No ~ Nonsense Tax Tips

Finally, the COVID Relief Package Is Law

Article Highlights

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After several months of the Republicans and Democrats not being able to agree on additional COVID-related tax relief and other matters, as 2020 was coming to an end, horses were traded, and deals were made so that Congress could put together the much-needed legislation. The result is a nearly 5,600-page omnibus bill, the Consolidated Appropriations Act, 2021, Included in that legislation are the "COVID-Related Tax Relief Act of 2020" (COVIDTRA) and the "Taxpayer Certainty and Disaster Tax Relief Act of 2020". The bill was signed by the President on December 27.

This article provides an overview of the many tax provisions included in the legislation, including the 2nd round of economic impact payments, another round of targeted PPP loans for businesses, favorable tax treatment of expenses paid with forgiven loan proceeds, temporary expanded deduction for business meals, and modifications to charitable contributions—along with an excess of 30 new, altered, and extended tax provisions.

Additional 2020 Recovery Rebates

An additional round of economic impact payments (EIPs) is included in the legislation but the amount is substantially less than the first round, which was $1,200 per eligible adult and $500 per dependent child under age 17. This new round will be $600 per eligible adult and $600 per dependent child under 17. Also, eligible this time are the so-called mixed-status households, for example where one of the spouses is a noncitizen, which were previously excluded from receiving payments.

Maximum Payment Amounts:

- Each eligible adult: $600
- Married couple (both eligible) filing jointly: $1,200
- Each dependent child under age 17: $600

Payment Phaseout – The payment is phased out by 5% of the taxpayer's 2019 AGI that exceeds the filing status threshold.

CREDIT PHASEOUT THRESHOLD	
Filing Status	Threshold
Unmarried Taxpayers (as well as Married Filing Separately)	$75,000
Head of Household	$112,500
Married Taxpayers Filing Joint & SS	$150,000

Payment Due Date - Although the Act includes a January 15, 2021 deadline for advance payments to be made, President Trump's delay in signing the bill may delay the payments.

No Social Security Number - In general, taxpayers without an eligible Social Security number are not eligible for the payment. However, married taxpayers filing jointly, and otherwise eligible, where one spouse has a Social Security Number and one spouse does not are eligible for a payment of $600, in addition to $600 per child under age 17 with a Social Security Number.

Deceased Taxpayers – There was considerable confusion related to the first round when the IRS issued EIPs to deceased individuals. This time around they have specified that anyone that was deceased before January 1, 2020 is not eligible for an EIP.

The payments will be treated as a refundable 2020 tax credit and reconciled to the correct amount on the 2020 return. Any excess payment will not be required to be repaid and if the payment was less than qualified for, the difference will be paid as a refundable credit when the 2020 return is filed.

Paycheck Protection Program (PPP) Loans & Small Business Support

The legislation includes over $300 billion for first and second forgivable PPP loans. Unlike the prior loan program, this round will truly be limited to small businesses that incurred a loss of revenue. Eligibility is limited to:

- Businesses with 300 or fewer employees that have sustained a 25% revenue loss in any quarter of 2020 as compared with the same period in 2019.
- Small 501(c)(6) organizations that are not lobbying organizations and that have 150 employees or fewer, such as local chambers of commerce, economic development organizations, and tourism offices.
- Certain 501(c)(6) nonprofits and Destination Marketing Organizations with 300 or fewer employees that do not receive more than 15 percent of their revenue from lobbying.
- Local newspapers and T.V. and radio stations previously made ineligible by their affiliation with other stations.

Forgivable Expenses – will be expanded to include covered (COVIDTRA Sec 304):

- Payroll costs – Including additional group insurance payments, including vision, dental, disability and life insurance.
- Operational Costs
- Property Damage Costs
- Supplier costs on existing contracts and purchase orders, including the cost for perishable goods at any time.
- Investments in facility modifications and personal protective equipment needed to operate safely and technology operations expenditures.

The term 'covered supplier cost' - Means an expenditure made by an entity to a supplier of goods for the supply of goods that —

- Are essential to the operations of the entity at the time at which the expenditure is made; and
- Is made pursuant to a contract, order, or purchase order—
    - In effect at any time before the covered period or
    - With respect to perishable goods.

The term 'covered worker protection expenditure'— Means an operating or a capital expenditure to facilitate the adaptation of the business activities of an entity to comply with requirements established or guidance issued by Federal, State and local governments during the period beginning on March 1, 2020 and ending the date on which, the national emergency related to COVID-19 declared by the President expires. NOTE: The legislation includes a long list of examples of what does and does not apply.

The term 'covered operations expenditure' - Means a payment for any business software or cloud computing service that facilitates business operations, product or service delivery, the processing, payment, or tracking of payroll expenses, human resources, sales and billing functions, or accounting or tracking of supplies, inventory, records and expenses.

The term 'covered property damage cost' - means a cost related to property damage and vandalism or looting due to public disturbances that occurred during 2020 that was not covered by insurance or other compensation.

Loan Size - Establishes a maximum loan size of 2.5 times the average monthly payroll costs, up to $2 million.

- Allows small businesses assigned to the industry NAICS code 72 (Accommodation and Food Services) to receive PPP second draw loans equal to 3.5 times their average monthly payroll costs in order to help these businesses combat onerous State and local restrictions.
- Maintains existing expansions in eligibility for businesses assigned to the industry NAICS code 72 (Accommodation and Food Services).

Loan Forgiveness – Full loan forgiveness is available if the borrower spends at least 60% of the second draw on payroll costs over either an 8-week or 24-week period selected by the borrower.

Simplified Loan Forgiveness - The loan forgiveness process is simplified for borrowers with PPP loans of $150,000 or less. (This means another version of the SBA's loan forgiveness application form will be forthcoming.)

Churches and Religious Organizations – Are eligible for loans and prevents future administrations from making them ineligible.

Planned Parenthood – Is ineligible

Set-Asides - $41 billion is set aside to ensure that smaller borrowers and under-served communities get the help they need, such as:

- Small businesses with 10 or fewer employees,
- Small community lenders,
- Independent live venue operators, including eligible independent movie theaters and museums, affected by COVID-19 stay-at-home orders.

