will be impacted by the SECURE Act 2.0 in 2024 or future years.

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TIME-SENSITIVE

ANYTIME

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2023

CHARITABLE TAX PLANNING

Supporting philanthropic causes not only allows us to impact our community, region or planet, but often results in a tax deduction. Due to the higher standard deduction provided under the 2017 Tax Cuts and Jobs Act, many taxpayers find their typical annual charitable giving does not provide an additional tax benefit. It is important to work with your tax advisor to determine whether strategies, such as bunching multiple years of giving within a single calendar year, using a donor-advised fund (DAF), or making qualified charitable distributions (QCDs) from your traditional IRA would increase the tax savings associated with your charitable giving.

Deductions for charitable contributions are limited to a stated percentage of adjusted gross income (AGI) in the year the deduction is taken. Limitations range from 20% - 60% of AGI based on the type of gift and nature of the receiving organization (e.g., gifts of long-term appreciated securities to a DAF are typically deductible up to 30% of AGI). Contribution amounts in excess of these deduction limits may be carried over, with a limit of five subsequent tax years.

Timing is very important for charitable donations made near year end. Generally, a charitable donation is deductible in the year it is delivered to the charity. While transfers of cash can be completed relatively quickly, it is often more tax-efficient to donate appreciated assets. Depending on the type of assets being donated, the method of delivery, and institutions involved, it is often necessary to organize and complete such gifts in early December, allowing ample time for processing and delivery to the charity.

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CHARITABLE TAX PLANNING

- Here is a list of Schwab's 2023 year-end giving deadlines.
- For more information on QCDs, click here. This resource mentions how inflation will impact QCDs starting in 2024 following SECURE Act 2.0.

ESTATE PLANNING

It is good practice to review your estate plan annually, at least briefly. At a minimum, check to see if any major changes have occurred in your goals and the authorized decision makers in your plan. The federal estate-tax exemption is the cumulative amount we can give away during our life and/or at our death without incurring a federal transfer tax of 40%. The Tax Cuts and Jobs Act, which became effective in 2018, doubled the previous exemption of $5 million, adjusted for inflation. For 2023, the estate-tax exemption is $12.92 million per person. Without further congressional action, this exemption will revert to $5 million (adjusted for inflation) in 2026.

For those with taxable federal estates, there are several strategies that can be employed to mitigate your future estate tax liability. Even those under this threshold should consider a detailed review of their projected net worth. The acceleration of this reduction has been an element of policy proposals in recent years and is a another reason to review your estate planning regularly.

Lifetime gifts may be outright gifts to heirs with no restrictions or may be completed through various types of irrevocable trusts providing resources to beneficiaries over time or for specific purposes. These trusts may offer tax advantages in addition to possible protections but do take time to develop. To ensure time for thoughtful planning that is consistent with your long-term goals, it is important to allow adequate time for any possible drafting by your attorney.

ANNUAL GIFT EXCLUSION

For 2023, individuals can give away $17,000 per recipient without incurring federal gift taxes or using up any portion of their $12.92 million lifetime transfer-tax exemption. Spouses can give away a combined $34,000. These gifts need to be received and deposited by the recipient by December 31 to qualify. Annual gifting can be an effective way to reduce your taxable estate.

For those interested in funding 529 (education) plans, there are special rules that allow "superfunding" 529 accounts with five years' worth of "annual gifts." See the 529 Plans for Education Savings section.

There are several things the IRS does not consider a gift. You may give an unlimited amount in these categories without gift tax consequences:

- Transfers to spouses who are U.S. citizens
- Charitable donations
- Tuition paid directly to educational institutions on behalf of someone else
- Funds paid directly to medical service or health insurance providers on behalf of someone else
- Gifts to a political organization for its use

MAXIMIZING CONTRIBUTIONS TO RETIREMENT PLANS

While contributions to traditional IRAs and Roth IRAs can be made up until April 15, 2024, employee contributions to many employer-provided retirement plans, such as 401(k)s, 401(a)s, 403(b)s and SIMPLE IRAs, must be made by December 31. Review your year-to-date contributions, and if you are falling short of the maximum allowed contribution, consider increasing your deferral out of your final paycheck.

The following chart highlights the 2023 contribution maximums by plan type.

