

HOW TRADERS CAN SAVE TAXES BEFORE YEAR-END

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Nov. 7, 2018 @ 12:00 pm EST
(Interactive Brokers Webinar)

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Robert Green's content

- Mr. Green is a leading authority on trader tax.
- He is the author of Green's 2018 Trader Tax Guide, which GreenTraderTax published as an annual tax guide every year since 1997. The 2018 edition discusses the Tax Cuts and Jobs Act's impact on investors, traders, and investment managers.
- Mr. Green has been a contributor to Forbes.com since 2010. Leading brokerage firms and other financial media feature Mr. Green's blog posts and Webinar content.

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Webinar description

- The 2017 Tax Cuts and Jobs Act (TCJA) made major changes in the tax rules for individuals and businesses.

  Join Robert A. Green, CPA of GreenTraderTax to learn how you can save taxes using savvy year-end planning strategies. Don’t miss the boat!

Defer income and accelerate tax deductions

- Consider the time-honored strategy of deferring income and accelerating tax deductions if you don’t expect your taxable income to decline in 2019.
- Tax rates are the same for 2019, although the IRS adjusts tax brackets for inflation each year.
- Enjoy the time-value of money with income deferral.

Traders have volatility in income

- Year-end tax planning is a challenge for traders because they have wide fluctuations in trading results, making it difficult to forecast their income.
- Those expecting to be in a lower tax bracket in 2019 should consider income deferral strategies.
- Conversely, a 2018 TTS trader with ordinary losses, hoping to be in a higher tax bracket in 2019 should consider income acceleration strategies.
- If you have trader tax status in 2018, consider accelerating trading business expenses, such as purchasing business equipment with full expensing.

Don’t assume that accelerating itemized deductions is also a smart move

- TCJA suspended and curtailed various itemized deductions, so there is no sense in expediting a non-deductible item.

- Even with the acceleration of deductible expenses, many taxpayers will be better off using the standard deduction of $24,000 married, $12,000 single, and $18,000 other taxpayers — these are roughly doubled by TCJA. There is an additional standard deduction of $1,300 for the aged or the blind.

- If itemized deductions are below the standard deduction, consider a strategy to “bunch” itemized deductions into one year and take the standard deduction in other years.

Accelerate income and defer certain deductions

- A TTS trader with substantial losses that are not subject to the capital loss limitation should consider accelerating income to soak up the business loss, instead of having an NOL carryover. TCJA repealed the two-year NOL carryback rule starting in 2018.

- Try to advance enough income to fully utilize the standard deduction and take advantage of lower tax brackets.

- Be sure to stay below the thresholds for unlocking various types of AGI-dependent deductions and credits.

Roth IRA conversion

- Consider converting a traditional IRA into a Roth IRA before year-end to accelerate income.
- The conversion income is taxable in 2018, but you avoid the 10% excise tax on early withdrawals.
- One concern is that TCJA repealed the recharacterization (reversal) option.
- There isn't an income limit for making Roth IRA conversions, whereas, there is for making contributions.

Sell winning positions

- Another way traders can accelerate income is to sell open winning positions to realize short-term capital gains.
- Consider selling long-term capital gain positions, too.
- In the bottom two ordinary tax rates of 10% and 12%, the long-term capital gains tax rate is zero.

BUSINESS EXPENSES

Business expenses

- TTS traders are entitled to deduct business expenses and home-office deductions from gross income.
- The home office deduction requires income, except for the mortgage interest and real estate portion.
- The SALT cap on state and local taxes does not apply to the home office deduction.

Business expenses

- TCJA expanded full expensing of business property; traders can deduct 100% of these costs in the year of acquisition, providing they place the item into service before year-end.
- If you have TTS in 2018, considering going on a shopping spree before Jan. 1.
- No sense deferring TTS expenses, because you cannot be sure you will qualify for TTS in 2019.

ITEMIZED DEDUCTIONS VS. STANDARD DEDUCTION

Miscellaneous itemized deductions

- TCJA suspended all “miscellaneous itemized deductions subject to the 2% floor” including investment fees and expenses, unreimbursed employee business expenses, and tax compliance fees.

- (See Investment Fees Are Not Deductible But Borrow Fees Are.)

Net investment tax

- Investment fees and expenses remain deductible for calculating net investment income for the 3.8% net investment tax (NIT) on unearned income.

