The Kiplinger Tax Letter

CIRCULATED BIWEEKLY TO BUSINESS CLIENTS SINCE 1925

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Dear Client: Washington, Feb. 7, 2020

HIGHLIGHTS

With the 2020 tax filing season under way…
And the passage of year-end tax legislation…
It's no wonder we're getting lots of questions.

I received a state tax refund last year.
Do I have to report it as income on my 1040?
It depends. If you didn't itemize deductions on your 2018 1040, then the state refund is tax-free and needn't be reported for 2019. If you itemized, then part of it may be taxable if you got a tax benefit on your 2018 1040 from overpaying your state taxes.

I didn't take the tuition deduction on my 2018 1040 because it had expired.
Now that it's retroactively revived from 2018 through 2020, how do I claim it?
By filing Form 1040-X to amend your 2018 return and attaching Form 8917. Lots of tax breaks have been brought back from the dead. If the breaks are for 2018, you'll have to decide whether filing an amended return for the year is worth the hassle.

What tax preparation software programs provide the best overall value?
Kiplinger's online editors ranked nine of the most popular ones and decided that Credit Karma's tax software program gives the most bang for the buck. The programs were reviewed based on cost, ease of use, availability of tax help, functionality, number of state returns included in the base price and other factors. Go to *https://www.kiplinger.com/links/taxsoftware* to view the full rankings.

The age for taking required minimum distributions has gone up to 72.
Does that mean that qualified charitable distributions are also pushed back?
No. People age 70½ and older can still transfer up to $100,000 annually from their traditional IRAs directly to charity. QCDs generally count as RMDs, except they are not taxable and they are not added to your adjusted gross income. Even though individuals turning 70½ in 2020 won't have to begin taking RMDs from their traditional IRAs for the year, they are still able to make QCDs in 2020.

I had uninsured personal losses from a federally declared disaster last year.
How do I report the losses on my return? Under the year-end spending law, individuals can claim uninsured casualty losses from federally declared disasters that occur between Jan. 1, 2018, and Feb. 18, 2020, in excess of a $500 threshold, even if they don't itemize. This net loss is treated as an additional standard deduction.
2019's losses can be claimed on 2018 or 2019 returns. The instructions to Form 4684 tell you how to do it. If you want to take 2019 losses on your 2018 return, you'll have to amend your 2018 return. If taking the loss on your 2019 return, you first figure the loss on the 4684 and transfer the amount to Schedule A, line 16 and write "Net Qualified Disaster Loss" on the dotted line. If you are not itemizing, then you would also put your regular standard deduction on line 16 of Schedule A and write next to it "Standard Deduction Claimed With Qualified Disaster Loss." You then combine these two amounts and transfer the total to Form 1040, line 9.

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FILING SEASON Having your refund deposited directly is the fastest way to get the money. IRS pays most refunds within 21 days. But some refunds will be held up. Filers claiming the earned income tax credit or refundable child credit will have to wait until at least early March for their refunds, or even later if they file paper returns. Measures to help detect tax identity theft and refund fraud could also result in delays.

Use the "Where's My Refund" tool on IRS's website to check on your refund.

You can ask IRS to directly deposit a refund into up to three bank accounts. They may be in your name, in your spouse's or in both names for a joint account. Taxpayers can split their refunds using tax software or by completing Form 8888. Any refund beyond the account amounts will be mailed in the form of a paper check.

PREPARERS Looking for a tax return preparer? IRS has an online directory of preparers that lists the following tax pros who have preparer tax identification numbers: Lawyers, CPAs, enrolled agents, enrolled retirement plan agents and individuals who met the requirements for the Service's voluntary annual filing-season program. The list includes names plus city and state. See *https://irs.treasury.gov/rpo/rpo.jsf*.

Tax pros worried about data theft can check the number of returns filed under their electronic filing ID numbers. To do this, go to your e-Services account and select "EFIN status." Preparers who file 50 or more returns and are attorneys, CPAs, enrolled agents or participants in IRS's voluntary annual filing-season program have another option. They can see how many electronically filed returns were done under their preparer tax ID numbers during the year. To access the information, sign in to your online PTIN account and go to "View Returns Filed Per PTIN."

