ClientLine®

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YEAR-END TAX TIPS

Although 2020 is drawing to a close, there's still time to maximize your tax deductions and credits to lower your tax bill.

GIVE A GIFT

Typically, you can only deduct your charitable contributions if you itemize deductions on Schedule A. But the CARES Act allows non-itemizers to deduct up to $300 in cash donations to qualified charities. For itemizers, the previous 60% adjusted gross income cap for charitable donations is bumped up to 100% for 2020.

INVEST FOR RETIREMENT

If you're a freelancer or self-employed, consider starting a simplified employee pension. Also called a SEP IRA, this type of retirement account allows you to contribute up to 25% of your self-employment earnings, with a maximum contribution of $57,000 for 2020. All contributions you make are tax-deductible.

TAKE CREDIT

For parents with children under age 17 at the end of the year, the child tax credit can provide a $2,000 credit per qualifying child to lower your tax bill. This is one of the few refundable credits. So if it reduces your tax bill to zero, you may get a partial refund. This credit begins to phase out for individuals with a modified adjusted gross income over $200,000.

GO GREEN

Tax credits are still available for installing renewable energy devices on your primary home. Installing things like solar panels, solar water heaters, geothermal pumps and small wind turbines can score you a tax credit of up to 26% of the costs. This credit is non-refundable so any unused credit can be carried forward to future years.

MAX OUT

Don't forget to max out retirement account contributions. Depending on your plan, you may be able to put away $19,500 in your 401(k) or $13,500 in to a SIMPLE IRA and $6,000 into your IRA, if your modified adjusted gross income is less than $65,000 for single filers or $104,000 for married filing joint taxpayers. Each plan also offers those age 50 and older the opportunity to make additional catch-up contributions.

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Business Tax Tips

The CARES Act allows corporations to deduct 25% of taxable income for cash contributions made in 2020 to qualified charities. Non-cash contributions don't qualify. If you're considering making cash donations in 2020, do so because the percentage drops back down to 10% in 2021, unless Congress intervenes.

If you need new equipment, consider purchasing it before the end of the year. With Section 179 and bonus depreciation rules, you may be able to deduct the entire purchase price this year, instead of depreciating it over the next several years.

Bumping up salaries increases the amount you pay in Social Security, Medicare, and unemployment taxes. But enhancing benefits won't. So, instead of giving pay raises, consider increasing other benefits. You could give additional paid days off or increase contributions to health insurance which would give you a larger tax write-off.

Consult your tax advisor now regarding recent tax law changes that you must act on before year's end.

SECTION 1031 EXCHANGES

Section 1031 exchanges, also called like-kind exchanges, have been around nearly a century. They involve swapping one property for another and if structured correctly, can let you defer tax on any gain.

REAL PROPERTY

The 2017 Tax Cuts and Jobs Act limited 1031 exchanges to real property used in business or held for investment. However, if a large part of your business involves selling real property quickly with no intent to hold it as an investment (i.e. a homebuilder or a fix-and-flipper), these types of properties are excluded from 1031 exchanges. Likewise, your primary residence will not qualify but your vacation rental may qualify if certain use requirements are met.

LIKE-KIND

Property involved must be similar in nature and character but can differ in quality. In general, all real property is like-kind. An apartment building is like-kind to a warehouse. However, real property in the U.S. isn't like-kind to real property outside the U.S.

FIND AN INTERMEDIARY

Unless you're able to find someone, who wants the exact property you have and has the exact property you want, you'll need a qualified intermediary. You'll relinquish your property to them, they'll sell it to the buyer, and hold on to the cash proceeds until you find your replacement property. There are strict timing rules for these types of delayed exchanges. You must designate the replacement property within 45 days and close within 180 days of the sale of your relinquished property.

BEWARE OF BOOT

Boot is anything you receive that isn't like-kind property and boot is taxable to the extent you recognize any gain.

If you relinquish a property worth $400,000 and acquire a property worth $300,000, the $100,000 difference you receive in cash is boot.

Boot isn't always cash. It could be a promissory note from the buyer or tenant security deposits you receive as the new landlord.

Client PROFILE....

Seth paid for his college tuition using funds from a 529 college savings plan. He received a partial refund for a course he dropped. Will he have to pay tax on this refund?

If possible, Seth should return the refund to his 529 plan within 60 days and it won't be taxable. However, if he misses the 60-day window, it gets complicated and the refund may be taxable. He may also owe a 10% penalty for failing to use 529 funds for qualified expenses unless he meets one of several exceptions. Taxability largely depends on whether Seth received any tax-free educational help from things like scholarships, veteran's benefits, Pell grants or employer provided assistance that offset his qualified education expenses.

Seth should also look for other qualified expenses he incurred. If he bought a laptop and pays for internet service to use for distance learning, these qualify and can be used to offset the refund.

