TAX PLANNING

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# Tax Considerations for 2025

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## Changes are on the way, but when?

**With the start of 2025, tax rules are similar to those in 2024. However, change is coming! The Tax Cuts and Jobs Act ("TCJA") is set to expire after December 31, 2025. Should the law expire, standard deductions will be reduced, tax rates will increase, tax brackets will be compressed, but many itemized deductions will return. To avoid this outcome, Congress must affirmatively act to change the law, which may prove difficult with the narrow majority margins in both the House and the Senate. As such, we will discuss tax considerations for both how the law is today, but also look at possible planning ideas in this year of change.**

## 2025 Income Tax Rules

Tax rates remain unchanged for 2025, but inflation adjustments have moved each threshold higher. For example, the standard deduction has increased to $15,000 for individual filers, while married taxpayers climb to $30,000[1].

The top income tax bracket stays at 37%, applying to individuals with more than $626,350 in income; $751,600 for married taxpayers. For those "in the middle," the middle tax bracket calls for a 24% rate. That rate begins at $103,350 single/$206,700 married. You need more than $197,300 single/$394,600 married to climb into the next bracket.

Of the three long-term capital gain tax rates, 0%, 15% and 20%, the most common and largest tax grouping is the 15% rate. While the 15% rate is the most common, the 20% rate is still historically low. That said, even if you fall into the 20% rate, this is still well below the 37% top marginal rate on ordinary income.

With these rates in mind, it's important to note that should the TCJA lapse, the top tax bracket will raise to 39.6%, and the middle tax bracket jumps to 28%. Standard deductions will be reduced by about half, but personal exemptions and many itemized deductions return. In short, taxes will likely increase for most.

| 2025 LT Capital Gain Tax Rates | Single | Married, Filing Jointly |
|---|---|---|
| **0%** | < $48,350 | <$96,700 |
| **15%** | $48,350 - $533,400 | $96,700 - $600,050 |
| **20%** | >$533,400 | >$600,050 |

[1] All references to "married taxpayers" will be defined as married filing jointly. An additional standard deduction applies for taxpayers who are aged 65 and older or blind.

## New SECURE 2.0 Retirement Reforms

We are now entering into the third year of retirement reforms enacted in 2022 to aid with increasing retirement savings, expanding retirement coverage and increasing access to retirement savings. Despite the slow ramp up while waiting for guidance, many highly anticipated reforms, such as "Rothification" of employer and employee contributions to workplace retirement plans, increased penalty-free access to retirement savings, and using long-term 529 savings account balances to fund a Roth IRA are now part of the landscape.

There are a few noteworthy changes that are new for 2025:

### Increased Employee Catch-Up Contribution Amounts if Aged 60-63

Most participants in workplace retirement plans, such as a 401(k), 403(b) or 457(b) plan, are familiar with catch-up contributions—the additional $7,500 in salary deferral contributions that can be made when reaching age 50. Now, some participants can save even more with a new special catch-up contribution. For 2025, the special catch-up contribution limit is $11,250 (instead of $7,500) for participants who are aged 60, 61, 62 or 63. For SIMPLE plan participants, the regular catch-up contribution limit is $3,500, while the special catch-up contribution limit is $5,250. These new special catch-up contributions will be subject to cost-of-living adjustments in the future.

### Mandatory Automatic Enrollment and Escalation for Certain New 401(k) and 403(b) Plans

All 401(k) and 403(b) plans that were established after 2022, must now include automatic enrollment of eligible employees and automatic escalation of salary deferral contributions in their plans beginning in 2025, unless an exception applies. For new participants, a minimum salary deferral rate can be set by the employer anywhere from 3% of pay to 10% of pay. For existing participants, an automatic contribution escalation rate of 1% per year will apply at least until the rate reaches 10% (but not more than 15%). These changes should help improve retirement savings. Employees always have the ability to opt out of the automatic enrollment or escalation features. SIMPLE plans, employers with less than 10 employees, new businesses that have been in existence less than three years, and plans that were established prior to 2023 are not required to include these new features.