A group of tax professional firms weighed in on IRS's future redesign. Their most pressing request: A dedicated Practitioner Service Division within IRS. They want this new division to improve practitioner priority phone lines, to engage with tax preparers, to have a special liaison in each division of the agency to act upon feedback from tax pros, and to provide online tax professional accounts.

SOCIAL SECURITY Individuals who've lost their SSA-1099 can obtain a replacement quickly by setting up an online Social Security account and printing the lost form. The form reports the amount of Social Security benefits received in the previous year. There's also more you can do with an online account. Go to *www.ssa.gov/myaccount*.

A reminder on overwithheld Social Security tax if you changed jobs last year. If your pay from two or more employers in 2019 exceeded the $132,900 wage base, you can claim a credit on your Form 1040 for the excess Social Security tax withheld from your wages. Report the surplus amount on Schedule 3, line 11, of the 1040.

PAYROLL TAXES Small firms have flexibility in choosing how often to file payroll tax returns. If you have a new business and expect your yearly federal employment taxes to be $1,000 or less, then you can select the option to file an annual Form 944 when you apply for an employer identification number. Those who don't check the box for annual filing will be required to submit the 941 quarterly payroll tax returns. Existing businesses that now file the 941 but meet the 944 eligibility rules can contact the Revenue Service by April 1 in a given year to request to file the 944. Firms that receive written permission from the Service can shift to annual reporting.

TAX FORMS Here's a peek at a new form that makes its debut next year: The 1099-NEC. Those who pay nonemployee compensation in excess of $600 in 2020 or later will file this form instead of the 1099-MISC. A prior version of the NEC was in use until the early 1980s. Look for the NEC form and instructions on IRS's website.

BUSINESS TAXES Net business losses on individual returns are capped. For 2019 returns, the amount of business losses that exceeds a $510,000 threshold for couples and $255,000 for other filers is nondeductible, with the excess carried forward. A business loss is the amount by which total deductions attributable to your trades or businesses exceed your total income and gains from your trades or businesses. This limitation, which was enacted under the 2017 GOP tax reform legislation, applies after application of the basis rules and at-risk and passive-activity loss rules.

Taxpayers use Form 461 to figure whether their business losses are limited. Do W-2 wages constitute trade or business income for this purpose?

It appears so. IRS's website and Publication 536 say that for this analysis, a trade or business includes being an employee. IRS training materials say that wages are attributable to a trade or business. And Form 461 has a line for wage, salary and tip income. However, the Joint Com. on Taxation, in its explanation of the tax reform law, says that income from being an employee shouldn't be included, but notes that a technical correction may be necessary to carry out that intent. So far, there have been no technical corrections by Congress and no IRS regulations.

Some filers are missing out on the 20% qualified business income deduction. Self-employeds, farmers and individual owners of partnerships, LLCs, S corporations and other pass-through firms can deduct 20% of their qualified business income, subject to limitations for upper-incomers. But not all eligible filers are taking the break. Treasury inspectors identified nearly 900,000 returns filed last year in which filers appeared to qualify for the deduction, but didn't take it for one reason or another.

IRS will step up outreach to preparers and taxpayers on this juicy tax break.

TAX DEBTS Tenancies by the entirety cannot be used to defeat IRS tax liens, an appeals court confirms, even when only one spouse owes the taxes. This precedent was set by the Supreme Court in a 2002 ruling. In the current case, only the husband owed back taxes. But the couple tried to conceal their ownership of real estate that they owned as tenants by the entirety, and it backfired on them. Only after IRS foreclosed on the realty and sold it did the wife admit to co-owning it. She argued she was owed half the sales price. The court said no because of her deceit and failure to assert her interest until after the property was sold (Bogart, 3rd Cir.).

ESTATE TAXES Distributing bequests to beneficiaries before paying IRS costs an executor, a court rules. The executor of a big estate knew additional estate taxes would be due after IRS audited the Form 706. He signed an agreement with IRS consenting to have the agency assess and collect a $200,000 estate tax deficiency. A few months later, he had the estate distribute property to himself and another heir for no consideration, which left the estate with no assets to pay its tax debt. That makes the executor personally liable for depleting the estate (Kohls, D.C., Ohio).

