ClientLine®

June 2021

CASUALTY, DISASTER AND THEFT LOSSES AFFECT TAXES

With the hurricane and wildfire seasons upon us, coupled with the risk of tornadoes and flooding, now's a good time to understand how casualty and disaster losses impact your taxes.

PRESIDENTIAL DISASTER

For 2018 – 2025, when parts of the country are declared federal disaster areas by the President, you can deduct losses you sustain to your home, personal belongings and vehicles. The damage to your property must be a result of the disaster.

CLAIMING YOUR LOSS

Typically, losses are deducted in the year of the disaster, but you can claim the loss for the preceding year by notifying the IRS and filing Form 4684.

Generally, casualty losses are an itemized deduction, so the amount of your loss must be more than 10% of your adjusted gross income. However, there are some exceptions.

The amount you can deduct is the lesser of the property's adjusted basis or the decrease in the market value due to the casualty. There are different rules for an income-producing property (e.g., rental homes). But if your insurance company reimburses you for losses, you'll have to reduce your tax loss by the proceeds you receive.

IT'S A STEAL

When you're the victim of theft as a result of a federally declared disaster, your loss is generally tax deductible under the same rules. Only, you'll claim the loss in the year you discover it.

PREVENTION

Although you may want to take preventative measures to protect against future disasters, like installing hurricane-impact windows, these costs won't be tax deductible since they don't meet the "sudden, unexpected, or unusual" requirement of a casualty loss. But these preventative measures may earn you a discount on your property insurance premiums.

TAXABLE GAINS

Keep in mind you can have casualty gains — like when your insurance company pays you more than your cost of the damaged or stolen property. In most cases, you'll pay tax on the difference. In limited circumstances, the gain can be deferred or not realized at all. But you'll be able to offset it with any losses you have—casualty or non-casualty. Consult your tax professional to get it right.

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Be Prepared

Natural and human-made disasters can strike anywhere and anytime. Here are ways your business can be prepared.

- Identify all your risks. Hurricanes, floods and wildfires may be on your list. But consider prolonged power outages and cyber threats.
- Develop an emergency plan, communicate employees' responsibilities and have alternate locations where you can work.
- Design a process for how to return to normal afterwards. Consider ways to compensate for lost revenue and other damages.
- Store computer files off site and/or in the Cloud. Draft a detailed IT recovery plan.
- Map out evacuation routes in your building and practice them with your staff. Train employees on what to do should a crisis occur.
- Consider having emergency kits or supplies on hand like batteries, first aid supplies, flashlights, and extra building and office keys.

UNDERSTANDING PAYROLL TAXES

Whether you're hiring your first employee or already have a few, understanding payroll taxes is a must.

FICA & FUTA

FICA stands for Federal Insurance Contributions Act and it funds the Social Security and Medicare programs. It's funded equally by the employer and employee. For 2021, each pays Social Security tax of 6.2% on the first $142,800 of an employee's wages and 1.45% on all wages. Each year, the wage base (the maximum earnings subject to Social Security tax) is adjusted for inflation. Self-employed taxpayers will pay both the employer and employee portion but they'll receive a deduction on their tax return for the employer portion.

Federal unemployment tax (FUTA) is paid by the employer and provides benefits to workers who become unemployed through no fault of their own. In 2021, the tax rate is 6% on the first $7,000 of each employee's salary. Credits for paying state unemployment tax on time are available and can reduce this rate significantly.

THERE'S MORE

Some employees will have to pay the Additional Medicare tax depending on their tax filing status and their taxable income. Employers need to withhold this tax from pay checks for employees who earn more than $200,000 a year. The tax rate for 2021 is 0.9% of the excess wages.

GET FIT

Federal income tax (FIT) is taken out of an employee's pay to cover their annual tax liability. How much taken out is based on information from the employee's Form W-4, which they should fill out when they start a new job or anytime their circumstances change that might impact how much tax they owe.

FILE & PAY

The most common payment frequencies are monthly or semi-weekly. However, quarterly or annual payments are allowed for FUTA.

Quarterly payroll tax returns are needed for FICA, FIT, and the Additional Medicare tax. FUTA returns will be filed quarterly or annually, depending on your payment frequency.

IN A STATE

Payroll taxes extend beyond the federal level to the state level. Depending on your state, you may have to withhold state income tax from employees' paychecks. And all states have an unemployment tax that employers pay. Some cities have payroll taxes too.

Client PROFILE...

Andrea will start a new job in Spain in a few months and she's not sure if she will still have to file taxes in the U.S.

The United States (U.S.) is one of a few countries that tax citizens on their worldwide income. So even though she lives and works outside the states, she'll need to file a tax return.

Andrea may qualify for the foreign earned income exclusion, if she's a bona fide resident of Spain. This requires that she live there for an entire tax year. Otherwise, she'll have to be out of the U.S. for 330 days during any consecutive 12-month period to qualify. This excludes the first $108,700 of her wages from U.S. tax for 2021, based on the theory that she probably paid income tax in Spain. If her wages exceed the exclusion threshold, she may be able to claim a tax deduction or tax credit for any income taxes she paid in Spain. This allows her to avoid the burden of double taxation. It's important to consult a tax professional prior to leaving the states.