Clarification of Tax Treatment of Covered Loan Forgiveness Expenses

The CARES Act provides that a recipient of a PPP loan may use the loan proceeds to pay payroll costs, certain employee benefits relating to healthcare, interest on mortgage obligations, rent, utilities, and interest on any other existing debt obligations. If a PPP loan recipient uses their PPP loan to pay those costs, they can have their loan forgiven in an amount equal to those costs. PPP loan forgiveness doesn't give rise to taxable income and the Code generally doesn't allow a taxpayer to deduct expenses that are paid with tax exempt income.

The IRS had issued a ruling essentially saying that since businesses aren't taxed on the proceeds of a forgiven PPP loan, the expenses aren't deductible. However, members of Congress have been saying all along that was not the Congressional intent.

In a rebuttal to the IRS, Congress made it crystal clear in the Act that taxpayers whose PPP loans are forgiven are allowed deductions for otherwise deductible expenses paid with the proceeds of a PPP loan, and that the tax basis and other attributes of the borrower's assets will not be reduced as a result of the loan forgiveness.

Business Meals

The Tax Cuts and Jobs Act of 2017 (TCJA) eliminated the deduction for entertainment and curtailed the expense deduction for meals. In a very business friendly transitional guidance (Notice 2018-76) on the deductibility of business meals, the IRS announced that taxpayers generally may continue to deduct the food and beverage expenses associated with operating their trade or business. Under this notice, taxpayers may deduct 50% of an otherwise allowable business meal expense.

Under Sec 210 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020, for 2021 and 2022, taxpayers will be able to deduct 100% of business meal expenses where the food or beverages is provided by a restaurant, provided:

- The expense is an ordinary and necessary expense paid or incurred during the taxable year in carrying on any trade or business.
- The expense is not lavish or extravagant under the circumstances.
- The taxpayer, or an employee of the taxpayer, is present at the furnishing of the food or beverages.
- The food and beverages are provided to a current or potential business customer, client, consultant, or similar business contact. Final regulation 1.274-12(b)(3) defines "business associate" as a "person with whom the taxpayer could reasonably expect to engage or deal in the active conduct of the taxpayer's trade or business such as the taxpayer's customer, client, supplier, employee, agent, partner, or professional adviser, whether established or prospective.

Educator Expense

The Act specifies that the $250 above-the-line educator expense deduction shall include personal protective equipment (PPE), disinfectant, and other supplies used for the prevention of the spread of COVID-19 effective for expenditures after March 12, 2020.

Unemployment Assistance

All Federal supplemental unemployment insurance benefits, which had already expired or would end on December 31, 2020, will be extended through March 14, 2021. However, the supplemental amount will only be $300 per week instead of the $600 that the CARES Act authorized.

Earned Income Tax Credit (EITC) & Child Tax Credit (CTC)

These credits are based upon earned income. Because families may have had reduced income during 2020 that would adversely affect the amount of these credits, the legislation allows the 2019 earned income to be used to compute the credits for 2020. However, this affects the computation of the EITC and CTC only and does not affect the 2020 gross income for tax purposes. This is temporary for 2020 only.

Cash Charitable Contributions for Non-Itemizers

For 2020, the CARES Act allows non-itemizers to deduct $300 of cash contributions regardless of filing status. The Act of 2020 changes that for 2021 and allows an above-the-line deduction for cash contributions of $600 for joint filers and $300 for all other filing statuses. However, Congress is concerned that taxpayers will abuse this provision and added a 50% underpayment of tax penalty where the contribution cannot be properly documented.

Cash Charitable Contributions for Itemizers

For 2020 the 60% limit on cash contributions was suspended for 2020, thus allowing larger cash contributions during the COVID crisis. Under the Act the suspension of the 60% limit has been extended to 2021.

Flexible Spending Arrangements Carryover

Under current law cafeteria plans may only permit a carryover of unused amounts remaining in a health FSA as of the end of a plan year in an amount of no more than $550.

The Act extends the carryover period to 12 months after the end of such plan year for unused benefits and contributions to health flexible spending and dependent care flexible spending arrangements for 2020 and 2021.

An employer may also allow an employee who ceases to participate in the plan during calendar year 2020 or 2021 to continue to receive reimbursements from unused benefits or contributions through the end of the plan year in which the employee's participation ceased, including any extended grace period.

Reduction in Medical Deduction AGI Floor

The medical deduction AGI threshold was scheduled to increase to 10% beginning in 2020. The Act makes the 7.5% threshold permanent.

Volunteer Firefighters and Emergency Medical Responders Benefits

Under prior law, for tax years beginning in 2020, for any member of a "qualified volunteer emergency response organization," gross income excluded certain state or local tax relief provided for performing volunteer emergency response services or any payments provided by state or local governments on account of performing volunteer emergency response services. The Act makes this exclusion permanent. (IRC 139B as amended by Act Sec. 103).

Education Credits Phaseouts Consolidated

Under prior law the American Opportunity Tax Credit (AOTC) and the Lifetime Learning Credit (LLC) each had a different phaseout range. The Act replaces the dual phaseouts with

a single one that applies to both credits. This increases the AGI at which the LLC phaseout begins which allow more individuals to qualify for the LLC. Effective for years after December 31, 2020. The phaseout ranges will not be adjusted for inflation in future years.

Filing Status	Phaseout Range
Unmarried Filing Status	$ 80,000 – $ 90,000
Joint Filing Status	$160,000 - $180,000
Married Separate	No Credit Allowed

Discharge of Qualified Principal Residence Indebtedness

For several years going back to 2008 taxpayers have been able to exclude from income up $2 Million, $1 Million for Married Filing Separate taxpayers, of home debt forgiveness income from their income. This provision has been previously extended and was scheduled to sunset after 2020. Because so many homeowners are behind in their home mortgage and property tax payments and may lose their homes, the Act extends the provision through 2025 but reduces the maximum exclusion for years after 2020 to $750,000 ($375,000 MFS)

Employer-Provided Educational Assistance

Educational assistance provided under an employer's qualified educational assistance program, up to an annual maximum of $5,250, is excluded from the employee’s income. The CARES Act expanded the definition of expenses to include employer payments of the employee’s student loan debt. But this special allowance was only available for payments made between March 27, 2020 through December 31, 2020. The Act extends the exclusion for loan repayments made through 2025.

