Clean Sweep Letter

Time for a Clean Sweep

Your tax return is a good window into your total financial picture.

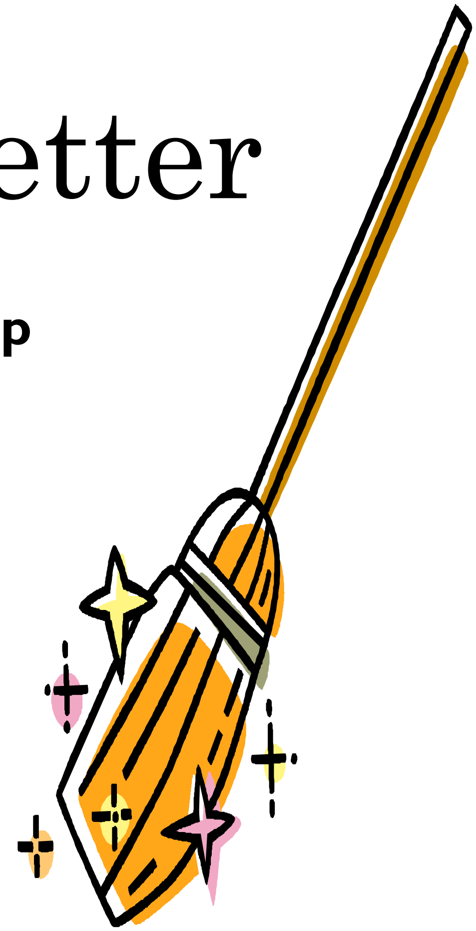
You can clean up your financial and tax life by reviewing your 2023 tax return. As you prepare to put the forms away, take a few moments to assess your situation:

Will your income or expenses change this year?

Did you like last year's results?

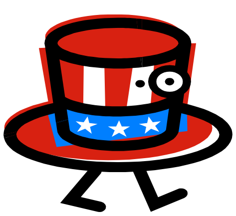
Have you ever taken a good look at your tax return? Maybe now's the time.

You can use this handy guide.



Did you get a large refund?

Owe too much? Now is the time to change this situation.



Is Uncle Sam walking away with an interest-free loan from you?

Or…

Is he collecting interest on your deficiencies?

<u>If you owed so much that you paid penalties:</u>

It might be wise to change your withholding at work by submitting a new W-4. The W-4 was recently redesigned and is more complex than before. Here are the steps on form W-4 that will result in increased withholding:

Step 2: If your spouse works (or if you have more than one job) completing this step will increase withholding.

Step 3: Removing one (or more) of your dependents will increase withholding.

Step 4: Completing subsections (a) and (c) will increase withholding. Completing subsection (b) will decrease withholding.

If you pay estimated tax, and expect this year to be similar to last, make sure your payments at least equal last year's tax.

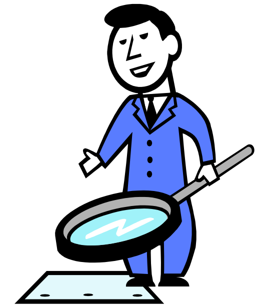
<u>If you got a large refund:</u>

Did you put the money to good use, or could you have used the money last year in a better way?

If you decreased your withholding on Form W-4, the extra money could be used to meet your current monthly payments or buy a few extra tanks of gas. If making ends meet isn't important, you could fund more retirement or open an investment account, thus enhancing your financial picture.

The average Federal tax refund is almost $3,000. That's about $250 per month that could be put to better use.

Take a look at your investment earnings.



Lines 2, 3, and 7 on Form 1040 are a snapshot of your current investment portfolio.

Are they small or nonexistent?

Perhaps a withholding change can help you build your nest egg. By decreasing your withholding on Form W-4, and depositing $50 per month into a 2% savings account, you will have $3,158 saved at the end of 5 years.

Did you know: Estimates indicate that 10.5 billion in loose change is sitting idle in American households? If you put just $2 in loose change into the 2% savings account each week, you would have $1,151 in 10 years.

Does your savings not earn enough interest? Nerd Wallet and other online financial advice websites publish lists of the best savings accounts.

