Highlights

- No Significant Tax Legislation on the Horizon
- Bunching Itemized Deductions
- Changes to Credits for Electric Vehicles
- Corporate AMT Returns in 2023

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Tax Briefing | 2022 Year-End Tax Planning

Planning strategies and techniques available through end of year

2022 has seen a continued return to stability from the impacts of the COVID-19 pandemic. Both businesses and individuals have almost totally returned to normal, though shifts in labor policies have led to big changes in the way people work and create personal balance.

The global economy, however, continues to feel the effects of the pandemic. Disruptions to supply chains, along with many other factors, led to high inflation in the last months of 2021 and throughout 2022. Many businesses and individuals have had to reckon with rapid price increases in raw materials, energy, and consumables.

In response to this issue, Congress passed the Inflation Reduction Act of 2022. While it is yet to be determined whether the legislation will lower inflation, many economists agree that the provisions of the bill won't make inflation worse, unlike earlier stimulus bills passed in response to the pandemic. However, what the Inflation Reduction Act of 2022 does provide are many of the green energy proposals that were promised by President Joe Biden during his 2020 campaign and included in his Build Back Better Plan in 2021.

The Act provides investment in clean energy, promotes reductions in carbon emissions, and extends popular Affordable Care Act premium reductions. The Act is primarily paid for through the implementation of a 15 percent corporate minimum tax and budget increases for the Internal Revenue Service to close the "tax gap."

Despite the bumpy road of the last two years, the tax world has largely stabilized since the passage of the Tax Cuts and Jobs Act (TCJA) in 2017. This has made year-end

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planning more predictable. Nonetheless, there are still steps that can be taken in response to recent developments, in addition to the tried-and-true methods than can be taken on an annual basis.

LEGISLATION

When President Biden was campaigning in 2020, he promised to provide a huge increase in social spending, with more robust health, education, and welfare programs meant to improve the quality of life for lower and middle-income voters.

Parts of those legislative promises were included in the American Rescue Plan Act of 2021. However, in conjunction with that legislation, Biden presented the Build Back Better Plan, which called for infrastructure investment, green energy incentives, and permanent extension of the credit expansions in the American Rescue Plan Act of 2021. These programs were to be paid for with tax increases on higher-income taxpayers, with a specific promise that no one making less than $400,000 would see a tax increase. Both ordinary income and capital gains tax rates were to be increased. An increase in the corporate tax rate was also proposed.

While the infrastructure provisions were rolled into the Infrastructure Investment and Jobs Act in 2021, the rest of the plan stalled out in the Senate and was seemingly dead. However, an announcement of a surprise deal among lawmakers in summer, 2022 brought many of the provisions back to life. Gone were the corporate and individual rate increases, instead replaced with a new corporate alternative minimum tax. Many of the new provisions have 2023 effective dates, which makes year-end planning in 2022 essential.

The remainder of 2022 could see additional legislation. Much will depend on the outcome of the election on November 8, 2022. Many of the provisions that are regularly extended for one or two years at a time, known as extenders, have expiration dates beyond 2022 due to various prior legislative efforts. However, there are a handful of provisions that expired at the end of 2021 that could be extended by a lame duck session of Congress.

MINIMIZING INDIVIDUAL TAXES

Income taxes

The key to any year-end planning strategy is to minimize taxes. This is generally done by either reducing the amount of income received or increasing the amount of deductions. In recent years, the possibility of increased rates on higher incomes due to proposed legislation, or changes in qualification for various stimulus proposals, made the decision of deferral or acceleration highly dependent upon individual circumstances. However, as the end of 2022 approaches, these factors are not really in play anymore.

Instead, the impact of inflation makes deferral of income a likely winner for almost all individuals. In October, the IRS released the inflation-adjusted tax brackets for 2023, and they reflected the 8% inflation that has been hitting the U.S. economy. As an example of the increase in the brackets, the rates for married taxpayers filing jointly in 2022 compared to 2023 are below:

2022

If Taxable Income Is:

Over	But Not More Than	The Tax Is	Of the Amount Over
$0	$20,550	$0 + 10%	$0
20,550	83,550	2,055.00 + 12%	20,550
83,550	178,150	9,615.00 + 22%	83,550
178,150	340,100	30,427.00 + 24%	178,150
340,100	431,900	69,295.00 + 32%	340,100
431,900	647,850	98,671.00 + 35%	431,900
647,850		174,253.50 + 37%	647,850

2023

If Taxable Income Is:

Over	But Not More Than	The Tax Is	Of the Amount Over
$0	$22,000	$0 + 10%	$0
22,000	89,450	2,200 + 12%	22,000
89,450	190,750	10,294 + 22%	89,450
190,750	364,200	32,580 + 24%	190,750
364,200	462,500	74,208 + 32%	364,200
462,500	693,750	105,664 + 35%	462,500
693,750		186,601.50 + 37%	693,750

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Individuals may not necessarily see increases in earnings that keep up with that level of inflation, meaning that if deferral of income from 2022 into 2023 is possible, it would mean that more income would fall into a lower tax bracket. In the long run, that would mean a lower aggregate tax burden.