Client Profile is based on a hypothetical situation.
The solutions we discuss may or may not be appropriate for you.

STAYING ON TRACK FOR RETIREMENT

Many companies have had to reduce expenses to retain employees during the pandemic. To save money, some companies paused matching contributions to employee 401(k) plans. If this happened to your 401(k), do not panic. Keep with your existing retirement strategy and consider the following options.

DON'T STOP

If your job feels secure and you're still financially able, continue making contributions. Don't stop just because your employer temporarily did. The tax benefits and the potential for growth are still there.

SAVINGS BECOME CONTRIBUTIONS

Perhaps you've cut back on spending because you're not going to the gym or the dry cleaner as often. Contribute the money saved to your retirement plans. This may help make up a portion of the lost employer contribution. And for an added bonus, some contributions, like those to a traditional IRA or 401(k), may be tax deductible.

REVISIT YOUR ALLOCATION

With all the turmoil in the markets, now's a good time to review your portfolio allocation. If you've incurred significant losses, look to ensure your current investment strategy makes sense. Avoid making hasty decisions. Instead take a detailed look at your current situation and reevaluate your future needs. And if you're unsure of what to do, have a conversation with your financial and tax professionals.

SALES TAX AND ONLINE RETAILERS

Sales tax nexus is the connection that exists between a state's taxing authority and a seller that requires the seller to register and collect and pay sales tax. For example, having an office, remote employees, affiliates or subsidiaries in a particular state will create nexus. But other specified business activities will trigger nexus with the state, too. Surpassing a set amount of sales transactions or sales income is one such business activity.

ECONOMIC NEXUS

In 2018, the U.S. Supreme Court recognized that states can require online retailers to collect and remit sales tax if they meet certain economic thresholds. This new form of nexus is referred to as economic nexus and it doesn't require a physical presence in the state. Depending on which states you sell into and how many sales you have will determine whether you have economic nexus. Each state is free to set their own thresholds; however, the minimum requirements for economic nexus are 200 transactions or more than $100,000 in sales per year.

MARKETPLACE SELLERS

Retailers operating exclusively via participating marketplaces (i.e. Amazon, Ebay) need not worry about collecting sales tax because the marketplace collects on your behalf. This is a huge benefit because sales tax is complex and varies by city, county and state, so it's important to follow the rules.

Q&A

Q **My son turns 19 in December. Can I still claim him as a dependent on my tax return?**

A There are several tests that determine eligibility. Your son needs to be a full-time student for five months of the year or permanently and totally disabled. He will also need to live with you for more than half the year with certain exceptions allowed. Additionally, he will need to receive more than half his support from you and not file a joint return with someone else.

To qualify as a student, he will need to be enrolled full-time at a college or vocational school for five months of the year. The five months need not be consecutive. On-the-job training courses or schools offering courses only through the internet don't qualify.

Q **I own a second home in Mexico that I rent out when I'm not there. Am I allowed to deduct the property taxes I pay to the local Mexican government on my U.S. tax return?**

A Yes, you can deduct them as a business expense when you complete Schedule E to report your rental activity. But you'll need to allocate the amount between the number of days it's rented versus used personally or used by friends or family who don't pay you a fair rental price.

However, you can't deduct these taxes on Schedule A if you itemize and don't file Schedule E because foreign real estate taxes aren't an itemizable deduction.

ClientLine® SHORT BITS....

> MARRIAGE AND COHABITATION
According to the Pew Research Center, the number of adults who have ever lived with a partner, but didn't get married, has surpassed the number of adults who have ever been married, 59% to 50%. Although 58% of married couples claim to be satisfied with the marriage, only 41% of cohabitators feel the same with their partner. And overall, married couples are more satisfied with the trust and communication they have with their spouse than those that cohabitate.

> DIGITAL INNOVATION
Tech experts foresee significant digital advances in the civic and social realm. Nearly seven out of 10 experts polled believe that the next decade will see technology mitigate problems. Driven by privacy concerns and misinformation, the social media landscape will change dramatically in the next 10 years. They also believe there will be significant political reform via technology and a focus on healthier living. Ethical artificial intelligence will be widespread to improve lives and quash misinformation.

> DIRTY DOZEN
Each year, the IRS puts out its dirty dozen tax scams to educate taxpayers. Scammers historically use tax season and emergencies to scam people out of their money. In addition to the usual scams like imposter phone calls and phishing, this year the IRS is seeing a rise in scams involving fake charities and cyber crime. Due to the pandemic, scammers have created fake charities to steal from good-intentioned individuals. They do this through unsolicited phone calls or emails. The unsolicited emails create the risk of installing ransomware on the victim's computer when the email recipient clicks on a link in the email. A list of legitimate and qualified charities is available on irs.gov.