Mortgage Insurance Premiums

For tax years 2007 through 2020 taxpayers could deduct as an itemized deduction the cost of premiums for mortgage insurance paid in connection with acquisition debt on a qualified personal residence. The deductible amount of the premiums phases out ratably by 10% for each $1,000 by which the taxpayer’s AGI exceeds $100,000 (10% for each $500 by which a married separate taxpayer’s AGI exceeds $50,000). If AGI is over $109,000 ($54,500 MFS), the deduction is totally phased out. The Act extends this provision for one year through 2021.

Nonbusiness Energy Credit

Since 2006 taxpayers have been able to claim a credit for making qualifying energy saving improvements to their existing homes. The dollar limits and credit percentages have been modified several times since the credit first became available. The credit of 10% of the amounts paid or incurred by the taxpayer for qualified energy improvements to the building envelope (windows, doors, skylights, and roofs) of principal residences ranges from $50 to $300 for energy-efficient property including furnaces, boilers, biomass stoves, heat pumps, water heaters, central air conditioners, and circulating fans, and is subject to a lifetime cap of $500. The Act extends this credit through 2021.

2-Wheeled Plug-In Electric Vehicle Credit

The Code provides a 10% credit for highway-capable, two-wheeled plug-in electric vehicles (capped at $2,500). Battery capacity within the vehicles must be greater than or equal to 2.5 kilowatt-hours. The Act extends this credit for one year so that it applies to property placed in service through 2021.

Solar (REEP) Tax Credit Phaseout

Under pre-Act law, individual taxpayers were allowed a personal tax credit, known as the residential energy efficient property (REEP) credit, equal to the applicable percentages of expenditures for qualified solar electric property, qualified solar water heating property, qualified fuel cell property, qualified small wind energy property, and qualified geothermal heat pump property. The Act extends the credit phaseout for two years as illustrated in the table.

SOLAR CREDIT RATE PHASEOUT		
Applicable Year	**Prior Law**	**New Law**
Thru 2019	30%	30%
2020	26%	26%
2021	22%	26%
2022	-0-	26%
2023	-0-	22%
2024	-0-	-0-

If you have questions about how this COVID-19 tax legislation might apply in your situation, please give this office a call.

How to Address Rising Tax Problems During COVID-19

COVID-19 has caused the death of over 300,000 people. There have been nearly 19 million reported cases in the United States. COVID-19 has touched nearly every aspect of the lives of every American.

It has even affected finances for most Americans as well, creating waves of economic stress. It will have some tax implications that many people have not considered. For some, it can mean simply reporting income or expenses differently. For others, it may mean having to pay additional income taxes that they had not planned.

Regardless of the situation, this year might be the year that you need to bring in a tax professional to help address some of the tax challenges that COVID-19 has caused.

Examples of Tax Complications Due to COVID-19: Unemployment and Retirement Plan Withdrawals

As individuals are losing their jobs or had to decrease work because of COVID-19, they are turning to other sources of income such as unemployment benefits and dipping into their retirement savings plans.

For those who are tapping into these funds for the first time, they might have questions about taxation—and they may not realize that they may have to pay taxes on these additional income sources.

Are unemployment benefits taxable?

Your unemployment benefits will be fully taxable at the federal level.

In general, unemployment benefits might be taxed by the state as well, depending on where you live. For example, Alabama and Califiornia do not impose any taxes on unemployment benefits, but the benefits are fully taxable as regular income in Iowa. Some states will only tax part of your benefits.

Are retirement benefit withdrawals taxable?

If you take out retirement benefits early, there is a 10% penalty imposed on any funds you remove. However, tax changes because of COVID-19 allowed individuals to take out funds from retirement without paying the 10% penalty as long as the withdraw took place during 2020. You must also meet certain requirements that indicate you have a stressful financial situation because of COVID-19.

Even if you meet the qualifications, avoiding the 10% penalty is not the only tax that you must pay. Instead, the money you take out is often taxed as income, depending on how your retirement plan was established.

Many people may not realize that they will face this additional tax hit after January 1, so they have not been planning for it over the past few months.

Dealing with the IRS and Unique Tax Problems After COVID-19

The best way to ensure that you are addressing tax issues appropriately is to get professional tax help. If you will owe taxes from 2020, you might be able to work out a deal with the IRS to decrease your tax obligations, for example.

If you get a notice from the IRS about taxes that you owe, you have a few options that you can use to address it.

- Make a full payment. You can pay the amount demanded in full by the due date noted on the notice. However, this might not be the best course of action, as the amount that the IRS says is due might not actually be accurate. Check with a tax professional before you make any additional payments.
- Create an installment agreement. You can work with your tax professional and the IRS to create an installment agreement to pay the tax obligation over time. If you work with the taxing authority directly, they will often demand a large monthly payment. Using a professional to help you negotiate will usually decrease this payment and help you create a plan that actually works for you.
- Suggest an offer in compromise. An offer in compromise is a technical term that means you are offering to settle your debt with the IRS for a lesser amount than what the IRS is demanding. Using this compromise method often requires a showing that you cannot afford to pay the full amount, even if you created an installment plan. A tax professional will be able to help you develop this type of offer and present it in a way that is most likely to be accepted.

Having a professional on your side to help you deal with tax preparation, back taxes, tax problems, and negotiations with the IRS can be invaluable. Do not work through this process alone, especially if COVID-19 has created some unique tax issues for you in 2020.

Your Annual Reminder to File Worker 1099s

Article Highlights:

- 1099-NEC Filing Requirements
- Independent Contractor Filing Threshold
- Form W-9
- Worksheet

This is our annual reminder that if you use workers other than employees to perform services for your business and pay them $600 or more for the year, you are required to issue each one a Form 1099-NEC after the end of the year to avoid facing the loss of the deduction for their labor and expenses. The 1099s for 2020 must be provided to workers no later than February 1, 2021. The forms are normally due January 31, but since it falls on a Sunday in 2021, the due date is extended until February 1.

