

Hons Tax Associates August 2021 Newsletter

Hi all

I am sure you are glad you don't have to think taxes these days!

Most of you who received unemployment benefits and filed before the tax law changed (first \$10,200 of unemployment benefits not federally taxed) have by now received from IRS your extra refund. A few still have not. If it is your case, all you can do is wait. IRS processed the simple returns first, the more involved returns after.

If you have children and normally get child tax credit, you should have received your first monthly direct deposit or check from IRS (\$300 per child under 7, \$250 per child under 18 or less if your child tax credit is partially phased out). These payments will be for 6 months to half of the total child tax credit.

At tax time I will ask you how much you got (to input in tax return). IRS is supposed to send taxpayers a letter early next year showing how much they paid, but it would be prudent to keep track of it yourselves. It is very likely an incorrect amount input in the return would delay your refund.

Tax planning may be useful to you

Below are a few situations when tax planning can be useful and often save tax.

. **Structure of your small business:** filing as a schedule C (including for one member LLCs) is usually OK as long as your net profit is not too high (usually below 50 to 75k, depending on many factors). Above that you can save self-employment tax (with little decrease in your future Social Security retirement) by filing as an S Corp, which requires a filing with IRS, often a filing with CO SOS, bookkeeping, salary (payroll) to the owner, and an S Corp return (\$600 or so if no complications and no more than 2 shareholders)

. **Retirement year:** It is difficult to plan the tax aspects of a retirement year because of the many changes involved and the unknown of some aspects of them. A physical move certainly compounds things (and States taxes can be very different). Many people end up having to pay an unexpected large tax bill at tax time when the tax bill could have been lowered (spreading the income to further years with usually a lower tax rate), the withholdings for a severance package and/or retirement distribution be estimated, and/or quarterly payments made.

. **Capital gains:** unexpected or large capital gains can have many effects on your taxes, some unanticipated by most people. Below are the main usual possible effects or issues:

- Capital gain taxes (for larger amount, larger income, see below)
- Social Security benefits (for both when filing married) taxed to the maximum (85% taxed) because of the higher income
- Net Investment Tax (3.8%) kicking in

- Being phased out of credits and deduction you usually get (college education children, EIC, student loans interest)
- Diminished allowed contributions to traditional and Roth IRA (and excess contributions can be messy to fix)
- Larger capital gain than expected when selling a rental which has been depreciated for many years (with also a 25% tax rate applying on the "unrecaptured section 1250 depreciation")
- Issue finding the basis of what was sold, when received long time ago (especially if gifted) and/or changes of financial institutions

. **Selling Employee Stock options.** IRS distinguishes statutory and non-statutory options with different rules for tax, and this can get confusing to most people. In any case if the stock went up from the granting and/or exercise price, there will be tax to pay, which can include tax on both ordinary income and capital gains. Often an adjustment to the basis needs to be done for tax reporting when the ordinary income part of the option exercising has been reported in the W2. Usual possible tax effects, if sizeable amounts, are about the same than the ones listed above for capital gains.

. **Real Estate:** Below are usual questions I can be of help for:

- is it a good time for tax to sell a rental, should a 1031 exchange be considered?
- Do I get the full capital gain exclusion if I sell my home? What about the second home/property I have?
- What are the tax implications of the above, can we run different scenarios?
- My ex stayed in the home we still own together; do I get the full exclusion on my share when sold?

Tax answers require tax knowledge and do not always follow common sense.

If you have one of the above situations, I can help. There will be a fee for it, but it would be small if a simple situation, and I would limit it to a maximum 25% of the net taxes I would save you (and show you) in a more complex situation.

Capital gains

Below are the current (2020) capital gain rates. These apply to the long term capital gains depending on the full taxable income (including the capital gains) indicated in the table. Please re-read above and see examples below if you are not familiar with the way it applies but want to fully understand it. It can be confusing. For example:

- . you are married, your total taxable income is 79,000 of which 20,000 capital gain: this capital gain will not be taxed. The remaining \$59,000 will be taxed at ordinary tax rate.
- . you are married, your total taxable income is \$500,000, of which \$200,000 capital gain: most of this capital gain will be taxed at 15% and a bit at 20%
- . you are married, your total taxable income is \$1,000,000 of which \$500,000 capital gain: all the capital gain will be taxed at 20%.
- . add to above the Net Investment Tax applying on the lower of investment income only (when income above \$250,000) and income above \$250,000 (check form 8960, this can also be confusing)

Below are the 2020 Long Term Capital Gain tax brackets

Rate	Single income	Married filing jointly
0%	Less than \$40,000	Less than \$80,000
15%	\$40,000 to \$441,450	\$80,000 to \$496,000
20%	More than \$441,450	More than \$496,000
+3.8% NIIT	More than \$200,000	More than \$250,000

Under the American Families Plan, which could be voted soon and for which we don't know when it would apply, could be retroactively for all 2021 (unlikely), starting in 2022, or starting at a given date in 2021, the current capital gain tax rate schedule would be kept (including the Net Investment Income Tax at 3.8%), but the top capital gain rate would increase to the equivalent of the ordinary income tax rate: 39.6% for taxpayers earning over \$1,000,000

This would be a very large difference for high earners with different tax strategies possible but depending on the exact law as it would be passed and date of application, both still unknown.

IP PIN and how to sign up for it

An IP PIN (Identity Protection Personal Identification Number) is a 6 digits number given by IRS in January (different number each year) to the taxpayer via mail. This IP PIN needs to be input in the electronic tax return to prove to IRS it is the "real you" filing, and in the case your identity was compromised, or you were subject to tax identity fraud before (fraudulent tax return filed at your name by others).

If IRS has you on file with an IP PIN and it is not in the return, the electronic return will be rejected by IRS computers and you will either have to find your IP PIN or file paper. This happens to people who moved/did not forward their mail and are not always able then to get their IP PIN as IRS, to give it again, asks quite a bit of info that not all are able to get.

The situation has improved in the last 5 years with less people being affected by tax identity theft, but it is a very unpleasant experience if it happens to you.

This IP PIN is given by IRS months after you file with them a "identity theft affidavit" (form 14039), or one can request one online as a preventative measure. The IRS says that those with secure Internet access should first consider the Get an IP PIN tool on IRS.gov. Users will need to have some personal information at hand when registering:

- *Email address*
- *Social Security Number (SSN) or Individual Tax Identification Number (ITIN)*
- *Tax filing status and mailing address*
- *One financial account number linked to your name:*
 - *Credit card – **last 8 digits** (no American Express, debit or corporate cards) or*
 - *Student loan – (Enter the student loan account number provided on your statement) or*
 - *Mortgage or home equity loan or Home equity line of credit (HELOC) or*
 - *Auto loan*
- *Mobile phone linked to your name (for faster registration) or ability to [receive an activation code by mail](#)*