

## The Newsletter

I had hoped to bring you a summary of Trump's tax law changes and/or updates, but much remains unsettled. So, I will wait to see if it becomes clearer in the summer. For now, here are a few items that you may find interesting and educational.

### **Alert: California, Illinois, and New York Laws Require Written Freelance Agreements**

If your business hires freelance workers—also known as independent contractors—you need to be aware of new laws now in effect in California, Illinois, and New York. These laws are designed to protect freelancers by requiring written contracts and prompt payment.

#### **What's New?**

These states have enacted freelance worker protection acts in response to widespread concerns from freelancers about late or missing payments. The laws apply to most private businesses, regardless of size, that hire freelancers located in or providing services in one of the three states.

#### **Key Requirements**

If you pay a freelance worker more than a threshold amount—\$250 in California, \$500 in Illinois, or \$800 in New York (within a 120-day period)—you must use a written agreement that includes the following:

- Names and addresses of both parties
- Description and value of the services
- Rate and method of compensation
- Payment due date (or how it will be determined)
- Date by which the freelancer must submit a service record for processing

You may use paper or electronic contracts, but you must keep a copy for two to six years, depending on the state.

#### **Who Is Covered?**

These laws apply only to freelancers—typically one-owner independent businesses. California's law applies only to freelancers in specified professions (e.g., writers, designers, appraisers), and Illinois excludes entities like LLCs and corporations.

#### **Penalties for Non-compliance**

Failure to pay a freelancer or to provide a proper contract can lead to double damages, attorney fees, and statutory penalties—up to \$1,000 per violation in some cases. New York may impose fines of up to \$25,000 for repeated violations.

## What You Should Do

- Use a compliant freelance agreement.
- Pay freelancers on time.
- Document performance issues carefully if withholding payment.
- Avoid retaliation against freelancers who assert their rights.

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## Beat the Estimated Tax Penalty with Strategic Withholding

If you're making quarterly estimated tax payments, missing a deadline can be costly. The IRS currently charges a 7 percent penalty for underpayments—and since penalties aren't deductible, the real cost can feel closer to 11 percent.

But here's good news: strategic withholding can often help you avoid or erase those penalties—even late in the year.

Here's why: while estimated tax payments are due on set dates (April 15, June 16, September 15, and January 15), withholding is treated differently. The IRS considers tax withheld from W-2 wages or IRA distributions as if paid evenly across all four quarters—or on the actual date withheld, if you so choose.

This means that if you're short on estimated payments for the year, you may still have options:

- Have your S or C corporation pay you a year-end bonus and withhold additional taxes (though be mindful of added payroll taxes).

- Adjust withholding from a W-2 job, and document the timing for quarterly allocation or direct identification.
- Use an IRA “rollover and replace” strategy: take a distribution, withhold 100 percent for taxes, then redeposit the funds within 60 days to avoid tax on the withdrawal.

Each of the methods can help you meet IRS safe harbor rules and avoid penalties—often with more flexibility than standard estimated tax payments.

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## Backdoor Roth IRA Conversions: Smart Move or Hidden Tax Trap?

If you've ever wondered how to get more money into a Roth IRA despite income limits, the backdoor Roth IRA conversion strategy may have caught your attention. It's a smart planning tool for high-income earners—but only when used with care.

First, a quick refresher: Roth IRAs offer two powerful benefits—tax-free withdrawals in retirement (if you meet certain conditions) and no required minimum distributions during your lifetime. These features make Roth IRAs excellent for retirement income planning and for long-term wealth transfer to heirs.

Unfortunately, direct contributions to a Roth IRA are phased out at higher income levels—\$236,000 to \$246,000 for joint filers and \$150,000 to \$165,000 for single filers in 2025. That's where the backdoor Roth comes in.

Here's how it works: You make a non-deductible contribution to a traditional IRA, then convert that amount into a Roth IRA. If you have no other traditional IRAs, this strategy can be a clean, tax-free move.

However—and this is key—if you have other traditional IRAs (including a SEP or SIMPLE IRA), the IRS looks at all of them when determining the taxable portion of your conversion. This can result in unexpected taxable income on the conversion. In other words, what appears to be a simple “tax-free” conversion could surprise you with a tax bill if you're not careful.

