Year-end Financial Planning: 10 Essentials To Check Off Your List

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As we near the end of the year, it's easy to get caught up in the holidays and let important steps in your financial plan lapse. However, taking a moment to reflect on your year-end finances is a vital task. Are you doing everything you can to prepare for next year, maximize your savings, and prepare for the impending gauntlet of tax season?

With so many moving parts in your portfolio, it can be hard to know where to start. Here are 10 essential things to consider as part of your year-end planning.

1. Redline Your Retirement Contributions

Time in the market is paramount. The sooner you can get your money saved and invested, the better off you'll be in retirement. When saving, be sure to make all your desired contributions by December 31st, when eligibility ends. The 2023 annual contribution limit for your 401(k) is $22,500, paired with an additional $7,500 catch-up contribution for individuals over the age of 50.

If hitting those maximum limits isn't in your budget this year, consider pushing any extra income from a year-end bonus toward your 401(k). If you received a raise, try to increase the percentage of your salary that you contribute to your 401(k) for next year. This can stave off a lifestyle creep, helping you increase savings rather than expenditures.

2. Roth Conversions

Whether a Roth conversion is right for you depends on several different factors, but the potential long-term benefits make it something worth visiting each year. Any amount converted from a Traditional Individual Retirement Account (IRA) to a Roth IRA counts towards ordinary income. Therefore, consider taking advantage of a year when you have lower taxable income by utilizing a Roth conversation to lock in low tax rates. This will allow you to enjoy tax-free growth and tax-free withdrawals on the converted amount later in retirement. Also, unlike other Traditional retirement accounts, Roth IRAs are not subject to required minimum distributions.

3. Required Minimum Distributions (RMDs)

There are two ways one might be subject to an RMD. The first and most common is that they have reached age 73 and must now begin withdrawals from qualified retirement accounts. The second is where a non-spousal beneficiary has inherited a retirement account and therefore must take distributions regardless of age. However, there are some special exceptions to this rule that you may want to dig into. The IRS requires that a specific dollar amount be withdrawn before the end of each calendar year. If this is not done, steep penalties are applied.

The end of the year is a great time to finalize a strategy for distributing these assets. Make sure you're electing appropriate withholding amounts and have a plan for how the RMD will be withdrawn. You'll have to decide if your withdrawals should be deposited in your bank account or allocated to a separate investment account. There are also unique charitable strategies that can be utilized and it's important to understand those before distributing from your retirement accounts.

4. Make Charitable Donations

Over 30% of all nonprofit giving happens during the last month of the year during the colloquially dubbed "Giving Season." While your charitable donations may be initiated by philanthropic convictions, gifting to eligible charities presents a financial opportunity for both parties. If you choose to donate, there may be significant reductions in taxable income.

However, there are more ways to donate than simply cutting a check, and some may be more impactful come tax season. Before writing that check, explore whether stock donation, Qualified Charitable Distributions, or Donor Advised Funds make sense for your circumstances. As we approach the end of the year, be sure to review your gifting strategy and complete any planned donations before December 31st. However, in some cases, it may make sense to hold onto your donations until the following year. This is called donation bunching and can be a good way to save on taxes.

5. Consider Tax-loss Harvesting

In addition to charitable donations, there are other ways to reduce your tax liability each year. One of those strategies is tax-loss harvesting. Put simply, this strategy involves selling off securities at a loss to offset capital gains. In some cases, this also may lower your taxable income. Nobody likes seeing securities lose value, but if you've accumulated losses within a taxable investment account, there's an opportunity to at least save on your overall tax liability for the year.

The end of the year is a great time to comb through your portfolio and identify any potential securities that can be sold at a loss. If you choose to sell, the loss can be used to offset capital gains in that year. Capital losses can also be held and carried over for an indefinite amount of time to use in future years. This strategy is complicated and, as with most portfolio management decisions, should never be executed in a vacuum. If you're considering this strategy, you should talk to an advisor. In some cases, tax-loss harvesting can work against you.