PLAN TYPE	2023 LIMITS
401(k), 403(b), Profit-Sharing Plans, etc.	$22,500
Catch up contributions for those age 50 and older	$7,500
SIMPLE Plan	$15,500
Catch up contributions for those age 50 and older »	$3,500
Traditional IRA and Roth IRA	$6,500
Catch up contributions for those age 50 and older	$1,000
Annual employer limit for 401(k), SEP IRA and solo 401(k)	$66,000

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MAXIMIZING CONTRIBUTIONS TO RETIREMENT PLANS

For high-income earners looking for ways to increase their tax-advantaged retirement savings, it may be worth exploring nonqualified compensation plans (e.g., deferred compensation plans) and the backdoor Roth. For tax year 2023, single taxpayers with a modified adjusted gross income (MAGI) more than $153,000 and married taxpayers more than $228,000 are completely phased out from directly contributing to a Roth IRA. The backdoor Roth sidesteps the Roth contribution income limits by making a nondeductible IRA contribution with after-tax dollars. The contribution is then converted to a Roth with no additional tax due, assuming there was no growth between contribution and conversion.

➔ Here is one of our resources addressing backdoor and mega-backdoor Roth strategies.

ROTH IRA CONVERSIONS

Although we are faced with uncertainty about future tax law, we currently have some of the lowest tax brackets in history. If you are in a low tax-rate year, and expect your rates to rise in the future, you should consider partial conversions of a tax-deferred retirement account to a Roth IRA. Although the conversion will create taxable income in the year of conversion, it can result in long-term tax savings by paying tax at a lower rate in the conversion year than you would on distributions in future years. This strategy should also be considered any time you have a uniquely low tax year, such as when making a large charitable contribution, are between jobs, or recently retired and not yet claiming Social Security.

Roth IRA conversions may also be advantageous over multiple generations. First, if your heirs may be in higher income tax brackets than you are, paying taxes at your lower rate now can save taxes across generations. Secondly, Roth conversions prior to death can reduce estate taxes by virtue of the income tax being paid during life, reducing the value of the taxable estate at death.

➔ Additional Roth conversion considerations can be found here.

REQUIRED MINIMUM DISTRIBUTIONS

The age at which required minimum distributions (RMDs) start has been adjusted twice in the past five years based on new law. It was 70 ½ prior to the passage of the SECURE Act in December 2019, which pushed the required age back to 72 for those who had not turned 70 ½ prior to January 2020. Following the SECURE Act 2.0 the age to begin taking RMDs depends on the year in which you were born. For people born before 7/1/1949 the RMD applicable age is 70 1/2. Those born on or after 7/1/1949, or in 1950, have an RMD applicable age of 72. Those born between between 1951 and 1958 have an RMD applicable age of 73. Those born in 1960 or later will not be subject to RMDs until age 75. Due to an oversight in the legislation those born in 1959 will require guidance on whether their RMD applicable age is 73 or 75.

Starting in the year your RMDs begin, and every year thereafter, the Internal Revenue Service (IRS) mandates that a certain amount of funds be withdrawn. These required distributions must be withdrawn by December 31 each year. Your initial distribution may be deferred until April 1 of the year after you reach your required beginning age, but the following year's distribution will also be required, resulting in two RMDs in one tax year. While some clients benefit by deferring their initial distribution (and resulting tax deferral) for one calendar year, other clients are pushed into a higher tax bracket as a result of receiving two distributions in the subsequent year.

For those interested in supporting charitable organizations, especially those who do not

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REQUIRED MINIMUM DISTRIBUTIONS

itemize their deductions on their tax return, qualified charitable distributions (QCDs) made directly from an IRA to a charitable organization may be attractive as they are not subject to income tax, reduce adjusted gross income and are eligible to satisfy the RMD requirement. QCDs are allowed for individuals over age 70 1/2 and may not exceed $100,000 in 2023. » As a result of SECURE Act 2.0, the annual $100,000 limit for QCDs will be indexed for inflation, effective 2024 and each year thereafter.

The SECURE Act also replaced the lifetime "stretch" provision for certain beneficiaries of inherited IRAs and other retirement accounts after 2020 with a 10-year distribution requirement. The 10-year distribution requirement imposed by the SECURE Act for beneficiaries inheriting an IRA has caused many individuals to adjust their plans. Strategies for mitigating the future tax impact to heirs include increasing withdrawals above the required annual minimums, converting a portion or the full IRA balance to a Roth IRA and including charitable beneficiaries, which are not subject to income or estate taxes.

