

# ClientLine®

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## TAXES IN RETIREMENT

Retirement is something almost all of us look forward to. But have you considered how your retirement income will be taxed? Not all retirement income is taxed the same, so it is important that you understand the details.

### SOCIAL SECURITY

If your total income is more than \$25,000 for an individual or \$32,000 for a married couple filing jointly, you must pay federal income taxes on your Social Security benefits. The tax rate is based on your total income from all sources, maxing out at the rate of 85%. Some states also tax social security income.

### 401(k) AND IRA WITHDRAWALS

Withdrawals from tax-deferred retirement accounts, such as a 401(k), are taxed as ordinary income. The taxability of a traditional IRA depends on how you treated your contributions before you retired. If you took a tax deduction in the years you contributed, your withdrawals are likely taxable.

Qualified withdrawals from a Roth IRA are non-taxable. Since your investment was made with after-tax dollars, you won't be taxed again when you withdraw it.

Although these accounts are long-term assets, they don't enjoy capital gains treatment.

### INVESTMENT INCOME

You'll pay taxes on dividends, interest and capital gains just as you did before you retired. The length of time you held an asset before selling it will determine your capital gains tax rate. It can be as low as zero if your total income for the year isn't high.

### SELLING YOUR HOME

If you've downsized and sold your home, you may be able to avoid paying tax on the gain. If you lived in your home for two of the

five years prior to the sale, you may be able to exclude up to \$250,000 in gain. The rules are a little more complex if you rented your home out, so consult with your tax professional to determine if you have taxable gains.



**Karen Petrucco**  
Account Manager

### LTM Client Marketing

45 Prospect Ave  
Albany, NY 12206

Tel: 518-870-1082

Toll Free: 800-243-5334 ext.505

Fax: 800-720-0780

kpetrucco@lstmclientmarketing.com  
www.lstmclientmarketing.com

### Succession Planning

Don't fail to plan for what will happen to your business when you retire. Perhaps your partner wants to buy you out or you want to leave the business to heirs. If you're planning to sell your business to outside investors, you'll need to complete a valuation so everyone can agree on the business's value. Include your consultation fees if the new owner needs assistance through the transition.

Regardless of how you plan to transition your business to new owners, consider how you'll receive payment for your ownership. Will it be one lump sum payment or will you receive monthly payments? You need to structure your payout in a way that allows you to enjoy the standard of living you desire in retirement and minimize your taxes.

Your succession plan is not just for retirement. It's also useful in the event you become ill, injured or worse. And remember that your succession plan isn't something you create and file away. Situations change that may require a tweak to your plan, so review it annually.

# THE COST OF NEW HIRES

Hiring employees is fundamental to business. Whether looking to hire your first employee or expand your team, be sure to understand the total cost of hiring help.

## RECRUITMENT

Employee recruitment can start with anything from the help wanted ad you place on job search boards to hiring a recruiter to handle the legwork. While the help wanted ad may cost you only a few hundred dollars, the professional recruiter will likely charge a percentage of the employee's annual salary. But the recruiter will handle everything from placing the advertisement, pre-screening applicants, and checking references.

## PRE-EMPLOYMENT SCREENING

Once you've offered the job to an applicant, you may choose to complete some pre-employment screening. The cost of criminal background checks, credit history, motor vehicle records, and drug testing can add up quickly.

## EMPLOYEE BENEFITS

Another big cost will be for benefits you provide. If you contribute to the cost of medical insurance, provide a retirement plan and other benefits for employees, factor in these costs.

## WORKERS' COMPENSATION

Many states require employers to carry workers' compensation insurance for employees. The requirements and rates vary by state. Some states require you to carry this insurance even if you have only one employee.

## TOOLS & EQUIPMENT

Your new employee may need equipment to do their work. You may need to provide a computer, phone or uniforms. Besides physical supplies, there may be additional costs to add employees to software programs for time tracking or project management.

## PAYROLL TAXES

In addition to salary, you'll have to pay payroll taxes. FICA tax is 7.65% of your employee's earnings.\*

The federal unemployment tax rate is 6% of the first \$7,000 earned and you'll have to pay state unemployment tax, too. Rates vary based upon state, industry and an employer's history of unemployment claims.

\*FICA tax includes 6.2% Social Security tax on the first \$142,800 of wages and 1.45% for Medicare.



## Client PROFILE....

**Elizabeth gave her brother \$10,000 for a down payment on a house and is considering giving him another \$10,000 to help with renovations. Will either of them owe gift tax on these amounts?**

The IRS considers this a gift and the general rule is any gift is taxable. However, the IRS has carved out several exceptions that make some gifts non-taxable.

The one that applies to Elizabeth is the annual exclusion. For 2021, a taxpayer can gift \$15,000 per year to an individual. If the total gift is \$15,000 or less, it is non-taxable to both the donor and the recipient.

Currently, the \$10,000 Elizabeth gave her brother wouldn't be taxable since it falls below

the annual exclusion amount. If she chooses to gift him another \$10,000 this year, then she will have to file Form 709 to report the gift and determine if any gift tax is owed.

However, if Elizabeth has a spouse, the spouse could gift the additional \$10,000 to her brother. Since both Elizabeth and her spouse have each gifted less than \$15,000 to her brother, there is no gift tax.