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

CHARITABLE REMAINDER TRUSTS FOR INHERITED IRAS

With the stretch IRA now a thing of the past, how will you pass on your IRAs? Charitable remainder trusts (CRT) give you some control and options.

10-YEAR RULE

Under the SECURE Act, with limited exceptions, non-spousal beneficiaries of tax-deferred IRAs have to withdraw all funds within ten years of inheritance. No longer can withdrawals be limited to the required minimum distribution amount and stretched out over a lifetime.

A CRT is set up to distribute a fixed percentage of the funds to beneficiaries in either a lump sum on the date the IRA is inherited by the trust or periodically over a maximum of 20 years. The remaining IRA balance is given to charity. Under either distribution method, at least 10% of the IRA value, when it passes to the trust, must be given to charity.

GIVE IT AWAY

By naming the CRT as the beneficiary of your IRA, the trust can be a valuable tool to let certain beneficiaries enjoy the IRA funds over a longer period of time.

MORE BENEFITS

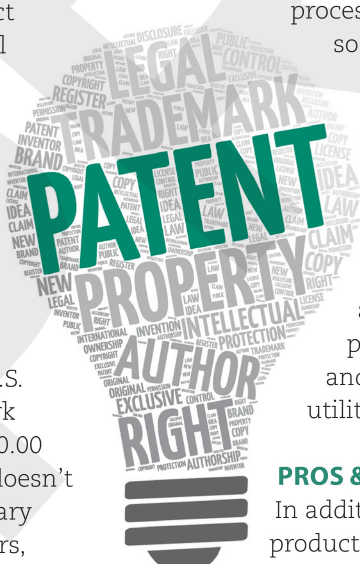
The trust funds are protected from you and your beneficiaries' creditors when placed in a trust. And with the transfer to the trust, the IRA funds are removed from your estate and won't be subject to estate tax.

UNDERSTANDING PATENTS

Have you ever considered getting a patent for an innovative idea or product? There are different types of patents, so work with a patent attorney.

INVENTIONS

Utility patents protect the creation of useful products, processes or machines. It provides legal protection for up to 20 years should anyone copy your invention without a licensing agreement with you. Initial filing fees with the U.S. Patent and Trademark Office range from $80.00 to $860.00, but that doesn't include the preliminary search for competitors, examination and maintenance fees which can tack on thousands more. Application processing can take a long time, so start early if you have a patentable product.



PROTECTING DESIGNS

If you want to protect an item's design or aesthetics, not how it is produced, you'll need a design patent. These patents have a 14-year life and overall cost is less than a utility patent.

PROS & CONS

In addition to protecting your product from copycats, a patent also can increase your chance of selling your idea.

... Q&A

Q **Can I choose my tax filing status?**

A Generally, your marital status on December 31 determines your filing status for that year. And choosing the proper status affects the amount of tax you'll owe. When multiple filing statuses apply, select the one that results in the least amount of tax due.

If you're unmarried, you'll generally file as single unless you have a dependent; then you may be able to file as head of household. And if you become a widow or widower, but don't remarry and have a dependent, you may claim the Qualified Widow(er) status for the two tax years after your spouse passes, which gives you the same tax perks as married filing jointly. Married taxpayers can file a joint return or file separately. Married filing separately can be used when it results in less tax owed or when one spouse wants to be responsible for their own tax.

Q **I am a sole proprietor but need to hire an employee. Are fringe benefits taxable to my employee?**

A As a general rule, all fringe benefits are taxable to your employee unless the IRS has expressly excluded them. Common fringe benefits that are tax free include health insurance, life insurance, employee discounts, employer-provided cell phones, certain commuting benefits, and ***de minimis*** (minimal) benefits like small non-cash holiday gifts or office-supplied coffee and drinks.

ClientLine® SHORT BITS...

> STATE BUDGETS
While many states prepared for a substantial revenue shortfall in 2020 due to the effects of the pandemic, states only saw a 1.6% revenue decline according to the National Association of State Budget Officers. Vermont, Colorado, and Alabama experienced revenue increases of more than 3%, boosting the national average. States are expecting a 4.4% decline for the fiscal year ending on June 30, 2021.

> RECORD BREAKERS
Consumer debt totaled $14.6 trillion at the end of 2020 according to the Federal Reserve. Historically low mortgage interest fueled the rise in debt. Mortgage debt passed $10 trillion for the first time and rose at the fastest pace since 2006. Credit card debt declined by $108 billion in 2020, while student loans and auto loans increased slightly.

> BACK TAXES
A report from the Treasury Inspector General for Tax Administration revealed that nearly 700,000 taxpayers who earn more than $200,000 annually owed the IRS $38.5 billion as of May 2019. But the majority, 69%, owed less than $25,000 each. And high-income taxpayers, those making at least $1.5 million a year, paid just 30% of the taxes they owed, leaving about $2.4 billion still due.

> FINAL NUMBERS
The final 2020 numbers for the airline industry are in. According to the Bureau of Transportation Statistics, U.S. airlines carried 557 million fewer passengers in 2020 than in 2019, a 60% decline. In 2019, U.S. airlines carried 927 million passengers. Passenger air traffic in 2020 was the lowest on U.S. airlines since the mid-1980s, while April 2020 saw the lowest monthly airline fuel usage on record.