Did your investments create a tax burden?

It might be wise to rebalance your investment portfolio: Long term capital gains are taxed at a lower rate than interest, so switching to tax-efficient mutual funds could decrease your tax burden.

Check to see if you have any losers that could be invested more wisely. You can offset your capital gains, plus $3,000 of other types of income, with stock losses each year.

Did you deduct a business loss on line 3 of Schedule 1?

The mere fact that you lost money on a business is a negative factor in your overall financial picture. It could also be a negative factor in your tax picture. Incorrect deduction of hobby losses amounts to billions of dollars in lost tax revenue a year, according to IRS estimates. With Congress and the IRS hot on reducing revenue losses, you should be aware that your business could be reclassified as a hobby. To get the point across, the IRS has created numerous special fact-sheets to highlight the problem. Visit the IRS Small Business and Self-employed tax center (in the business section) at irs.gov for resources and information to help you profit from your business. To determine whether your business is a hobby, the IRS asks you to consider the following factors:

- Does the time and effort put into the activity show intention to make a profit?
- Do you depend on the income from the activity?
- Have you changed your methods of operation to improve profitability?
- Do you have the knowledge to make your business successful?
- Have you made a profit in the past?
- Can you expect a profit in the future?

It would be wise to invest a little effort in growing your business to profitability.

If your business is profitable you'll likely get a deduction

Aside from avoiding the hobby rules mentioned above, The Tax Cuts & Jobs Act (TC&JA) has created another incentive for making your business profitable. It's called the Qualified Business Income (QBI) deduction. Here's how it works:

- **Who gets to take the deduction?** Profitable business owners (excluding C-corporations) with taxable income (in 2024) under $383,900 (married) and $191,950 (single) will get the deduction. If you end up making more than that it gets complicated, so lets focus on folks below these limits first.
- **How big is the deduction?** Taxpayers below these income thresholds will generally get to deduct the lesser of; 1) 20% of Qualified Business Income (QBI), or 2) 20% of taxable income minus capital gains.
- **What is QBI?** QBI is closely related to profits. If your business is profitable you likely will have QBI. There are some exceptions. For example, business owners with an extremely high mileage deduction might be profitable but not have QBI. Additionally, profitable business owners with high adjustments/deductions for health insurance premiums and/or SEP/Simple/Solo(k) contributions might not have QBI.
- **Example:** Paul is a single consultant with $75,000 in QBI and no capital gains. His taxable income (after deductions) is $57,701. His deduction is 20% of $57,701, or $11,540. This saves him $2,539 in tax.

This is an over-simplification of the QBI deduction. There are separate rules for folks with taxable income greater than $191,950 (single) and $383,900 (MFJ). If you are a specified service business your deduction begins to phase-out above these income levels. If you are NOT a specified service business you still might be able to get the deduction, but it depends on other factors such as wages paid and the value of certain business assets. It gets complicated, so ask for help to understand how to take full advantage of this favorable business deduction.

Did you pay surtaxes or were you phased out of credits and/or deductions for IRAs, student loan interest, tuition, or children due to high income?

Many tax deductions and credits phase out at certain income levels.

The best way to improve your present tax situation and your future retirement is by deferring more into your company's retirement plan. Increasing your retirement contribution will lower your income used to calculate the phase-outs.

Self-employed? You can put up to 20% of your net income into a SEP plan, thus reducing your income for each dollar contributed.

You can also offset your income with capital losses of up to $3,000 each year, as explained earlier.

Consider investing in municipal bonds. They're tax free for federal purposes.

Signing up for the Flexible Spending Account (FSA) at work can enable medical deductions that would not otherwise be deductible. It also reduces the income used to calculate the phase-outs.

No company FSA? Perhaps you could qualify for an HSA (Health Savings Account). You must be under 65, covered by a compatible high-deductible health plan, and have no other insurance to set up an HSA. For 2024, you can contribute up to $4,150 ($8,300 family) into the HSA and deduct the payment. This gets you a medical deduction without having to itemize. Withdrawals from the HSA are not taxed if used for medical expenses.