As you probably noticed, the IRS has switched forms for 2020 reporting. They have resurrected a form that hasn't been used since the early 1980s—Form 1099-NEC, Nonemployee Compensation. The prior 1099-MISC form was used for reporting more than just nonemployee compensation; because 1099s reporting non-employee compensation need to be filed by January 31, and the ones reporting other information are not due to the IRS until March 31, this created enough confusion that the IRS made the change.

The requirement to file Form 1099-NEC may also apply to landlords in light of tax reform's 20% pass-through deduction (Sec. 199A deduction). The IRS, in regulations for this tax code section, cautions landlords that to be treated as a trade or business (and therefore to be generally eligible for the 199A deduction), they should consider reporting payments to independent contractor service providers on IRS Form 1099-NEC. This generally wasn't required for rental activities in the past and still isn't required when a rental is classified as an investment rather than as a trade or business.

It is not uncommon to, say, have a repairman out early in the year, pay them less than $600, and then use his services again later and have the total for the year exceed the $600 limit. As a result, you could easily overlook getting the necessary information, such as their complete name and tax identification number (TIN), to file the 1099s for the year. Therefore, it is good practice to have unincorporated individuals complete and sign the IRS Form W-9 the first time you use their services. Having properly completed and signed Form W-9s for all independent contractors and service providers eliminates oversights and protects you against IRS penalties and conflicts.

The government provides IRS Form W-9 as a means for you to obtain the data required to file 1099s for your vendors. This data includes the vendor's name, address, type of business entity and TIN (usually a Social Security number or an Employer Identification Number) as well as certifications of the ID number and citizenship status. It also provides verification that you complied with the law should the vendor provide you with incorrect information. We highly recommend that you have potential vendors complete Form W-9 prior to engaging in business with them. The form can either be printed to fill out or completed onscreen and then printed. A Spanish-language version is also available. The W-9 is for your use only and is not submitted to the IRS.

CAUTION: 1099-NEC worker reporting does not apply to household workers, as they are considered employees. Call for additional information.

To avoid a penalty, the government's copies of the 1099-NECs must also be sent to the IRS by February 1, 2021. The penalties can be significant, ranging between $50 and $280 for each 1099-NEC filed late. If you failed to obtain a worker's Social Security number but file

the 1099 on time, the penalty for not including the SSN is $50, which is less than the potential $280 penalty for filing late or not at all.

1099-NEC forms must be filed electronically or on special optically scannable forms. If you need assistance with filing 1099-NEC or have questions related to this issue, please give this office a call. You can complete the 1099-NEC worksheet and forward it to this firm to prepare 1099s. Also, make sure you have all of your non-employee workers or service providers complete a Form W-9 for 2020.

Didn't Get Your Economic Impact Payment? You Can Claim It on Your 2020 Return.

Article Highlights:

- Economic Impact Payments
- High-Income Taxpayer Phaseout
- Using the 2018 and 2019 Returns
- Who Qualified for a Rebate?
- Deceased Individuals
- Tax Return Non-filers
- Reconciliation on the 2020 Return

One of the more tax-troubling issues this year has been the distribution of what Congress referred to as the recovery rebates. You may know these payments as the Economic Impact Payments (EIPs) or stimulus payments, names that the IRS took the liberty of creating. These payments were meant to provide financial assistance to individuals and families struggling during the initial outbreak of the COVID-19 pandemic.

Congress authorized the payment amounts in late March 2020, in the CARES Act, to be $1,200 for each filer ($2,400 if married and filing a joint return) and $500 per dependent child under age 17. Congress mandated that the IRS get these payments out as quickly as possible. However, the payments were phased out for higher-income taxpayers at a rate of 5% of the taxpayer's adjusted gross income (AGI) in excess of a threshold, also based upon the taxpayer's AGI.

Filing Status	AGI
Unmarried Taxpayers (and Married Filing Separately)	$75,000
Head of Household	$112,500
Married Taxpayers Filing Joint	$150,000

In addition, the recovery rebates are actually a refundable tax credit on the 2020 tax returns, so to meet the Congressional mandate, the IRS issued the rebates in advance based upon each family's makeup and income on their 2019 tax return. However, because a significant portion of the population had yet to file their 2019 return, especially because the April 15 due date for the 2019 return had been extended to July 15, 2020, the IRS then turned to the information on the 2018 returns on which to base the rebates.

Example: *Phil and Karla are married with one dependent. They are always slow in getting their returns filed, so the IRS based their rebate on their 2018 tax return. The AGI was $162,000, making them subject to the rebate phaseout. From the table above, their phaseout threshold is $150,000. Their phaseout is $600 (($162,000 –*

$150,000) x 5%). Without the phaseout, they would have been entitled to an EIP of $2,900. Because of the phaseout, their payment was $2,300 ($2,900 – $600).

Complicating the IRS's ability to quickly issue the EIPs was the fact that the higher standard deduction included with the 2018 tax reform meant that a significant portion of the population did not even have to file a 2018 (or 2019) tax return. So, the IRS then used data from the Social Security and Veterans Administrations to determine non-filers who were entitled to a payment.

Another issue was that, unlike during the 2008 financial crisis, when stimulus payments were allowed to those who had passed away, the IRS took a hard stand with the pandemic EIPs and required that those payments be returned, which complicated issues for surviving spouses when the check was payable jointly.

Many individuals were entitled to EIPs who were not receiving Social Security, Railroad Retirement, or Veterans benefits and were not required to file a return. They were required to go to the IRS's website and register in order to get a payment. The IRS initially did not issue EIPs to inmates (the CARES Act was silent as to whether or not these individuals qualified), but a federal court later overruled the IRS.

As you can see, what Congress envisioned would be a simple credit on the 2020 return quickly became complicated as a result of the mandate to issue payments in advance of the 2020 return being filed. Many individuals are still waiting for their rebates or are entitled to more than they received.

If you are among those eligible for a rebate who haven't received a payment, or the amount you received is less than what you are allowed, take heart. Since it is really a credit on the 2020 tax return, you can claim your missing or additional rebate amount when you file your 2020 return. But this means that if you wouldn't normally have to file a return, you will need to do so in order to get your recovery rebate credit.