Delaying and reducing gains

Like taxes on ordinary income, taxes on capital gains also apply at different rates depending upon the amount of taxable income. For 2022, the rates are as follows:

	0%	15%	20%
MFJ/SS	$0 - $83,350	$83,351 - $517,200	over $517,200
MFS	$0 - $41,675	$41,676 - $258,600	over $258,600
HoH	$0 - $55,800	$55,801 - $488,500	over $488,500
Single	$0 - $41,675	$41,676 - $459,750	over $459,750
E&T	$0 - $2,800	$ 2,801 - $13,700	over $13,700

For taxpayers whose income tends to fluctuate from year to year, it would be wise to examine the impact of sales of investment items. For taxpayers who think they may have lower income in 2023, it would be smart to hold off on a sale of a capital item if their income is at or near a threshold for a higher capital gains bracket.

This type of consideration should not be limited to capital gain taxes, but also the net investment income (NII) tax. The 3.8% NII tax kicks in at $200,000 of modified adjusted gross income for single and head-of-household filers, $250,000 for joint filers, and $125,000 for married taxpayers filing separately.

COMMENT. *Since the NII thresholds fall right in the middle of the 15% capital gains bracket, a taxpayer to whom the NII applies because of a sale of a capital item would likely not be able to reduce the tax to 0%. But, a taxpayer who is barely in the 20% bracket could defer a sale and get into the 15% bracket, meaning a sale of a capital item would only be taxed at 18.8% instead of 23.8%.*

Maximizing deductions

For 2022, the inflation-adjusted standard deduction amounts are $25,900 for joint filers, $19,400 for heads of households, and $12,950 for all other filers. With standard deduction amounts so high, coupled with the $10,000 limitation on the deduction of state and local taxes, it is difficult for many taxpayers to claim enough deductions to make itemizing deductions beneficial. Thus, maximizing deductions may not be beneficial for all taxpayers.

One of the best ways to maximize the amount of deductions is to develop a bunching strategy. This involves accumulating charitable contributions, or even medical expenses (see below), from two or more years into one year. For example, a taxpayer may have not made any of his or her normal charitable contributions in 2021, and then made double the normal amount in 2022 in order to help surpass the standard deduction amount.

COMMENT. *Again, the impact of inflation must be considered here, as the standard deductions are much higher for 2023 as compared with 2022. Even with bunching, it might be difficult to achieve itemized deductions high enough in 2023 to surpass the standard deduction.*

The same strategy can be employed for deductible medical expenses where the timing is somewhat flexible, such as for elective procedures (remember that purely cosmetic procedures are not deductible).

COMMENT. *Bunching can be a very effective strategy, but it has to be effectively used, and potentially planned out two or three years in advance to maximize the benefit, while also taking into account shifts in tax policies as a result of political change.*

Clean vehicles

Prior to the Inflation Reduction Act of 2022, a fairly broad tax credit was available for taxpayers who purchased a plug-in electric vehicle. The credit could be as high as

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$7,500, depending upon the battery capacity of the vehicle. Under the new Clean Vehicle Credit, the maximum credit amount is still $7,500, but the requirements for a vehicle to qualify for the credit have become much more stringent. While the new credit eliminates the old limitation based upon the number of qualifying vehicles sold by particular manufacturers, there will be a new limitation based on the MSRP of the vehicle. Additional requirements take effect in 2023. However, the rules applicable to the old credit can still be applied to vehicles purchased in 2022, except that the vehicles' final assembly must be in North America, even if applying the old law.

COMMENT. *Very few vehicles qualify under the final assembly requirement, so taxpayers should speak with a tax professional before relying on the expected credit amount when making purchase decisions.*

After 2022, a credit is also available for the purchase of a previously owned clean vehicle. Similar requirements for qualification of a new clean vehicle apply to a previously owned clean vehicle, and there are also income limitations.

