



2020

National Income Tax Workbook

Chapter 9: Individual Issues – PART 1

Issue 2: Casualty

Losses

Pg. 302

Casualty Defined



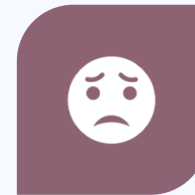
FEDERALLY DECLARED
DISASTER – WEATHER
OR ECONOMIC



SUDDEN, UNEXPECTED,
UNUSUAL, SWIFT



CAUSES DAMAGE OR
DESTRUCTION



UNEXPECTED,
UNINTENDED,
UNUSUAL EVENT



DESTRUCTION OF
PROPERTY – NOT
CAUSED BY PETS,
WILLFUL ACTS OR
WILLFUL NEGLIGENCE

Personal Property

pg 302 - 303

- I.R.C. § 165(c)(3) – losses allowable if casualty
 - 2018 thru 2025 = Federally Declared Disaster Areas only
- Calculating a loss = smaller of
 - Property's adjusted tax basis
 - Decreased in FMV
- Reduce gross loss by insurance proceeds
 - Proceeds > deductible loss = NO LOSS
 - Reportable Gain?

Loss Deduction Limits

pg 303

- \$100 for each separate casualty
- 10% of taxpayer's AGI (after \$ 100 reduction) = SUM of all personal casualty losses
- Practitioner Note: Disaster Relief Act of 2019
 - Continued until 1/19/20 & declared before 2.19.20
 - \$500 for each separate casualty & NO 10% AGI limitation even if don't itemize
 - Occurred in 2018 AND before Dec 21, 2019

Losses Offset Gains

pg 303



Examples

pg 303

Example 9.5 Personal Casualty Loss

- ✓ \$ 10,000 personal casualty loss
- ✓ \$ 85,000 AGI
- ✓ NO deductible loss (no federal disaster)

Example 9.6 Personal Casualty Loss Offset

- ✓ \$ 16,000 personal casualty gain
- ✓ \$ 10,000 personal casualty loss
- ✓ \$ 85,000 AGI
- ✓ \$ 6,100 casualty gain ($\$ 16,000 - (10,000 - 100)$)

Example 9.7 Federally Declared Disaster Loss

pg 303

- ✓ Same facts as 9.6 except
- ✓ \$ 20,000 personal casualty loss
- ✓ Federally declared disaster
- ✓ \$ 6,100 loss offsets \$ 6,100 gain
- ✓ \$ 5,300 deductible loss $[(\$ 20,000 - 100) - \$ 6,100 \text{ gain} - \$ 8,500 \text{ AGI limit}]$

Costs Not Included in Loss

pg 303 -304

- Cleaning after casualty
- Repairing or replacing damaged/destroyed property
- Temporary housing
- Rental car
- Incidental expenses
- Decreased FMV = substantiation

PRACTITIONER NOTE

Protective Measures

The taxpayer cannot include in a casualty loss deduction the cost of proactive measures taken to protect personal property from a potential casualty loss. Such measures include boarding up windows in anticipation of a hurricane and sand-bagging an area in anticipation of a flood. The taxpayer can deduct the cost to protect business property as a business expense.

Proof of Loss

pg 304

- Type of casualty and when it occurred
- And direct result of the casualty
- That taxpayer owned the property (or, if the taxpayer leased the property, that the taxpayer was contractually liable to the owner for the damage)
- Whether there is a reasonable expectation of recover from a claim for reimbursement



Calculating a Gain

pg 304

- Involuntary conversion rules
 - Reinvest in similar or related use property
 - Replacement period
 - 2 years after year of gain
 - 4 years after year of loss
- Treas. Reg. § 1.1033(a)-2(b) – nonrecognition of gain is mandatory if property is involuntarily or compulsorily converted

Example 9.8

pg 304 - 305

- 2020 Hurricane destroyed garage
- Basis \$ 15,000
- Insurance proceeds \$ 35,000
- Rebuild costs \$ 45,000
- Deferred Gain = \$ 20,000 (35,000 – 15,000)

FIGURE 9.2 Statement re Deferral of Casualty Gain

Deferral of Casualty Gain under I.R.C. § 1033	
On February 8, 2020, Jenna Silverstein realized a casualty gain from the collapse of a garage caused by a hurricane. The taxpayer postpones this casualty gain and has purchased replacement property that is similar or related in use.	
Insurance proceeds received	\$35,000
Adjusted tax basis	(15,000)
Gain realized	\$20,000
Gain deferred	(20,000)
Gain recognized	\$ 0
Cost of replacement property (garage)	\$45,000
Gain deferred	(20,000)
Basis of replacement property	\$25,000