However, here is yet another potential problem: when you claim the rebate credit on your 2020 return, it will be based upon your 2020 AGI and family makeup, which may or may not be to your benefit. Here are some situations that you may encountered:

Example #1A – You had a dependent child in 2019 who had since become emancipated in 2020. If you received an EIP in 2020, it would have included the dependent's rebate amount. However, if it is based on the 2020 return, it will not. On the bright side, your dependent will be eligible for a $1,200 rebate in their 2020 return if it is not phased out. More good news: you aren't required to repay the dependent portion of the EIP you received.

Example #1B – You are divorced and claimed your 10-year-old son as a dependent on your 2019 return, and based on your 2019 return, you received a $1,700 EIP ($1,200 for yourself and $500 for your son). Your ex-spouse will claim your son as a dependent on your ex-spouse's 2020 return. Your ex-spouse will claim the dependent portion of the recovery rebate credit on their 2020 return. You will not be required to pay back the $500 dependent portion of the EIP that you received.

Example #2 – The IRS used your 2018 AGI to figure your rebate, and because it was over the threshold, it was partially phased out, and the payment you received was $800 instead of $1,200. Your 2020 AGI is below the phaseout threshold, so you will be able to receive the $400 as a credit on your 2020 tax return.

Example #3 – The opposite of example #2: when you file your 2020 return, the amount of the rebate you receive will be larger than what you are entitled to on your 2020 return. You will not have to pay back the difference.

These are only examples of the many situations that a change in filing status, dependents, and/or AGI can create with regard to the recovery rebate credit when filing your 2020 tax return. One good thing is that Congress wrote the law so that if the EIP you received was larger than the recovery rebate credit you are entitled to on your 2020 return, you will not have to pay back any of the difference. On the other hand, if your EIP was less than what's allowed on your 2020 return, you can claim the difference as a credit on the 2020 return.

Be sure to keep the confirmation that the IRS sent you showing the amount of your advance rebate (the EIP); we'll need it when preparing your 2020 return.

This office will automatically take care of reconciling the advance rebate with the amount determined on your 2020 return. Please call if you have other questions.

W-2 or 1099-NEC: Which Form Should Your SMB Use for Which Workers?

Filing annual wage reports is just one of the many end-of-year responsibilities expected of every business. But the task is not as straightforward as some would think. The reports get sent to the people who have received wages, and at the same time they get filed with the Social Security Administration (SSA) or the Internal Revenue Service (IRS). In some cases, they get filed with both. The question of which is appropriate rests entirely on who is being paid and how the relationship between them and the business is categorized.

Wage reports are prepared for employees as well as for independent contractors, but each type of wage earner receives a different form for filing their income tax returns. The information that a business provides to the appropriate government agency needs to match the information submitted by the wage earner, both to ensure accuracy and that they are paying the taxes that they owe. Businesses are expected to use the correct form, and in order to do that they need to be certain as to whether or not the person that they are paying is considered an employee. Getting this right is important, as incorrectly labeling an individual as a non-employee can result in significant penalties.

The Difference Between an Employee and an Independent Contractor

Though at first glance it may seem obvious whether a wage earner is a nonemployee or an employee, there are a lot of instances where business owners are not certain how an individual's role is best defined. To clear up confusion, the IRS has identified three specific distinguishing criteria: the relationship between the worker and the employer; whether the business has financial control over the individual's payment terms; and whether the business has behavioral control over the individual. Let's take a closer look at each.

The Relationship Between the Worker and the Employer

Business owners who are not sure whether an individual is an employee should determine the answers to specific questions about their role within the organization – or whether they have one at all. Examples of appropriate questions would be whether the duties that the person is responsible for are integral to the operations of the business and whether the individual receives paid vacation or benefits from the organization. Though some point to the existence of a written contract as evidence supporting an individual being either an independent contractor or an employee, a contract by itself is not enough to support an argument one way or another.

Financial Control

Another straightforward indication of whether a wage earner is an employee or a contractor is based upon how the individual is paid, and why. A person that charges based on their own fee structure in exchange for a service performed is not an employee. A business owner has the choice of paying or not paying the amount demanded or seeking somebody else to provide the service. That is not the case with an employee, whose pay is determined by the employer from the start. Employers are able to control the work that an employee is assigned to do and the employee is required to perform based upon instructions. The same is not true for an independent contractor.

Behavioral Control

Finally, an employee's work is directed by their employer, both in terms of what they do and how, where and when they will do it. The same is not true for an independent nonemployee. These individuals are self-directed and create their own terms and conditions for their schedule, their work environment, and more. Though a business may provide specifications for the work product or job, the professional that is being paid is not controlled by the business' code of conduct, work hours, or any other specifics that an employee is obligated to follow.

Using the Correct Forms to Suit the Individual

Employees get W-2 Forms
Employees' wage information gets reported on W-2 forms. These contain the following information:

- The amount of taxable income that the employee was paid and the amount of federal income tax that the employer withheld from the employee's paychecks
- The amount of Medicare and Social Security income that the individual earned and the amount FICA taxes withheld on that income
- The amount of state income and related taxes withheld from the amount paid to the employee
- Employee tip income
- The value of any taxable and non-taxable employee benefits

Non-employees get 1099-NEC Forms
Wage information for non-employees gets reported on Form 1099-NEC for any non-employees that have been paid $600 or more during the tax year. Appropriate recipients of this form include:

- Nonemployees such as freelancers and independent contractors
- Attorneys under specific circumstances
- An individual or entity in the business of catching fish from whom you have purchased fish or "other aquatic life"

This form reflects all of the payments made to the individual over the course of the tax year but no withholding, Social Security, or Medicare income, as they are not withheld for independent contractors. Take note that this form is new for 2020, replacing the previously used Form 1099-MISC for independent contractors. There are others that had previously received 1099-MISC for payments, and that form will continue to be used for them.

Individuals that Are Both Employee and Contractor Get Both Forms

There are some situations where an individual can be both an employee and an independent contractor. An example would be an administrative assistant who also consults as an interior decorator. In this case the individual would be a paid employee who receives a W-2 for their role within your organization and would also receive a 1099-NEC for the interior design work done for your offices.