HEALTH SAVINGS ACCOUNTS AND FLEXIBLE SPENDING ACCOUNT FUNDS

Health savings accounts

Contributions to health savings accounts (HSAs) must be made by April 15 of the following year. If you have a high-deductible healthcare plan, you may be eligible to open and fund an HSA even if your employer doesn't sponsor one as a part of their benefit package. These accounts are unique in that they can be triple-tax free. Contributions are deductible (up to annual limits), the funds grow tax-free and withdrawals are tax-free when used for eligible medical expenses. In 2023, an individual can contribute up to $3,850 for the year to their HSA. An individual with family coverage can contribute up to $7,750 for the year.

Flexible spending account funds

Unlike funds in HSAs, flexible spending account (FSA) funds do not rollover from year-to-year. Each plan is unique, but generally they are a use-it-or-lose it account and qualified expenses often need to be incurred by December 31. It is not uncommon to overlook funds set aside in FSAs, so take a moment to confirm the deadline for your FSA, review any outstanding balances and plan to use them up before year end.

Some plans may allow for a small balance, $615 in 2023, to be rolled over to future years if done within a specific time frame. Check with your employer to verify the exact rules and deadlines applicable to your FSA.

Additional consideration

If you have already met your health insurance plan's annual deductible, consider incurring any additional medical expenses before the end of the year, at which point your annual deductible will reset.

529 PLANS FOR EDUCATION SAVINGS

If you are planning for the education of children or grandchildren, consider making an annual contribution to a 529 plan. Many states offer a tax benefit in the form of a deduction or credit for contributing to a 529 plan.

Contributions to 529 plans are considered gifts for tax purposes. In 2023, you can give up to $17,000 per recipient without triggering a gift tax. However, a special rule allows you to “superfund” five years’ worth of “annual gifts” into a 529 in a single year without gift-tax consequences. For 2023, you can contribute up to $85,000 per 529 plan beneficiary and treat the contribution as if it were made over five consecutive years. This superfunding feature allows a donor to front-load a 529 plan and over time removes assets from the donor’s estate. Additional details on superfunding can be found here.

Review the rules for your state plan and consult with your tax advisor to confirm the state tax benefit available.

STRATEGIZING WITH YOUR CPA AND PORTFOLIO MANAGER

Income-tax rates, capital-gains tax rates, the taxation of Social Security and Medicare premiums are all affected by levels of income. Depending on your circumstances, you may benefit from harvesting capital losses or even accelerating capital gains as part of a multiyear tax and investment strategy.

The ability to influence your taxable income becomes even more meaningful if you live in a state and/or county that assesses additional taxes.

There are policy proposals from time to time that may impact the tax code. Partnering with your professional tax, legal and financial advisors to understand your current situation and how it may be impacted by future changes will enable you to respond if appropriate.

On first reflection, we may feel that we have little control over the timing of income. However, there are a number of common strategies for shifting income and deductions. Following is a list of common strategies you may wish to review with your tax advisor:

Grouping deductions

- Charitable deductions including the use of donor-advised funds, qualified charitable distributions, or charitable remainder trusts
- Healthcare expenses
- Business expenses for pass-through entities

Deferring income

- Contributing to qualified retirement plans

continued

STRATEGIZING WITH YOUR CPA AND PORTFOLIO MANAGER

- Nonqualified retirement savings such as deferred compensation plans
- Harvesting losses
- Installment sales
- 1031 like-kind exchange

Accelerating income

- Withdrawals from retirement accounts
- Partial Roth IRA conversions
- Selling appreciated assets
- Taking bonuses or other compensation where you can control the timing
- Exercising stock options.

Regardless of policy changes, most individuals will benefit from thinking strategically about how their income tax brackets and rates are likely to evolve over the course of their life. Seeing the big picture will help identify opportunities for accelerating income into lower bracket years and grouping deductions into higher bracket years.

REVIEW YOUR BUDGET

The start of a new year is a good time to compare actual income and expenses to your projected figures. During this review, revisit recurring expenses, such as subscriptions and memberships and eliminate those you are no longer using or enjoying.

Confirm you have a comfortable amount of cash for your near-term needs, in addition to an appropriate emergency reserve. A good practice is to have cash available to cover a minimum of three-to-six months' worth of expenses.

Our clients and their families have access to our *Dollar Sense* education program, which includes a basic budget and finance course called, *Financial Footwork*. Contact dollarsense@fergwell.com for more information about enrollment.