*Client Profile is based on a hypothetical situation.*

*The solutions we discuss may or may not be appropriate for you.*

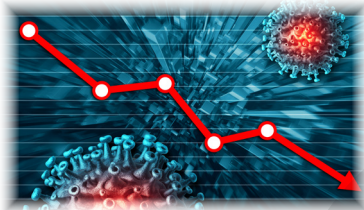
# HOW BUSINESS LOSSES AFFECT YOUR TAX RETURN

Many businesses may have incurred a loss in 2020 due to the pandemic-induced economic slowdown. When expenses exceed revenue, a loss is generated. How these losses affect your business tax return depends on many factors.

## CARRYBACK OR CARRYFORWARD

Under the CARES Act, businesses that incurred a loss for 2020 can carryback that loss five years. That means an amended tax return would need to be filed. Carrying back the loss could result in a refund of taxes paid in prior years.

However, if carrying back the loss won't benefit you, because your business already had a loss, then you can carry the loss forward indefinitely to offset income in future years.



Note that carrying back losses will not be an option for 2021 as the rules return to pre-CARES Act standards,

which do not allow carry backs. Any loss for 2021 can only be carried forward. And there are limits to the amount of the loss that can be used in future years.

## EXTRAORDINARY LOSSES

Business losses are not limited to operating losses. Businesses that incur extraordinary losses can also claim these on tax returns. Losses for things like fires and natural disasters can generate a loss for your business. Any insurance proceeds received from a loss will reduce your deduction.

Tax implications for business losses can be tricky. Speak with your tax professional to ensure your loss is calculated correctly.

# IS YOUR HOBBY A BUSINESS OR IS YOUR BUSINESS A HOBBY?

Everyone has hobbies and sometimes those hobbies provide some income. But when does your hobby become a business? Getting the right classification determines how this income is taxed.

## PROFIT BASED

Generally, if you engage in your hobby with the intent to generate profit, then it's a business, not a hobby. And if your hobby is strictly for recreation or personal entertainment, it's not a business. But many other criteria should be considered, including whether you rely on the income for your livelihood and how much time and effort you put in.

## IT'S YOUR HOBBY

You must report all your hobby income on your tax return. However,

following the 2017 Tax Cuts and Jobs Act, hobby expenses were eliminated and are no longer deductible on Schedule A as a miscellaneous itemized deduction.

## IT'S YOUR BUSINESS

However, unlike your hobby, if you're operating a business, you can deduct all your business expenses even if it creates a taxable loss. And the upside is that if you generate a loss, it can usually be used to offset other income from things like wages or investment income.

# ... Q & A

**Q** I'm working on my Master's degree online. Can I write off any of my tuition on my tax return?

**A** You can deduct up to \$4,000 in tuition expenses in 2020 but the deduction begins to phase out for single taxpayers with income of \$65,000.

However, you may prefer to take the Lifetime Learning Credit. It provides a credit of up to \$2,000 on your tax bill and has similar phase out thresholds as the deduction. As an extra bonus, there is no limit to the number of years you can claim the credit. The credit may be a better option because tax credits are generally more valuable than tax deductions since a tax credit directly offsets the tax you owe. Tax deductions only lower the amount of income on which you are taxed.

**Q** My business sells goods online and my customers live all over the world. Do I have to pay taxes on income earned from other countries?

**A** Most countries will require you to pay taxes only if you have a meaningful presence in their country. This could mean maintaining an office or warehousing inventory in their country. If your business has no connection to a foreign country other than sales to its citizens, generally you won't have to worry about paying taxes there. But international tax is complicated. Consult with your tax professional if you have specific questions.

# ClientLine® SHORT BITS....

## > BANK ACCOUNT USAGE

A recent study by the FDIC found that 95% of American households had a bank or credit union account in 2019. From 2017 – 2019, 1.5 million new households opened accounts and the use of mobile banking to access accounts has more than doubled since 2017. Roughly 73% of American households used bank credit, such as credit cards, personal loans, or lines of credit in 2019.

## > LOST HEALTH INSURANCE

According to a survey by the Employee Benefit Research Institute, nearly 7.7 million workers lost their employer-sponsored insurance during the COVID-19

pandemic. Women and young workers made up most of the losses. Fifty-five percent of the job losses were incurred by women and workers younger than 54 bore the brunt of the losses. Not only were employees impacted but dependents covered by the employer-sponsored plan also lost coverage. An estimated 6.9 million dependents lost insurance coverage.

## > IDENTITY THEFT AND THE IRS

The Taxpayer First Act requires the IRS to notify parents when it detects an unauthorized use of a dependent's Social Security number. However, in 2019,

Treasury inspectors found that the IRS didn't send letters to parents of 133,864 dependents that its computers identified as employment-related identity theft victims.

## > \$1 AND \$5

According to the Federal Reserve, a \$1 bill has an estimated life span of 6.6 years. The first \$1 note was issued in 1862. The current design of the \$5 bill entered circulation in 2008. It has a slightly shorter life span of 4.7 years and in 2019, a total of \$15.3 billion in \$5 bills was in circulation. Each bank note is made of a blend of 25% linen and 75% cotton and weighs approximately 1 gram.

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