- NIT only applies to individuals with net investment income (NII) and modified adjusted gross income (AGI) exceeding $200,000 (single), $250,000 (married filing jointly), or $125,000 (married filing separately).

- The IRS does not index these thresholds for inflation. (Learn more on my website.)

Retirement plans and investment fees

- If you engage outside investment advisors for managing your retirement accounts, try to pay the advisors from traditional retirement plans, but not Roth IRAs.
- An expense in a traditional tax-deferred retirement plan is equivalent to a tax-deferred deduction. (Roth IRAs are permanently tax-free, so you don't need deferred deductions in Roth plans.)
- A postponed deduction is better than a suspended itemized deduction, which is not deductible.

Retirement plans and investment fees

- Some brokerage firms might not cooperate unless you engage the firm's wealth management service.
- Consider a retirement plan custodian or intermediary who is more accommodating on these expense payments.
- Don't allow your retirement plan to pay investment fees to you, or close family members: It's self-dealing, a prohibited transaction, which might blow up your retirement plan.
- If you don't have TTS, consider trading in your retirement plan, instead of taxable accounts.

Employee business expenses

- Ask your employer if they have an “accountable plan” for reimbursing employee-business expenses.

- You must “use it or lose it” before year-end.

- TTS traders allocate a portion of tax compliance fees to TTS business expense.

Short-selling stock borrow fees

- Short-selling stock borrow fees, remain deductible under TCJA as “other miscellaneous deductions” on Schedule A (Itemized Deductions) line 28.
- If you qualify for TTS, short-selling expenses are business expenses.
- (See Investment Fees Are Not Deductible But Borrow Fees Are.)

Investment interest expense

- TCJA did not change investment-interest expense rules: This itemized deduction is limited to investment income, and the excess is carried over to the subsequent tax year(s).

- TTS traders deduct margin interest expenses on trading positions as a business expense.

- TCJA curtailed business interest expenses for larger companies only.

State and local income, sales and property taxes (SALT)

- TCJA's most contentious provision was capping state and local income, sales and property taxes (SALT) at $10,000 per year ($5,000 for married filing separately).

- Many high-tax states continue to contest the SALT cap, but they haven't prevailed in court.

- The IRS reinforced the new law by blocking various states' attempts to recast SALT payments as charitable contributions, or payroll tax as a business expense.

Estimated income taxes

- If you already reached the SALT cap, you don't need to prepay 2018 state estimated income taxes by Dec. 31, 2018.
- Pay federal and state estimated taxes owed by Jan. 15, 2019, with the balance of your tax liabilities payable by April 15, 2019.
- (You can gain six months of additional time by filing an automatic extension on time, but late-payment penalties will apply.)

Alternative minimum tax (AMT)

- In prior years, taxpayers had to figure out how much they could prepay their state without triggering alternative minimum tax (AMT) since state taxes are not deductible for AMT taxable income.

- It's easier for 2018 with SALT capped at $10,000 and because TCJA raised the AMT exemption.

- If you are subject to AMT for 2018, then don't accelerate AMT preference items.

Standard deduction

- TCJA roughly doubled the standard deduction and suspended and curtailed several itemized deductions.
- The 2018 standard deduction is $24,000 married, $12,000 single, and $18,000 other taxpayers.
- There is an additional standard deduction of $1,300 for the aged or the blind.
- Many more taxpayers will use the standard deduction for 2018, which might simplify their tax compliance work.

Keep tracking itemized deductions

- For convenience sake, some taxpayers may feel inclined to stop tracking itemized deductions because they figure they will use the standard deduction.
- Don’t overlook the impact of these deductions on state tax return where you might get some tax relief for itemizing deductions.
- Plus, certain repeals and curtailed itemized deductions might be deductible on other parts of your tax return.

20% DEDUCTION ON QBI

This deduction might be one of the most crucial TCJA changes to consider for 2018, and you should take action before year-end.

20% deduction on qualified business income

- The IRS recently issued proposed reliance regulations for the TCJA's 20% deduction on qualified business income (QBI) in pass-through entities.
- The proposed regulations confirm that traders eligible for TTS are a "specified service activity," which means if their taxable income is above an income cap, they won't get a QBI deduction.
- Hedge funds eligible for TTS and investment managers are also specified service activities.

20% deduction on qualified business income

- The taxable income (TI) cap is $415,000/$207,500 (married/other taxpayers).