When Should the Forms Be Prepared and What Should Be Done with Them?

Both employees and the Social Security Administration must receive completed W-2 forms no later than January 31st following the tax year for which they have been prepared. The same date applies for 1099-NEC forms, though they are submitted to the IRS rather than to Social Security. Both W-2 forms and 1099-NEC forms can be submitted online.

If you have any questions about which forms need to be submitted from your business, please contact our office.

Saver's Credit Can Help You Save for Retirement

Article Highlights:

- Benefits
- Eligible Taxpayers
- Rules for Students, Dependents of Others and Individuals Under the Age of 18
- Due Date for Contributions

Low- and moderate-income workers can take steps to save for retirement and earn a special tax credit.

The saver's credit, also called the retirement savings credit, helps offset part of the first $2,000 workers voluntarily contribute to traditional or Roth individual retirement arrangements (IRAs), SIMPLE IRAs, SEPs, 401(k) plans, 403(b) plans for employees of public schools and certain tax-exempt organizations, 457 plans for state or local government employees, and the Thrift Savings Plan for federal employees. The saver's credit is available in addition to any other tax savings that apply as a result of contributing to retirement plans.

Credits for 2020 and 2021 are determined from the tables shown below and are based upon both filing status and income (AGI).

2020 PHASE-OUTS						
Modified Adjusted Gross Income*						Applicable Percentage
Joint Return		Head of Household		Others		
Over	Not Over	Over	Not Over	Over	Not Over	
$ 0	$39,000	$ 0	$29,250	$ 0	$19,500	50
39,000	42,500	29,250	31,875	19,500	21,250	20
42,500	65,000	31,875	48,750	21,250	32,500	10
65,000		48,750		32,500		0

2021 PHASE-OUTS						
Modified Adjusted Gross Income*						Applicable Percentage
Joint Return		Head of Household		Others		
Over	Not Over	Over	Not Over	Over	Not Over	
$ 0	39,500	$ 0	29,625	$ 0	19,750	50
39,500	43,000	29,625	32,250	19,750	21,500	20
43,000	66,000	32,250	49,500	21,500	33,000	10
66,000		49,500		33,000		0

** **Modified AGI** is determined without regard to the foreign earned income exclusion (also applies to US possessions) and foreign housing exclusion or deduction.*

Like other tax credits, the saver's credit can increase a taxpayer's refund or reduce the tax owed. Though the maximum saver's credit is $1,000 ($2,000 for married couples if both spouses contribute to a plan), taxpayers are cautioned that it is often much less and, due in part to the impact of other deductions and credits, and may in fact be zero for some taxpayers.

The amount of a taxpayer's saver's credit is based on his or her filing status, adjusted gross income, tax liability, and amount contributed to qualifying retirement programs.

Example *– Eric and Heather, ages 32 and 30, are married and filing a joint return. In 2020, Eric contributed $3,000 through his 401(k) plan at work, and Heather contributed $500 to her IRA account. Their modified AGI for 2020 was $40,000. The credit is computed as follows:*

Eric's 401(k) contribution was $3,000, but only the first $2,000 can be used	*$2,000*
Heather's IRA contribution was $500, so it can all be used……………………………	*500*
Total qualifying contributions…………………………………………………………………………	*$2,500*
Credit percentage for a joint return with AGI of $40,000 from the table………	*X.20*
***Saver's credit**……………………………………………………………………………………………*	***$500***

This example illustrates how the credit phases out for higher-AGI taxpayers. In this example, the couple's AGI of $40,000 limits the credit to 20% of their qualifying contributions. Had their AGI been $39,500 or less, their credit percentage would have been 50% of their qualified contributions, for a credit of $1,250.

The saver's credit supplements the other tax benefits available to people who set money aside for retirement. Generally, except for Roth IRA contributions, workers' contributions to retirement plans are tax deductible, either in the form of a deduction on their tax return (traditional IRAs and certain self-employed retirement plans) or through a reduction of wages that would otherwise be taxable (such as pre-tax contributions to a 401(k), 403(b), etc.). So, in addition to the saver's credit, contributions to retirement plans provide a tax deduction for traditional IRAs or income reductions for certain other plans, which lowers an individual's tax before the credit is applied. The credit itself can only be used to reduce taxes (income and alternative minimum taxes only) to zero, and any amount in excess of a taxpayer's tax liability is lost.

Other special rules that apply to the saver's credit include the following:

- Eligible taxpayers must be at least 18 years of age.

- Anyone claimed as a dependent on someone else's return cannot take the credit.
- A full-time student cannot take the credit. A person enrolled as a full-time student during any part of five calendar months during the year is considered a full-time student.

The credit is provided to encourage taxpayers to save for retirement. To prevent taxpayers from taking distributions from existing retirement savings and re-depositing them to claim the credit, qualifying retirement contributions used to figure the credit are reduced by any retirement plan distributions taken during a "testing period." The testing period includes the prior two tax years, the current year, and the subsequent tax year before the due date (including extensions) for filing the taxpayer's return for the tax year of the credit.

As you can see, qualifying for and using this credit involves following a complicated set of rules, but the credit can be very beneficial. If you are not sure you can afford to fund your retirement plan, contributions to an IRA or a self-employed retirement plan (SEP) can be made after the close of the year, allowing you time to determine the tax benefit of the saver's credit and your overall tax refund before you make a contribution to one of those plans. For example, IRA contributions for 2020 can be made up to April 15, 2021, while SEP contributions can be made until October 15, 2021 if your return is on extension.

If you have questions about how this tax benefit might apply in your situation, please give this office a call.

Sold or Thinking of Selling Your Home?

Article Highlights:

- Home Sale Exclusion
- 2 out of 5 Rule
- Business Use of the Home
- Gain or Loss from a Sale
- Previous Use as a Rental
- Form 1099-S IRS Matching
- Records

In spite of (or in some cases, because of) the COVID-19 pandemic, and with near-record-low home mortgage interest rates, the housing market has been booming. September 2020 existing home sales were up 9.4% from August 2020 and 20.9% from 2019, according to the National Association of Realtors. If you sold your home this year or are thinking about selling it, there are many tax-related issues that could apply to that sale. To help you prepare for reporting the sale you may have already made or make you aware of what issues you may face if you are in the "thinking about" stage, this article covers the tax basics and some special situations related to home sales and the home-sale gain exclusion.