IRAs A compulsive gambling addiction doesn't avoid a fine on an early IRA payout. Pre-age-59½ distributions from retirement plans and IRAs are generally hit with a 10% penalty. There's an exception for people who can't do gainful activity because of a physical or mental disability that is permanent or of indefinite duration. Here, a woman's medication led to compulsive behavior and a gambling addiction, and she tapped her IRA early to pay debts. She claimed she didn't owe the 10% fine because she was disabled, but an appeals court said her condition didn't prevent her from doing regular activities. Also, the impairment was temporary (Gillette, 7th Cir.).

An IRA easing for graduate students and postdoctoral candidates: Under the SECURE Act, their taxable nontuition fellowship payments and stipends are treated as compensation for IRA purposes. So they'll be able to use those funds for making payins to traditional and Roth IRAs and build their retirement nest eggs.

VIRTUAL CURRENCY IRS is intensely interested in filers who transact in virtual currency. And it's requiring more disclosure. Starting with returns filed this year, people must answer on Schedule 1 of the 1040 whether they've received, disposed of, sold, exchanged or acquired any financial interest in virtual currency, such as bitcoin. If the answer is no, Schedule 1 is not required to be attached to the 1040 filing unless the taxpayer has income or deduction items to include on the schedule.

EXEMPT GROUPS IRS has developed an electronic version of the application for tax exemption. Applicants must now e-file the 1023 at *www.pay.gov* and pay the $600 fee. The Revenue Service has updated the form a bit and says e-filing will reduce errors and result in a smoother application process. IRS is giving groups a grace period... it will accept paper Forms 1023, as long as the submission is postmarked by April 30.

Nonprofits get guidance from IRS on how to seek refunds of overpaid UBIT... unrelated business income tax...in 2017 and 2018 as a result of the retroactive repeal of the so-called parking tax. They file an amended Form 990-T, write on the top "Amended Return — Section 512(a)(7) Repeal" and follow instructions that IRS posted on its website. Typically, filers have three years from the date of the original 990-T to seek a refund. Go to *www.kiplinger.com/letterlinks/ubitrefunds* to view the details.

IN CONGRESS People who work briefly in another state shouldn't bank on state tax relief, even though there's a bipartisan proposal in Congress to ease their load. The bill provides a uniform federal standard that bars states from taxing wages paid to nonresidents working in the state, unless they worked there for more than 30 days. The goal is to ease the filing burden for workers and to simplify withholding rules for employers. It wouldn't apply to athletes, entertainers and certain prominent figures. Of course, workers would still be taxed by their home states on out-of-state earnings.

Expect this to be placed on the back burner, especially in an election year, despite the fact that similar bills easily passed the House in 2012, 2016 and 2017.

Fixing many of the slip-ups in the tax reform law is still on Congress's plate.

A key flub is on depreciation for restaurant, retail and leasehold remodeling. It's now consolidated under the grouping of qualified improvement property (QIP). Congressional Republicans intended to give QIP a 15-year depreciable life and to make it eligible for 100% bonus depreciation. But the statutory language didn't reflect this intent. Business owners and influential lobbyist groups have clamored for a fix to this snafu since the 2017 tax legislation was first enacted.

But the forecast for a correction this year is not looking very rosy.

CAMPAIGN TAX PLANS Look for Donald Trump to announce his election campaign tax plan soon... Possibly in mid-April to coordinate with the due date of individual returns. Some ideas potentially on the table: Making permanent the individual tax provisions and business-asset expensing rules in the tax reform law. Lowering the 22% tax rate for individuals or adjusting the tax brackets. And lowering the favorable tax rates on capital gains and dividends or allowing capital gains to be indexed for inflation.

Trump will be sure to tout his plan as tax cuts for the middle class, to stand apart from Democratic candidates pushing higher taxes on upper-incomers.

Any action on the proposal would be pushed off till after the Nov. elections... assuming Trump is reelected and the GOP keeps the Senate and takes the House.

Yours very truly,

The Kiplinger Editors

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