Reporting Individual Losses & Gains pg 305

- Form 4684, Section A
- I.R.C. § 165 = ordinary
- Form 1040, Schedule A if loss
- Form 1040, Schedule D if gain

Example 9.9 Casualty Loss

pg 305

- 2020 Tornado
- Federally declared disaster area
- Personal residence and personal property destroyed
- Coin collection
- Gain from insurance proceeds

FIGURE 9.3 Tornado Damaged Personal Property

Item	Date Acquired	Adjusted Basis	FMV Before	FMV After	Difference In FMV	Insurance Payment	Gain or (Loss)
House, land, and trees	2/01/2007	\$287,000	\$523,000	\$235,000	\$288,000	\$257,000	\$ (30,000) ¹
Household items	Various	86,878	65,000	0	65,000	50,000	(15,000) ²
Coin collection	Various	3,546	6,000	0	6,000	6,000	2,454 ³
Anne's car	7/19/2018	14,000	13,000	0	13,000	0	(13,000) ⁴

¹ \$257,000 insurance proceeds – \$287,000 adjusted basis (\$287,000 cost basis is less than the \$288,000 reduction in FMV)

² \$50,000 insurance proceeds – \$65,000 decrease in FMV (\$65,000 decrease in FMV is less than the \$86,878 adjusted basis)

³ \$6,000 insurance proceeds – \$3,546 adjusted basis (\$3,546 adjusted basis is less than the \$6,000 decrease in FMV)

⁴ \$0 insurance proceeds – \$13,000 decrease in FMV (\$13,000 decrease in FMV is less than the \$14,000 adjusted basis)

FIGURE 9.4 Form 4684, Casualties and Thefts, Section A, Personal Use Property

Form **4684** **Casualties and Thefts** OMB No. 1545-0177

▶ Go to www.irs.gov/Form4684 for instructions and the latest information. ▶ Attach to your tax return. ▶ Use a separate Form 4684 for each casualty or theft.

Department of the Treasury Internal Revenue Service 2019 Attachment Requirements Exp. 2/5

Name(s) shown on tax return: Charles and Marie Seddel Identifying number: XXX-XX-XXXX

SECTION A – Personal Use Property (Use this section to report casualties and thefts of property **not** used in a trade or business or for income-producing purposes. You must use a separate Form 4684 (through line 12) for each casualty or theft event involving personal use property. **If reporting a qualified disaster loss, see the instructions for special rules that apply before completing this section.**)

If the casualty or theft loss is attributable to a federally declared disaster, check here and enter the FEMA disaster declaration number. (See instructions.) DR-4478

1 Description of properties (show type, location city, state, and ZIP code, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft. If you checked the box and entered the FEMA disaster declaration number above, enter the ZIP code for the property most affected on the line for Property A.

	Type of Property	City and State	ZIP Code	Date Acquired
Property A	PERSONAL RESIDENCE	SLIPPERY ROCK, MISSISSIPPI	38618	02/01/2007
Property B	PERSONAL HOUSEHOLD ITEMS	SLIPPERY ROCK, MISSISSIPPI	38618	VARIOUS
Property C	COIN COLLECTION	SLIPPERY ROCK, MISSISSIPPI	38618	VARIOUS
Property D				