Home Sale Exclusion – For decades, Congress has encouraged home ownership, including by providing a tax break for taxpayers selling their homes. Under the current version of the tax code, you are allowed an exclusion of up to $250,000 ($500,000 for married couples) of gain from the sale of your primary residence if you owned and lived in it for at least 2 of the 5 years previous to the sale. You also cannot have previously taken a home-sale exclusion within the 2 years immediately preceding the sale. There is no limit on the number of times you can use the exclusion as long as you meet these time requirements; however, extenuating circumstances can reduce the amount of the exclusion. The home-sale gain exclusion only applies to your main home, not to a second home or a rental property.

2 out of 5 Rule – As noted above, you must have used and owned the home for 2 out of the 5 years immediately preceding the sale. The years don't have to be consecutive or the closest to the sale date. Vacations, short absences and short rental periods do not reduce the use period. If you are married, to qualify for the $500,000 exclusion, both you and your spouse must have used the home for 2 out of the 5 years prior to the sale, but only one of you needs to meet the ownership requirement. When only one spouse in a married couple qualifies, the maximum exclusion is limited to $250,000 instead of $500,000.

Although this situation is quite rare, if you acquired the home as part of a tax-deferred exchange (sometimes referred to as a 1031 exchange), then you must have owned the home for a minimum of 5 years before the home-gain exclusion can apply.

If you don't meet the ownership and use requirements, there are some situations in which a prorated exclusion amount may be possible. An example of this situation would be if you were required to sell the home because of extenuating circumstances, such as a job-related move, a health crisis or other unforeseen events. Another rule extends the 5-year period to account for the deployment of military members and certain other government employees. Please call this office if you have not met the 2 out of 5 rule to see if you qualify for a reduced exclusion.

Business Use of the Home – If you used your home for business and claimed a tax deduction—for instance, for a home office, storing inventory in the home or using it as a day care center—that deduction probably included an amount to account for the home's depreciation. In that case, up to the extent of the gain, the claimed depreciation cannot be excluded.

Figuring Gain or Loss from a Sale – The first step is to determine how much the home cost, combining the purchase price and the cost of improvements. From this total cost, subtract any claimed casualty loss deductions and any depreciation taken on the home. The result is your tax basis. Next, subtract the sale expenses and this tax basis from the sale price. The result is your net gain or loss on the sale of the home.

If the result is negative, the sale is a loss; losses on personal-use property such as homes cannot be claimed for tax purposes.

If the result is a gain, however, subtract any home-gain exclusion (discussed above) up to the extent of the gain. This is your taxable gain, which is, unfortunately, subject to income tax. If you owned the home for at least a year and a day, the gain will be a long-term capital gain; as such, it will be taxed at the special capital-gains rate, which ranges from zero for low-income taxpayers to 20% for high-income taxpayers. Depending on the amount of all of your income, the gain may also be subject to the 3.8% net investment income surtax that was added as part of the Affordable Care Act. The tax computation can be rather complicated, so please call this office for assistance.

Another issue that can affect your home's tax basis (discussed above) applies if you purchased your home before May 7, 1997 after selling another home. Prior to that date, instead of a home-gain exclusion, any gain from a sale was deferred to the replacement home. Although this is now rare, if it matches your situation, the deferred gain would reduce your current home's tax basis and add to any gain for the current sale.

Prior Use as a Rental – If you previously used your home as a rental property, the law includes a provision that prevents you from excluding any gain attributable to the home's appreciation while it was a rental. The law's effective date was the beginning of 2009, which means that you only need to account for rental appreciation starting in that year. This law was passed to prevent landlords moving into their rentals for 2 years so that they could exclude the gains from those properties. Prior to the law change, some landlords had done this repeatedly.

Form 1099-S – Usually, the settlement agent—typically an escrow or title company—prepares IRS Form 1099-S, Proceeds from Real Estate Transactions, which reports the home seller's name, tax ID number, proceeds of the sale, date of the sale, etc. This form is provided to both the IRS and the seller. Note that this form only includes information from the sale; it doesn't provide any basis information to the IRS. Sometimes, sellers think that if the home sale gain exclusion eliminates all of their gain from the sale of their home, they don't need to report the transaction on their tax return. Unfortunately, this thinking could lead to correspondence (i.e., a bill for tax due) from the IRS as it attempts to match the sales price shown on the 1099-S to the seller's tax return. To avoid this interaction with the IRS, you should report the home's sale on your income tax return for the year of the sale; in doing so, you will be including your basis and exclusion information for the IRS.

Records – Assets worth hundreds of thousands of dollars, including your home, need your attention, particularly regarding records. When figuring your gain or loss, you will, at a minimum, need the escrow statement from the purchase, a list of improvements (not maintenance work) with receipts, and the final escrow (settlement) statement from the sale. If you encounter any of the issues discussed in this article, you may need additional documentation.

A few other rare home-sale rules are not included here. As you can see, home-sale computations and tax reporting can be very complicated, so please call this office if you need assistance.

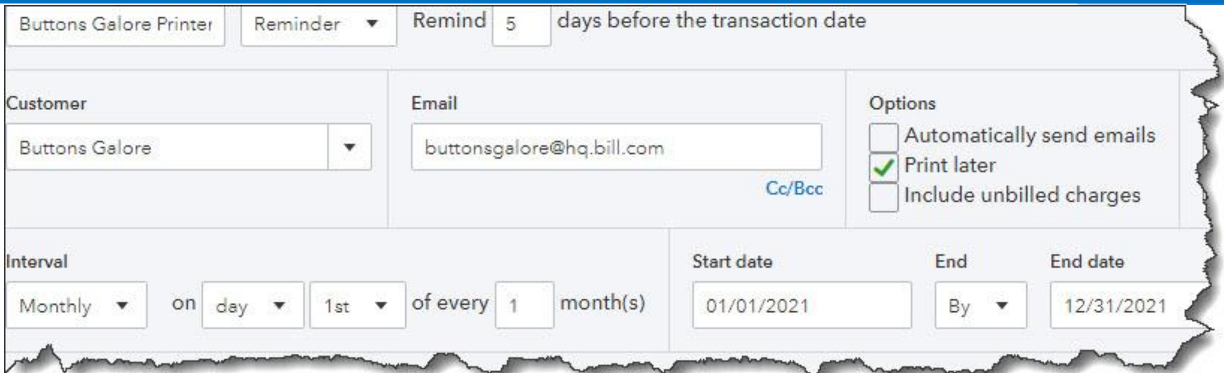
How to Create Recurring Transactions in QuickBooks Online

QuickBooks Online saves time and improves accounting accuracy in numerous ways. One example is its support for recurring transactions.