If you have children in day care, you can further reduce your income by signing up for pretax dependent care benefits.

You might also be able to deduct a contribution to a traditional IRA. The reduction that this contribution makes to your income might qualify you for the Retirement Income Savings Credit.

Did you deduct charitable contributions on Schedule A?

The rules for deducting charitable gifts are tight, (no proof = no deduction).

Cash donations must be substantiated with a receipt, cancelled check or a bank record to get a deduction. If you are still dropping cash into the collection plate at church, it would be a good idea to start writing a check. Small donations that you give to people who come around to your door can really add up. Remember to ask for a receipt. If you keep an envelope handy to collect the receipts, you'll have the documentation that is needed to satisfy IRS recordkeeping rules.

Non-cash donations need to be in at least good condition. Items of minimal value, such as socks and underwear could be disallowed. Make sure you get a receipt and document your deduction in detail. Make a list of your donated items with the fair market value and original cost. A photograph of the donated goods could also be helpful. Be sure you get a receipt.

Volunteering costs are an itemized deduction if the organization you are helping is a 501c(3) charity. This includes travel expenses if there is no significant element of pleasure, recreation, or vacation involved. You can also deduct $0.14/mile for charity work (if you track your mileage).

If you are older than age 70$^{1/2}$ you can give to a charity directly from an IRA. This is called a **Qualified Charitable Distribution** (QCD). QCDs must be made directly from the IRA to the charity. QCDs can be deducted <u>even if you don't itemize</u>.

Invest your tax savings in a Roth

You can improve your future financial picture by investing the money you saved using the above strategies in a Roth IRA. Although contributions to your Roth are not deductible, the money grows tax free and will never be taxed as long as the rules are met.

If your income is over $240,000 (MFJ) or $161,000 (Single) you have been phased out of Roth IRA participation for 2024. There is no income limit, however, on the Roth 401k. Ask your employer if this is an option for your company's retirement plan.

Did you know that taxpayers with any amount of income can convert a traditional IRA to a Roth by paying tax on the amount converted? Just remember that once you do that it can't be undone. The Tax Cuts & Jobs Act eliminated the ability to "re-characterize" such converted funds back to a traditional IRA.

Record retention guide

Filing your tax papers away can be a chore. Perhaps you need to make a clean sweep of the file cabinet.

The IRS advises that you keep your tax returns forever, but much of the supporting documentation can be destroyed after the statute of limitations for the tax year is over (three years in most cases). You can use the following guide to help make your decision.

1 YEAR

Copies (misc.)

Correspondence (routine)

Duplicate deposit slips

Stenographer's notebooks

3 YEARS

Appointment books

Correspondence (general)

Employee personnel records (after termination)

Insurance policies (expired)

Internal reports (misc.)

Petty cash vouchers

5 YEARS

Invoices

Loan documents

Notes receivable ledgers and schedules

Purchase orders

7 YEARS

Accident reports and claims (settled)

Accounts payable ledgers and schedules

Bank statements

Brokerage statements

Cancelled checks (misc.)

Employee expense reports

Employee payroll records

Inventory of products, materials and supplies

Safety records

Sales records

Scrap and salvage records

Stock and bond certificates (cancelled)

Subsidiary ledgers

Time cards and daily reports

Voucher register and schedules

Voucher for payments made

PERMANENTLY

Adoption papers

Articles of incorporation

Audit reports of accountants

Birth certificates

Bylaws

Capital stock and bond records

Cancelled checks (important payments)

Cash books

Charts of accounts

Citizenship papers

Contracts and leases (expired)

Contracts and leases (existing)

Copyright, patent and trademark registration

Death certificates

Deeds, mortgages and bills of sale

Depreciation schedules

Divorce decrees, alimony and child custody agreements

Financial statements

General and private ledgers

Insurance records (existing)

Internal audit reports

Journals

Military records

Minute books

Property appraisals and records

Retirement plan information (IRA, 401(k), etc.)

Savings bond registration

Tax returns

Training manuals

Union agreements

W-2/s/proof of income