	Properties			
	A	B	C	D
2 Cost or other basis of each property	2 297,000	86,878	3,548	
3 Insurance or other reimbursement (whether or not you filed a claim) (see instructions). Note: If line 2 is more than line 3, skip line 4.	3 237,000	50,000	6,000	
4 Gain from casualty or theft. If line 3 is more than line 2, enter the difference here and skip lines 5 through 8 for that column. See instructions if line 3 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year.			2,454	
5 Fair market value before casualty or theft	5 323,000	65,000		
6 Fair market value after casualty or theft	6 235,000	0		
7 Subtract line 6 from line 5	7 88,000	65,000		
8 Enter the smaller of line 2 or line 7	8 297,000	65,000		
9 Subtract line 3 from line 8. If zero or less, enter -0-	9 30,000	15,000		
10 Casualty or theft loss. Add the amounts on line 9 in columns A through D				10 45,000
11 Enter \$100 (\$500 if qualified disaster loss rules apply; see instructions)				11 100
12 Subtract line 11 from line 10. If zero or less, enter -0- Caution: Use only one Form 4684 for lines 13 through 15.				12 44,900
13 Add the amounts on line 4 of all Forms 4684				13 2,454
14 Add the amounts on line 12 of all Forms 4684. If you have losses not attributable to a federally declared disaster, see the instructions. Caution: See instructions before completing line 15.				14 47,354
15 • If line 13 is more than line 14, enter the difference here and on Schedule D. Do not complete the rest of this section. • If line 13 is equal to line 14, enter -0- here. Do not complete the rest of this section. • If line 13 is less than line 14, and you have no qualified disaster losses subject to the \$500 reduction on line 11 on any Form(s) 4684, enter -0- here and go to line 16. If you have qualified disaster losses subject to the \$500 reduction, subtract line 13 from line 14 and enter the smaller of the difference or the amount on line 12 of the Form(s) 4684 reporting those losses. Enter that result here and on Schedule A (Form 1040 or 1040-SR), line 16, or Form 1040-NR, Schedule A, line 7. If you claim the standard deduction, also include on Schedule A (Form 1040 or 1040-SR), line 16, the amount of your standard deduction (see the instructions for Forms 1040 and 1040-SR). Do not complete the rest of this section if all of your casualty or theft losses are subject to the \$500 reduction.				15 0
16 Add lines 13 and 15. Subtract the result from line 14				16 47,354
17 Enter 10% of your adjusted gross income from Form 1040 or 1040-SR, line 8b, or Form 1040-NR, line 35. Estates and trusts, see instructions				17 15,800
18 Subtract line 17 from line 16. If zero or less, enter -0-. Also, enter the result on Schedule A (Form 1040 or 1040-SR), line 15, or Form 1040-NR, Schedule A, line 5. Estates and trusts, enter the result on the "Other deductions" line of your tax return				18 31,554

For Paperwork Reduction Act Notice, see instructions. Cat. No. 12997D Form **4684** (2018)

Topics on pg 308

- Multiple Casualties during the year
- Mixed-Use Property
- Timing & Deductibility of Losses
- Reimbursement $<$ expected = Loss
- Reimbursement $>$ expected = Additional Income

Polling Question 1

When multiple casualties occur within the same year the \$100 floor limitation _____.

- a. Is deducted from only one of the events.
- b. Isn't deducted for personal losses.
- c. Is deducted from each of the events.

Temporary Living Expenses pg 308

- I.R.C. § 123 – insurance reimbursement excluded from income
- Costs = actual temporary living expenses - household's normal expenses
- Expenses = rent, meals, utilities, transportation, laundry, misc
- Excess payments = taxable income