Here are some other budget and expense tracking apps and resources to support you:

- Consumer Finance Protection Bureau – Basic budgeting tips to get started
- The best budgeting apps and tools according to *The New York Times*
- You Need a Budget (YNAB)
- Simplifi by Quicken
- Mint by Intuit

INSURANCE REVIEW

Planning for the risk of unknown events is a key component of a solid financial plan. There are many considerations to building a solid insurance plan and we recommend conducting an annual review with your insurance agent, particularly given changes to real estate values and replacement costs in recent years. If you are looking for an agent specializing in coverage for high-net worth individuals, we are happy to provide potential resources. Annual insurance considerations include:

Homeowners

- Does your policy allow you to repair or rebuild your home at today's replacement costs?
- Is your property vulnerable to natural catastrophe (e.g., earthquake, wildfire, flood)?

Health/long-term care/life

- Do you have a plan for coverage throughout retirement?
  - » If retiring prior to age 65, will you have coverage prior to Medicare?
- Can you afford to self-insure your potential long-term care needs?
- Would your family need additional resources if you died prematurely?

Personal liability

- Is your coverage appropriate to your risk factors and net worth?
- Common risk factors include pool, trampoline, dog, teenage drivers, public visibility, investment real estate, owning a business or employing staff.

INSURANCE REVIEW

Additional considerations

- Are you a board member of a public, private or nonprofit company?
- Do you have coverage for personal or cybersecurity threats?
- Have you had any significant changes in personal status?

LIABILITY REVIEW

Credit card review

Assess whether you are effectively utilizing their benefits and rewards, ensuring you are getting real value from them. Carefully review the annual fees associated with each card to determine if they are justified by the benefits they offer. Additionally, consider how different types of rewards, such as cashback versus airline miles, align with your spending habits and financial goals.

Mortgage refinance

Before deciding to refinance your mortgage, consider the terms of your mortgage, particularly the interest rate and remaining term. Evaluate potential risks of variable rate mortgages in the current interest rate environment. Many lines of credit will also reset at least annually. The impact of these interest rate changes can have a negative impact on your cash flow.

Furthermore, the Tax Cuts and Jobs Act decreased the limit on mortgage-interest deductions for new mortgages. Most itemizing homeowners can deduct mortgage interest paid on up to $750,000 worth of acquisition debt, on their primary residence or vacation home if the debt was put in place after December 15, 2017 and up to $1 million in principal if the debt was put in place prior to December 16, 2017. Homeowners exceeding these limits may want to evaluate if restructuring their debt would result in increased deductibility or rate savings.

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LIABILITY REVIEW

Credit lines

Lower-cost credit lines can increase your financial flexibility. Review your options using a margin line, pledged-asset line, or home-equity line of credit. Even in a higher rate environment, adding credit before it is needed can help to increase your financial flexibility.

Credit report check

Monitor for fraud and ensure your file is accurate before you ask a prospective lender to review it during underwriting. You can access your free credit report at www.annualcreditreport.com, the official free credit report available from the three most prominent credit bureaus: Equifax, Experian and Transunion. By regularly monitoring your credit report, you can identify any errors or discrepancies and stay informed about your credit health.

WEALTH HORIZON™

Wealth planning is a comprehensive process of understanding clients financial, family and philanthropic goals in the context of their current resources and projected cash flow. Wealth planning at Ferguson Wellman and West Bearing leverages our *Wealth Horizon*™ planning process for clients and includes:

- Wealth projections
- Asset allocation review
- Cash flow and spending analysis
- Goal-based planning
  - Home purchase
  - Major purchases
  - Gifting
  - Philanthropic strategies
  - Education planning

The *Wealth Horizon*™ process can be especially helpful in forming a plan or evaluating your readiness for retirement, reviewing your asset allocation, prior to making large family or charitable gifts and in identifying many ongoing planning opportunities and risks. If you have not completed a Wealth Horizon™ or changes have occurred in your life that warrant a refresh, please contact your portfolio manager to begin the process.

➔ Take a look at our wealth planning approach here.

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Ferguson Wellman creates customized investment portfolios and wealth management strategies with assets starting at $4 million. Our division, West Bearing Investments, has a minimum of $1 million for portfolio and wealth management. Our family office solution, Octavia Group, provides personal financial services for Ferguson Wellman and West Bearing clients who have a minimum of $10 million managed by our firm.

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