Before you make a move, it's essential to review your entire IRA picture. In some cases, consolidating or converting other IRAs first can help set the stage for more tax-efficient backdoor conversions down the line.

**Bottom line:** A backdoor Roth IRA conversion can be a powerful tool, but it's not a one-size-fits-all solution.

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## Solo Biz Owner? No Employees? Is the Mega Backdoor Roth for You?

If you are a business owner with no employees and prefer Roth-style retirement savings, you may want to consider the mega backdoor Roth strategy.

This powerful tool allows you to contribute significantly more to a Roth account than the standard Roth IRA or even the regular backdoor Roth route—up to \$70,000, or \$77,500 if you're age 50 or older.

Compare that to the regular backdoor Roth limit of \$7,000 (\$8,000 with the age 50-plus catch-up), and you'll see why the “mega” title fits.

Here's the basic idea: You set up a solo 401(k) plan that permits two key features—after-tax contributions and either in-service withdrawals or in-plan Roth conversions. These elements are essential to make the mega backdoor Roth work seamlessly.

Once your plan is in place, you contribute through a combination of

- elective Roth contributions (up to \$23,500, or \$31,000 if you're age 50 or older), and
- voluntary after-tax contributions (up to \$46,500 in 2025, depending on your plan design and income).

From there, you either roll the after-tax funds into a Roth IRA or convert them inside the solo 401(k) to Roth status.

The benefits of Roth accounts are compelling: tax-free growth, no required minimum distributions, and more flexible estate planning options. Your heirs can inherit Roth funds income-tax-free, although non-spouse beneficiaries must withdraw the funds within 10 years.

While the after-tax value of Roth versus traditional contributions can be similar under constant tax rates, the Roth still offers more control and flexibility—especially valuable if you expect tax rates to rise or want to simplify distributions in retirement.

**Bottom line:** If you are self-employed, own a corporation, or are a partner in a partnership with no full-time employees, the

mega backdoor Roth could be a high-impact retirement strategy.

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## **Beat the Taxman: Use the Tax Code–Created QCD to Kill Your RMD**

If you have one or more traditional IRAs and are age 73 or older, you're probably familiar with three of the most dreaded letters in the tax world: RMD, short for *required minimum distribution*.

Starting the year you turn 73, the IRS requires you to withdraw a certain amount from your traditional IRAs annually. This amount is based on your age and increases as you get older.

RMDs are taxable income, which is precisely why many retirees dread them. But if you're charitably inclined, there's a powerful way to meet your RMD requirement without increasing your taxable income: the qualified charitable distribution, or QCD.

With a QCD, you direct money from your IRA straight to a qualified charity. That amount counts toward your RMD for the year—but it doesn't count as taxable income to you.

Even better, you can use a QCD whether or not you itemize deductions, so you can still benefit from charitable giving on your tax return.

A QCD can help you

- satisfy all or part of your RMD for the year;
- support the charities you care about;
- avoid reporting the RMD as taxable income; and
- reduce the risk of being pushed into a higher tax bracket.

While RMDs don't start until age 73, you can make QCDs when you turn 70 1/2.

The annual QCD limit is generous: up to \$108,000 per person per year. For married couples filing jointly, each spouse can make a QCD of up to \$108,000 from their own IRA, for a combined total of \$216,000 for 2025.

The QCD must go to a Section 501(c)(3) charity—such as a church, school, or other non-profit organization. You cannot make QCDs to donor-advised funds or private foundations.

Your best choice is to have your IRA trustee transfer the QCD directly from your IRA to the charity. Also, make sure you get a written acknowledgment from the charity for your records.

Make the QCD first if you plan to take multiple withdrawals from your IRA during the year. The IRS treats your first withdrawal as your RMD, so taking the QCD first ensures it counts toward your RMD.

And most important, don't forget to let your tax preparer (us) know you made a QCD. We need to report it correctly on your tax return.

As always, please let me know if you have any questions or wish to discuss anything in this newsletter.

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