Example 9.10
Reimbursed
Temp. Living
Exp

Facts same as 9.9

Insurance proceeds for Temp Living = \$
15,900

Normal living costs = \$ 10,000

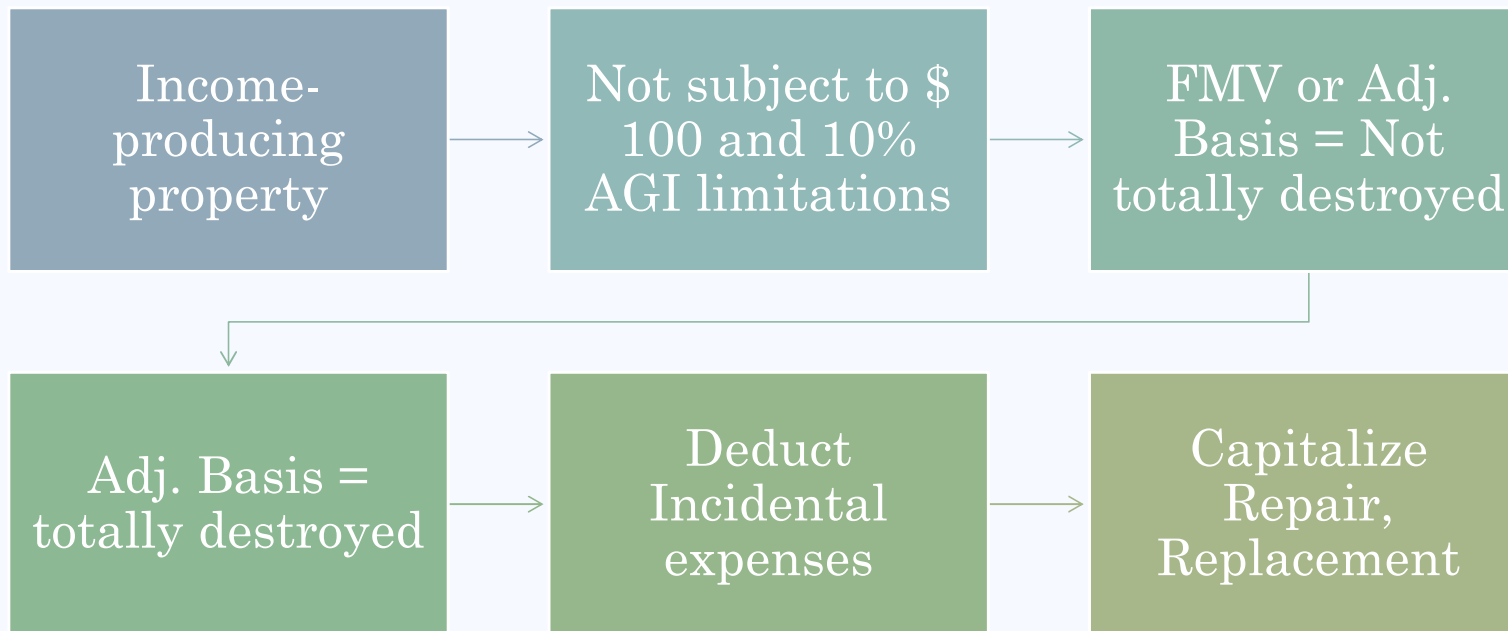
Actual Temp Living costs = \$ 14,500

Exclude \$ 4,500 (14,500 – 10,000)

Taxable Income = \$ 11,400 (15,900 –
4,500)

Business Property

pg 309



Deduction of Loss

pg 309



Form 4684,
Section B



Investment – Form
1040, Schedule A



Business Property –
form 4797

PRACTITIONER NOTE

Passive Activity Loss Limits

Treas. Reg. § 1.469-2(d)(2)(xi) excepts casualty losses from the passive activity loss deduction limits.

PRACTITIONER NOTE

Casualty Gain

Prior use of the section 179 expense election and accelerated depreciation frequently results in a casualty gain. However, the taxpayer may be able to defer that gain if he or she purchases replacement property. The deferral of gain is discussed later in this section.

Example 9.11
Trade or Business
Prop. Loss

pg 309

- 2015 Purchased Business Building
= \$ 245,000
- Adj. Basis = \$ 225,000
- 2020 tornado destroyed building
- Insurance proceeds = \$ 155,000
- Loss = \$ 57,377 (212,377 – 155,000)
- Form 4684, Schedule B

FIGURE 9.5 Form 4684, Casualties and Thefts
Section B, Business and Income-Producing Property