Important note: be aware of the IRS's Wash Sale Rule that prevents you from deducting a capital loss on a sold security if you, or your spouse, purchase similar securities in any account within 30 days before or after the sale.

6. Rebalance Your Portfolio

While portfolio management should be a constant for any investor, the end of the year presents a great opportunity to take a deeper dive and make sure your portfolio is balanced. Your portfolio isn't a set-it-and-forget-it kind of thing, and auto-investing and auto-rebalancing are oversimplifications that could have unintended consequences. Markets move, and that movement can skew the weightings of asset classes in your portfolio. Checking in and rebalancing your accounts toward your planned allocation can help shield you from undesired levels of risk.

7. Fully Fund Your HSA

We've written before about the often-overlooked strengths of Health Savings Accounts (HSAs). These accounts provide triple tax benefits - contributions are made with pre-tax dollars, earnings grow tax-free, and distributions are tax-free as long as they are used towards qualified medical expenses. While HSAs are subject to annual contribution limits, you are not required to use a certain amount per year, allowing contributions to grow over time and be taken in later years when your health expenses are higher.

The annual contribution limits for 2023 are $3,850 for individuals, $7,750 for families, and an additional $1,000 catch-up contribution for individuals over 55. Fully funding each year can set up a nice cushion in the event of high medical bills, while taking advantage of the HSA’s triple tax benefits.

If your employer deducts contributions directly from your paycheck, they will typically contribute only for the current year. However, you have the flexibility to keep adding money to your HSA for 2023 until April 15th, which is the tax deadline. But be aware that contributions from your paychecks starting in January may be assigned to your HSA for 2024.

Due to the timing of the end of the year versus the tax deadline, it's a good idea to adjust your contribution amounts to ensure your HSA is fully funded by December 31st. This way, you can make the most of your HSA and avoid unintentionally contributing to the next year.

8. Spend From Your FSA

Similar to HSAs, Flexible Spending Accounts (FSAs) are accounts that provide tax advantages, while allowing you to pay for certain healthcare costs. Where HSAs are typically used for your healthcare expenses, FSAs are most often used to pay for the health and childcare costs of dependents. Unlike HSAs, FSAs generally don’t allow account holders to carry over funds between calendar years. If you have an FSA, be sure to use any funds remaining for qualified medical and childcare expenses before the New Year when they may disappear.

9. Maximize Your Gift Allowance

The IRS allows a lifetime tax exemption on gifts and estates, up to a certain limit, which is adjusted yearly to keep pace with inflation. If you are worried that you may have significant enough assets for the estate tax to be imposed, consider gifting money to loved ones. In 2023, you can gift $17,000 ($34,000 per couple) to as many individuals as you want without the need to report the gift to the IRS.

For example, if you and your spouse wish to gift money to your child and their spouse, you can collectively gift up to $68,000. This is possible because you and your spouse together can gift up to $34,000 per person.

Gift Allowance

Parent One + Parent Two = Gift Allowance to Child
$17,000 + $17,000 = $34,000

Parent One + Parent Two = Gift Allowance to Child's Spouse
$17,000 + $17,000 = $34,000

This results in a total gift allowance to your child and their spouse of $68,000

10. Update Estate Plan

In addition to taking advantage of your gift allowance, the end of the year presents an opportunity to do some routine maintenance on your estate plan. Has anything changed in the last year? Take the time to update your beneficiary designations and review trustee appointments, power of attorney provisions, and health care directives. Even if nothing needs to be adjusted, reviewing what you've already prepared is always helpful, **especially during the holidays when families are often together**. If changes need to happen, you can have complex discussions face-to-face, show documentation, and get documents notarized easier under one roof.

The Bottom Line

The end of the year can be hectic, and it is easy to be swept up in all the excitement that comes with the holidays. Take a moment to review that you are doing everything you can to get ready for the coming year. If you're feeling overwhelmed, consider giving us a call. A trusted advisor can help you make informed decisions in your year-end planning and throughout the rest of the year, giving you more peace of mind.