## Final SECURE Act Guidance Impacts Certain RMDs in 2025

Long-awaited guidance regarding the 10-year rule for inherited retirement accounts may impact required minimum distributions (RMDs) in 2025 for certain non-spouse beneficiaries. In 2022, we got a glimpse of how the IRS would interpret the 10-year rule when they issued proposed regulations. In July 2024, they finalized those regulations with limited modifications to the proposed rules. Below are a few of the highlights.

For any non-spouse beneficiary subject to the 10-year rule, the final rules confirm:

- If the new beneficiary inherited a retirement account from someone who was already receiving RMDs at the time of death, they must also continue to receive annual RMDs in years one through nine, in addition to making the final distribution in year 10. This is referred to as the "at least as rapidly" rule.
- There will be no extension of the automatic waiver of the excise tax penalty for missed RMDs under the 10-year rule that has applied since 2021. For tax years 2021-2024, no penalty applied if a beneficiary failed to take an RMD that would have been required due to the "at least as rapidly" rule.
- There will be no extension of time for applying the 10-year rule. For example, if the account owner died in 2020, the final distribution will be required by the end of 2030—the year containing the 10th anniversary of the account owner's death.

In addition, there are two new RMD rules that apply for year-of-death distributions:

- Any beneficiary can now take the decedent's year-of-death RMD—it doesn't have to be shared by all beneficiaries on a pro-rata basis.
- An automatic waiver of the missed RMD excise tax penalty will apply for any year-of-death distribution that a beneficiary failed to take in the year of death, as long as the beneficiary receives the RMD by their tax filing deadline (including extensions) for the tax year of the account owner's death, or by the end of the following year.

## Consider Planning for the 2026 Reversion of Tax Laws

We know that the tax laws will change by the end of 2025. Either the TCJA will lapse as scheduled, or Congress will affirmatively act to change the law in some way. Since the election in November, many articles have been published claiming that the sunset will not occur because of the "Red Wave" in Congress and the White House. However, given the fact that Congress must affirmatively act to change the law, questions remain. Congress often struggles to proactively address such issues, and many times only addresses tax issues at the last minute.

Another factor affecting any change in the law is that the rules traditionally require 60 affirmative votes in the Senate, which seems unlikely. What is more likely is that Congress will use the "reconciliation" rules to pass any new tax laws, which is what was used to pass the TCJA. The reconciliation process only requires a majority of the Senate to pass new law, but the bill must either pay for itself or must lapse within 10 years (which is what is forcing the changes in 2026). Calculating these numbers can be very confusing, but many agree it will take a huge reduction in spending (probably north of $4 trillion) to use reconciliation again.

Should the reversion occur as scheduled, many planning opportunities may take a long time to implement, so here are a few items to consider today in anticipation of the reversion taking place:

### Standard Deductions Will Be Halved While Many Itemized Deductions Return

The TCJA doubled the standard deduction, limited state and local tax deductions, eliminated most other deductions and the personal exemption. The return of the lower standard deduction, coupled with the availability of renewed personal exemption and itemized deductions, will greatly affect many taxpayers, with most likely to see higher tax liabilities. Work with your tax advisor to determine if you should shift income or delay deductions in preparation of the tax law reversion.

### Tax Rates Increase

The tax rates will generally increase for everyone. The “middle” bracket will increase from 24% to 28%, and the top tax bracket will increase from 37% to 39.6%. Again, consider whether it may be more advantageous to accelerate income or defer deductions to address these tax increases. For example, Roth conversions may be more attractive this year because income tax on the converted amounts would be taxable at current lower tax rates while future qualified withdrawals in retirement would be income tax free when tax rates could be higher.