It's easy to get distracted when you're doing dull, repetitive accounting work. That distraction leads to errors sometimes. So, besides the time you're spending on work that could be automated, you have to tack on additional time to chase down your mistakes.

QuickBooks Online already reduces repetitive data entry by saving your lists of customers, vendors, products, etc., and making them accessible when you're creating transactions. But it does more to save time and minimize errors by allowing you to create *recurring transactions.* Enter a transaction like an invoice or bill once, and QuickBooks Online memorizes it for future use!

Here's how it works. Let's say you have a customer who wants to rent a printer from you for one year. You create an invoice for one month's rental. At the bottom of the screen, click **Make recurring**. A partial view of the screen that opens is pictured below.



QuickBooks Online allows you to set up a transaction to repeat at scheduled intervals.

Much of this screen will have already been filled in. You'll need to enter a name for the template you're creating at the top of the screen, one that will remind you of its content. In the second field, the drop-down list displays three options for how the recurring transaction will be handled by QuickBooks Online They are:

- **Scheduled**. Your invoice will go out automatically at the scheduled interval, with only a change to the date. As with any automated process, you should be very careful when selecting this option.
- **Reminder**. You will get a reminder ahead of each occurrence so you can make any necessary changes before sending.
- **Unscheduled**. No automation is involved here. The invoice is memorized, but you'll have to remember when it needs to go out.

If you chose **Reminder**, the next field will read **Create (x) days in advance**. Enter the number of days here. On the next line, you'll only have to check or uncheck the **Options**.

Under **Interval**, you'll tell QuickBooks Online when the invoice is scheduled to go out. You can choose from **Daily**, **Weekly**, **Monthly**, and **Yearly**. The invoice in this example should be processed and sent on the first day of every month. The start date is January 1, 2021, and it will end on December 31, 2021. If your recurring transaction should continue to go on indefinitely, you'll have the option to select **None** from the drop-down list under **End**. You can also choose **After**.

Check the fields below this line to make sure they're correct. You can change the message if you'd like and add an attachment. If everything looks correct, click **Save Template** in the lower right corner.

Using Recurring Transactions

If you've set this transaction up to recur automatically, you don't have to do anything more with it unless you need to edit it at some point. If you need to do so, or if you're responding to a reminder (or chose not to be reminded), you can access the list of transactions you've memorized by clicking the gear icon in the upper right and selecting **Recurring Transactions** under **Lists**. A screen containing this section will open:

CUSTOMER/VENDOR	AMOUNT	ACTION
Caribou Coffee	125.00	Edit ▾
Buttons Galore	347.38	
Bridget O'Brien	161.94	
Adam Saraceno	1,649.01	

Use
Duplicate
Pause
Skip next date
Delete

Once you've created recurring transactions, you have several options for managing them.

The table that appears will contain other columns describing the recurring transactions, like **Type** and **Interval**. The image above shows the end of each row that reads **Edit** until you open the drop-down menu. You can see what your options are. They include **Use**, which you would select when you want to edit and/or send a transaction. You can also create a **Duplicate**, **Pause** the recurrences temporarily, **Skip next date**, or **Delete** the template. Click the arrow next to **Reminder List** in the upper right and select **Run Report** to see the **Recurring Template List Report**.

As you can see, recurring transactions can not only save time, but they can also help reduce errors and minimize unnecessary work. They're not overly difficult to create, but you should use caution if you choose to automate them. We're available to answer your questions about this useful tool and about any other element of QuickBooks Online. Stay healthy, and here's to 2021!

JANUARY 2021 INDIVIDUAL DUE DATES

January 4 - Time to Call for Your Tax Appointment -

January is the beginning of tax season. If you have not made an appointment to have your taxes prepared, we encourage you to do so before the calendar becomes too crowded.

January 11 - Report Tips to Employer -

If you are an employee who works for tips and received more than $20 in tips during December, you are required to report them to your employer on IRS Form 4070 no later than January 11.

January 15 - Individual Estimated Tax Payment Due -

It's time to make your fourth quarter estimated tax installment payment for the 2020 tax year.

No ~ Nonsense Tax Tips

JANUARY 2021 BUSINESS DUE DATES

January 15 - Employer's Monthly Deposit Due -

If you are an employer and the monthly deposit rules apply, January 15 is the due date for you to make your deposit of Social Security, Medicare and withheld income tax for December 2020. This is also the due date for the nonpayroll withholding deposit for December 2020 if the monthly deposit rule applies. Employment tax deposits must be made electronically (no paper coupons), except employers with a deposit liability under $2,500 for a return period may remit payments quarterly or annually with the return.

NOTE: Delayed Payment of Employer Payroll Taxes from 2020

The CARES Act allows employers to delay paying 2020 payroll taxes, with 50% of the employer's share of the 2020 Social Security tax due by December 31, 2021, and the remainder due by December 31, 2022. Any payments or deposits the employer makes before December 31, 2021, are first applied against the payment due on December 31, 2021, and then applied against the payment due on December 31, 2022.

January 15 - Farmers and Fishermen -

Pay your estimated tax for 2020 using Form 1040-ES. You have until April 15 to file your 2020 income tax return (Form 1040 or Form 1040-SR). If you don't pay your estimated tax by January 15, you must file your 2020 return and pay any tax due by March 1, 2021, to avoid an estimated tax penalty.

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