- The phase-out range below the cap is $100,000/$50,000 (married/other taxpayers), in which the QBI deduction phases out for specified service activities.

- The W-2 wage and property basis limitations also apply within the phase-out range.

QBI likely includes Section 475

- QBI likely includes Section 475 ordinary income, whereas, TCJA expressly excluded capital gains and losses from it.
- (See How Traders, Hedge Funds, And Investment Managers Can Qualify For The New 20% QBI Deduction.)

Non-service businesses

- TCJA favors non-service businesses, which are not subject to an income cap.
- The W-2 wage and property basis limitations apply above the TI threshold of $315,000/$157,500 (married/other taxpayers).
- The IRS will adjust TI income cap, phase-out range, and the threshold for inflation in each subsequent year.
- Calculate QBI on an aggregate basis.

Year-end planning for QBI

- You might be able to increase the QBI deduction with smart year-end planning.

- If your taxable income falls within the phase-out range for a specified service activity, you might need wages, including officer compensation, to avoid a 50% wage limitation on the QBI deduction.

- Try to defer income to get under the TI threshold and use up less of the phase-out range.

FILING STATUS

Married couples should compare filing joint vs. separate

- Each year, married couples choose between "married filing joint" (MFJ) vs. "married filing separate" (MFS).

- TCJA fixed several inequities in filing status, including the tax brackets by making single, MFJ, and MFS brackets equivalent, except for divergence at the top rate of 37%.

- See the ordinary tax brackets: MFJ/MFS enter the top 37% rate at $600,000/$300,000 vs. $500,000 for single.

- TCJA retains the marriage penalty at the top rate only.

Married couples should compare filing joint vs. separate

- Married couples may be able to improve QBI deductions, AGI and other income-threshold dependent deductions, and credits with MFS in 2018.
- It’s wise to enter each spouse’s income, gain, loss and expense separately and have the tax software compare MFJ vs. MFS.
- In a community property state, there are special rules for allocating income between spouses.

MISCELLANEOUS CONSIDERATIONS FOR INDIVIDUALS

Estimated taxes

- Consider estimated tax payment rules including the safe-harbor exceptions.
- If you accelerate income, you may need to pay Q4 2018 estimated taxes by Jan. 15, 2019.
- Alternatively, increase tax withholding on wages to avoid estimated tax underpayment penalties.

Avoid underestimated tax penalties

- If you still need to avoid estimated tax underpayment penalties, arrange a rollover distribution from a qualified retirement plan with significant tax withholding before year-end.

- Next, roll over the gross amount into a rollover IRA. The result is zero income and avoidance of an estimated tax penalty.

Passive losses and obstacles

- Sell off passive-loss activities to unlock and utilize suspended passive-activity losses.
- The IRS has many obstacles to deferring income including passive-activity loss rules, a requirement that certain taxpayers use the accrual method of accounting and limitations on charitable contributions.
- TCJA allows more businesses to use the cash method.

Retirement and employee benefit plans

- Maximize contributions to retirement plans.
- That lowers AGI, which can unlock more of a QBI deduction, reduce net investment tax, and unlock AGI dependent benefits.
- Make sure to fund FSAs and HSAs before year-end fully.

Charitable contributions

- Consider a charitable remainder trust to bunch charitable contributions for itemizing deductions.

- Donate appreciated securities to charity: You get a charitable deduction at the FMV and avoid capital gains taxes.

Retirement and charity

- Retirees must take required minimum distributions by age 70½.
- Per TCJA, consider directing your retirement plan to make "qualified charitable distributions" (QCD).
- That satisfies the RMD rule with the equivalent of an offsetting charitable deduction, allowing you to take the standard deduction rather than itemize.

TCJA improves family tax planning

- Consider “kiddie tax” rules and the annual gift exclusion increased to $15,000 per year.
- Section 529 qualified tuition plans now can be used to also pay for tuition at an elementary or secondary public, private or religious school, up to $10,000 per year.
- The unified credit for estate tax is significantly higher at $11.18 million per person, and “step-up in basis” rules still avoid capital gains taxes on inherited appreciated property.
- TTS traders should consider hiring children as employees.