### While Deductions Return, So Too May the AMT

Should tax law reversion occur, limitations on the state and local tax deductions depart as well. Deductions like those for personal casualty losses, or miscellaneous deductions subject to the 2% floor, for example, return in 2026. However, the Alternative Minimum Tax (AMT) thresholds also revert to their 2017 lower numbers. The AMT was designed to make sure wealthy taxpayers paid their “fair share” of taxes.

Accordingly, individuals with high income, high deductions, stock options or with large capital gains may once again face the AMT. Review whether you can increase income or realize long-term capital gains now. Moreover, controlling or decreasing your AGI going forward may help reduce the chance of facing the AMT in 2026 and beyond.

### Estate and Gift Tax Exclusions are Reduced by Half

The elevated estate and gift tax exclusions, $13.99 million in 2025, are also scheduled to be cut in half. Note, however, the annual gift exclusion, which increases to $19,000 per person per year for 2025, will not be affected by the expiration of the TCJA. That said, for high-net-worth clients, consider planning to utilize the large exclusions now. Techniques like accelerated gifting, Spousal Lifetime Access Trusts, or other wealth transfer strategies may be appropriate to reduce your total transfer tax liability.

## Ongoing Considerations

While the new retirement savings rules may provide new opportunities, traditional planning can still help manage your tax situation. Discuss with your tax advisor whether one or more of the following actions could be beneficial for your specific situation:

### Itemize or Not?

Should you itemize or use the standard deduction this year? With the higher standard deduction, coupled with limited itemized deductions, you may need to review tax planning opportunities for 2025. Ideas like bunching or delaying expenses or gifts, like medical expenses or charitable gifts, along with taking or deferring gains or losses where possible, may benefit you more depending on the fate of the TCJA.

### For Higher Income Earners: Be Mindful of Those Taxes That Do Not Index

Recall that the Affordable Care Act implemented a 0.9% Medicare Health Insurance Surtax and a 3.8% Net Investment Income Tax for individuals earning more than $200,000 and married couples earning more than $250,000. The 0.9% surtax is levied on earned income, and the 3.8% Net Investment Income Tax applies to passive earnings like interest, dividends, capital gains, etc.

Neither of these thresholds index for inflation. Consequently, if your income has increased, you may become subject to these taxes. These numbers will not be affected by a lapse of the TCJA, but they may become a bargaining chip should Congress look to proactively address the tax code. If you may be subject to these additional taxes, be sure to review your estimated income and adjust your payroll exemptions accordingly. You should also review your portfolio to determine whether your investment decisions may subject you to these surtaxes.

### Higher-Income Earners Should Also Review Medicare IRMAA Limits

Receiving a high income when you are age 65 or older can have unexpected implications when it comes to Medicare premiums. While your financial plan should include an allocation for healthcare expense in retirement, many forget to include the impact of the “Income-Related Monthly Adjustment Amount” or IRMAA. IRMAA is a surcharge that is added to Medicare Part B and Part D premiums. This extra cost you pay on top of the Medicare standard premiums impacts individuals with a modified adjusted gross income (MAGI) greater than $106,000 and married couples with a MAGI greater than $212,000. The premium surcharge is capped for MAGIs above $500,000 for individuals and $750,000 for married couples. Because the additional premiums can significantly impact your Medicare costs, managing your income and taking appropriate steps to control your MAGI can help you reduce or avoid future IRMAA surcharges. Your MAGI from this year will impact your Medicare premiums two years from now. As an example, your MAGI from your 2025 income tax return determines your Medicare premiums in 2027.

### Review Your Gift and/or Estate Planning Situation

With the larger $13.99 million exclusion in 2025, you want to make sure your existing plan meets your legacy goals, as many plans divide assets based on the applicable exclusion amount.

The annual gift tax exclusion amount also increases in 2025 from $18,000 to $19,000 per person per year (or $38,000 if you are married). This is the fourth year in a row the annual exclusion

has increased, which is unprecedented. The increase in the gift limit also allows more impactful funding of 529 Education Savings Plans. For individuals looking to use the five-year advance gifting available for 529 plans, that's $95,000 per individual ($190,000 for a married couple).