COMMENT. *Taxpayers considering the purchase of a previously owned clean vehicle may want to wait until 2023 to make the purchase, if they would qualify for the credit.*

Student loan forgiveness

On August 24, 2022, President Biden announced the forgiveness of up to $20,000 of federal student load debt for qualifying borrowers. Applications are now open for borrowers to apply for forgiveness.

COMMENT. *While not strictly a tax-related issue, the application process is time sensitive, and under a provision of the American Rescue Plan Act of 2021, any discharged student loan debt before 2026 is excluded from income.*

Other year-end strategies

A number of other traditional year-end strategies may apply. These include:

- Maximizing Education Credits – Individuals can claim a credit for tuition paid in 2022 even if the academic period begins in 2023, as long as the period begins by the end of March.
- Increasing 401(k) Contributions – Adjusted gross income (AGI) can be reduced if individuals increase the amount of their 401(k) contributions.
- IRA Contributions – Individuals eligible for deductions for IRA contributions can claim deductions, and thus reduce AGI, for amounts contributed through April 18, 2023.
- Teacher deductions – Educators can claim a deduction for up to $300 of classroom expenses (like books, supplies, and computer equipment, as well as personal protective equipment, disinfectant, and other supplies used to prevent the spread of COVID-19), and should maximize those expenses by year-end.

YEAR-END BUSINESS STRATEGIES

Corporate AMT

The Inflation Reduction Act of 2022 resurrected the corporate alternative minimum tax (AMT) which was eliminated by the TCJA, although in a slightly altered form. Effective for tax years beginning after 2022, the new corporate AMT equals 15 percent of the corporation's "adjusted financial statement income" for the tax year, reduced by a corporate AMT foreign tax credit. The tax only applies to corporations with average annual adjusted financial statement income in excess of $1 billion for the three prior tax years. This threshold is reduced to $100 million in the case of certain foreign-parented corporations. Certain exceptions also apply to the determination of an applicable corporation where there is a change in ownership or a consistent reduction in income.

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"The Inflation Reduction Act of 2022 resurrected the corporate alternative minimum tax."

A corporation's adjusted financial statement income is the amount of net income or loss the corporation reports on its applicable financial statement, for purposes of determining when to include income for tax purposes. That amount is adjusted for various purposes, including certain adjustments in the case of consolidated returns or for certain foreign income.

COMMENT. *Affected corporations may want to try to accelerate profitability on their financial statements into 2022 where possible.*

Depreciation and expensing

The TCJA provided very generous depreciation and expensing limitations. Businesses may want to take advantage of 100-percent first-year depreciation on machinery and equipment purchased during the year. Additionally, Code Sec. 179 expensing has an investment limitation of $2,700,000 for 2022, with a dollar limitation of $1,080,000.

COMMENT. *These provisions do not apply to 2022 only, so there is time to take advantage of them in later years. Notably, the IRS announced a big jump in the investment and dollar limitations for 2023, to $2,890,000 and $1,160,000 respectively, so it may be advantageous to hold off in these expenses to 2023 to take advantage of dramatically higher limitations.*

Research and development expenses

The TCJA required that any research and development costs incurred after 2021 would have to be amortized ratably over five years rather than deducted in the year the costs are incurred (or amortized over five or ten years at the election of the taxpayer, subject to specific requirements).

COMMENT. *There have been proposals to extend the direct expensing of these costs to years beyond 2021. While there is nothing currently proposed, retroactive extension is a possibility, so the door may not be entirely closed.*

Clean commercial vehicles

The Inflation Reduction Act of 2022 also provides a new $7,500 credit for the purchase of clean commercial vehicles after 2022. The requirements for this credit are very similar, so the same considerations made by individuals should be made by businesses thinking about purchasing environmentally friendly vehicles.

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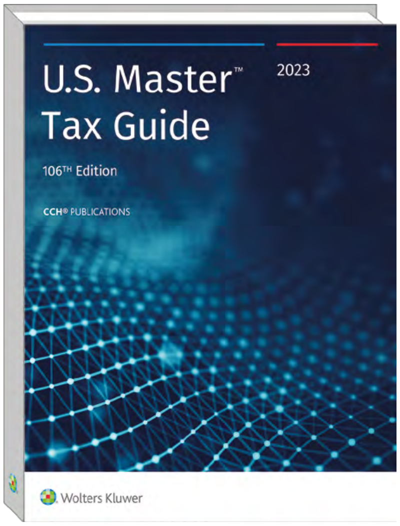

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