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

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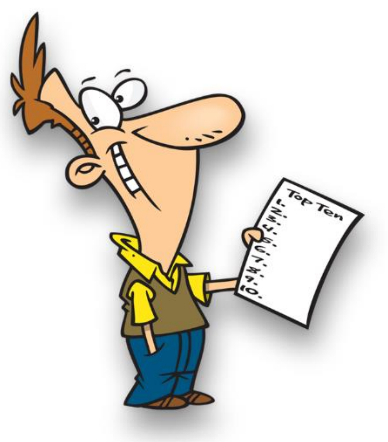

As we near the end of the year, it's easy to lose track of time and let important steps in your financial plan lapse. It is important to step back and carefully review your year-end finances. Are you doing everything you can to prepare for next year, maximize your savings, and prepare for the impending 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 longer your savings are invested, the larger your portfolio may be in retirement. When saving, be sure to make all your desired contributions by December 31st, when eligibility ends. The 2022 annual contribution limit is $20,500, paired with an additional $6,500 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 there were adjustments and changes to your income, consider reflecting those in your retirement plan contributions. Higher income should often lead to higher saving rates.

2. Complete 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 revisiting each year. Any amount converted from a traditional IRA to a Roth IRA counts towards ordinary income. Consider taking advantage of a year when you have lower taxable income by utilizing a Roth conversation to lock in those 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 (RMD)

There are two ways one might be subject to an RMD. The first and most common is that they have reached age 72 and must now begin withdrawals from qualified retirement accounts. The second is where an individual has inherited a retirement account before 2020 (these rules changed after 2019) and therefore must also take distributions regardless of age. 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 distributed. 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 a 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.

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 taxes. 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.

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 2022 are $3,650 for individuals, $7,300 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 HSAs triple tax benefits.

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

While talking about money and death doesn't exactly go hand in hand with the holidays, having an open conversation about these things now can help ensure financial legacies are carried out as intended. Where estate tax thresholds will be at this time next year, let alone at the time of one's death, is anybody's guess. 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 before passing. In 2022, you can give $16,000 ($32,000 per couple) to as many individuals as you want without the need to report the gift to the IRS. Keep in mind, the limits only apply to individuals. If you and your spouse are gifting money to a married couple, that total becomes $64,000.

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. Be sure to pause and make sure you are doing everything you can to prepare for next year as well as the years that follow. 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.