## Explore Retirement Savings Opportunities

Consider fully funding your employer-sponsored plans and/or tax-deductible IRAs. Maximizing these contributions may lower your tax bracket. Below are the contribution limits that are in place for this year.

Employee salary deferral contribution limits for 401(k)s, 403(b)s and governmental 457(b) plans increased to $23,500. The base catch-up contribution for individuals aged 50 or older remains at $7,500. For individuals aged 60-63, the special catch-up contribution limit is $11,250.

For SIMPLE IRAs, the standard employee salary deferral limit increased to $16,500, while for SIMPLE IRAs with no more than 25 employees, the salary deferral limit is $17,600. SIMPLE IRA catch-up contributions remain at $3,500 unless your plan covers no more than 25 employees, in which case it increases to $3,850. The special catch-up contribution limit for individuals aged 60 – 63 is $5,250.

Traditional and Roth IRA contributions remain at $7,000 (plus an additional $1,000 for individuals aged 50 or older). Individuals can contribute to a traditional IRA if they (or their spouse, if married) have earned income. To make Roth IRA contributions, in addition to the earned income requirement, you must also fall below modified AGI limits.

## QCDs Can Reduce Tax Impact of RMDs

If you are age 70½ or older and are charitably inclined, tax-free qualified charitable distributions (QCDs) can be a great way to satisfy your charitable giving from your IRA without increasing your taxable income. In 2025, the annual QCD gift limit increased to $108,000. A one-time QCD can also be made to a split-interest entity of up to $54,000.

QCDs can only be made by individuals who are at least age 70½ (six months past your 70th birthday), even if your RMD start age is later, and are income tax free—even if you are using the standard deduction and do not itemize. If you are aged 73 or older or have a beneficiary IRA with an RMD, QCDs also count toward your RMD, but are not limited to the amount of the RMD if less than the limits described above. Keep in mind that if you have also made deductible IRA contributions after the age of 70½, you must adjust the amount of the tax-free QCD by the aggregate amount of your deductible IRA contributions.

### Roth Savings Can Provide Tax Diversification in Retirement

Roth retirement planning options are also a strategy to consider, whether you save through annual Roth IRA contributions, through Roth features in your workplace retirement plan or by converting existing pre-tax retirement savings to Roth. The tax-free nature of Roth IRA qualified distributions is a way to provide more after-tax cash flow during retirement and a way to manage AGI. In turn, that can impact the taxation of Social Security benefits you receive and the Medicare premiums you pay. Roths also may be a more beneficial way to transfer wealth now that distributions for most non-spouse beneficiaries are limited to 10 years.

While Roth IRAs are subject to modified AGI limits, contributing to Roth accounts through a workplace retirement plan, if your employer makes them available to you, has no income restriction.

Converting existing pre-tax retirement assets to a Roth IRA does create taxable income in the year you convert. With the current income tax rates expected to revert to higher rates in 2026, converting now can take advantage of lower tax rates. A conversion cannot be undone, so consider the tax consequences carefully before acting.

### Consider the Benefits of Life Insurance

If you have a large traditional IRA or 401(k) and you are concerned about the taxes your heirs will have to pay after your death, adding permanent life insurance as part of your legacy plan may also be a strategy to consider. Upon the death of an insured person, life insurance provides a leveraged income tax-death benefit as a lump-sum for beneficiaries. In addition, some policies offer an option to pay out the death benefit over time for any long-term care expenses, income tax-free. Keep in mind that to purchase life insurance you must be able to qualify via medical underwriting with an insurance company.

## Work With Your Tax Professional and Your Financial Advisor

We know change is coming this year, whether that change is passive with the TCJA lapsing, or whether Congress passes new tax laws. While the old saying of “Don’t let the tax tail wag the dog” still applies to your long-term investment goals, this year the tail may have a little more influence. Accordingly, plan on working closely with your tax professional and your financial advisor to address your specific situation and seek the most flexibility possible to meet your goals. ■