More year-end planning resources

- Webinar Dec. 5, 2018: Traders Have Unique Issues For Year-End Planning.
- Blog post: To Save Taxes, Traders Need To Deal With Unique Issues Before Year-End.
- Blog post: To Get The Most Out Of Tax Reform, Traders Need To Act Fast

CLOSING REMARKS, QUESTIONS & ANSWERS

Closing Remarks

- Thank you for attending this Webinar or watching the recording.
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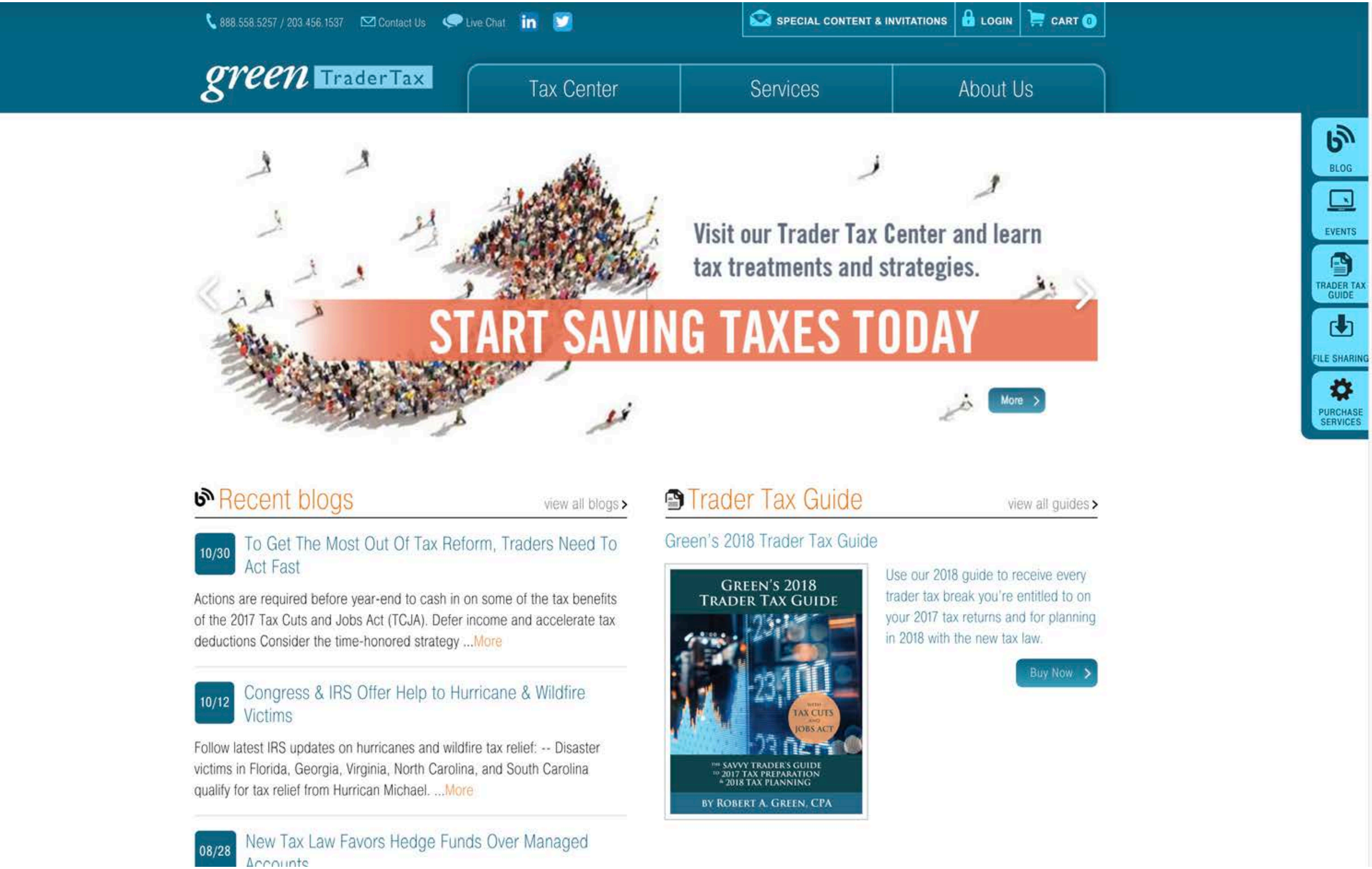
- Call us toll free at 888.558.5257 or 203.456.1537
- Email us your questions at info@greentradertax.com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