Name(s) shown on tax return. Do not enter name and identifying number if shown on other side. Charles and Marie Seidel		Identifying number 999-99-9999			
SECTION B—Business and Income-Producing Property					
Part I Casualty or Theft Gain or Loss (Use a separate Part I for each casualty or theft.)					
10 Description of properties (show type, location, and date acquired for each property). Use a separate line for each property lost or damaged from the same casualty or theft. See instructions if claiming a loss due to a Ponzi-type investment scheme and Section C is not completed.					
Property A	WAREHOUSE BUILDING, SLIPPERY ROCK, MD, 2/10/2012				
Property B					
Property C					
Property D					
		Properties			
		A	B	C	D
20 Cost or adjusted basis of each property	20	212,377			
21 Insurance or other reimbursement (whether or not you filed a claim). See the instructions for line 3. Note: If line 20 is more than line 21, skip line 22.	21	155,000			
22 Gain from casualty or theft. If line 21 is more than line 20, enter the difference here and on line 29 or line 34, column (c), except as provided in the instructions for line 32. Also, skip lines 23 through 27 for that column. See the instructions for line 4 if line 21 includes insurance or other reimbursement you did not claim, or you received payment for your loss in a later tax year.	22				
23 Fair market value before casualty or theft	23	225,000			
24 Fair market value after casualty or theft	24	0			
25 Subtract line 24 from line 23	25	225,000			
26 Enter the smaller of line 20 or line 25. Note: If the property was totally destroyed by casualty or lost from theft, enter on line 26 the amount from line 20.	26	212,377			
27 Subtract line 21 from line 26. If zero or less, enter -0-	27	57,377			
28 Casualty or theft loss. Add the amounts on line 27. Enter the total here and on line 29 or line 34 (see instructions)	28				57,377
Part II Summary of Gains and Losses (from separate Parts I)		29 Losses from casualties or thefts		30 Gains from casualties or thefts includable in income	
30 Identify casualty or theft		(i) Trade, business, rental, or royalty property		(ii) Income-producing property	
Casualty or Theft of Property Held One Year or Less					
29					
30 Totals. Add the amounts on line 29	30				
31 Combine line 30, columns (i) and (ii). Enter the net gain or (loss) here and on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions	31				
32 Enter the amount from line 30, column (ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040 or 1040-SF), line 16, or Form 1040-NR, Schedule A, line 7. (Do not include any loss on property used as an employee.) Estates and trusts, partnerships, and S corporations, see instructions	32				
Casualty or Theft of Property Held More Than One Year					
33 Casualty or theft gains from Form 4797, line 32	33				
34 TORNADES			57,377		
35 Total losses. Add amounts on line 34, columns (i) and (ii)	35		57,377		
36 Total gains. Add lines 33 and 34, column (i)	36				
37 Add amounts on line 35, columns (i) and (ii)	37				-57,377
38 If the loss on line 37 is more than the gain on line 36: a Combine line 35, column (i) and line 36, and enter the net gain or (loss) here. Partnerships and S corporations, see the Note below. All others, enter the amount on Form 4797, line 14. If Form 4797 is not otherwise required, see instructions	38a				-57,377
b Enter the amount from line 35, column (ii) here. Individuals, enter the amount from income-producing property on Schedule A (Form 1040 or 1040-SF), line 16, or Form 1040-NR, Schedule A, line 7. (Do not include any loss on property used as an employee.) Estates and trusts, enter on the "Other deductions" line of your tax return. Partnerships and S corporations, see the Note below	38b				
39 If the loss on line 37 is less than or equal to the gain on line 36, combine lines 36 and 37 and enter here. Partnerships, see the Note below. All others, enter this amount on Form 4797, line 3	39				-57,377
Note: Partnerships, enter the amount from line 38a, 38b, or 39 on Form 1065, Schedule K, line T1. S corporations, enter the amount from line 38a or 38b on Form 1120-S, Schedule K, line 10.					

Example
9.12
Rental
Property
Loss
pg 311

- Rental Home purchased \$ 185,000
- Adj. Basis \$ 121,379
- FMV \$ 245,000
- 2020 Wildfire, no insurance
- Estimated Restoration cost \$ 75,350
- Loss Deduction \$ 75,350 (lower of Adj. Basis or restoration cost)
- Adjust Basis by Loss Deduction

Example 9.13

Income- Producing Property Loss

pg 311

Gem investor

Lockbox in basement for his Gems

Basis \$ 7,855

Uninsured

2020 basement flooded and Gems lost

Loss Deduction \$ 7,855

Form 1040, Schedule A

FIGURE 9.6 Dori Frank's Schedule A (Form 1040), Itemized Deductions

Casualty and Theft Losses	15 Casualty and theft losses) from a federally declared disaster (other than net qualified disaster losses). Attach Form 4684 and enter the amount from line 18 of that form. See instructions	15	28,647
Other Itemized Deductions	16 Other—from list in instructions. List type and amount ▶ FORM 4684, INCOME PRODUCING PROPERTY 7,855	16	7,855

OBSERVATION

Income-Producing Property Losses

Losses on income producing property are miscellaneous itemized deductions that are not subject to the 2%-of-AGI reduction. Income producing property for this purpose is property held for investment. Because the IRS considers rental real estate to be business property for a casualty loss deduction, taxpayers can deduct a rental property loss even if they did not itemize deductions.

Deferral of Gain

pg 312



Reimbursement =
similar property



Basis in new property
= Adj. of replaced
property



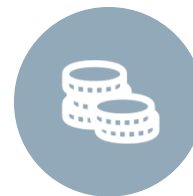
Realizes & Reports
Gain = money or
unlike property
received



Deferred Gain =
similar property



Postponed Gain – only
if cost of replacement
= reimbursement
amount



Excess
Reimbursement =
included income

- 2 years after close of 1st tax year of realized gain
- 4 years following loss of main home in Federally Declared Disaster Area
- Extension of replacement period – apply to IRS
 - Limited to not more than 1 year
 - Construction of replacement period – IRS may grant extension

Replacement Property pg 312

- Specified use, purpose & similar
- Cannot be gifted or inherited
- Can use borrowed funds
- Federally declared disaster area

- Purchased Truck \$ 46,500
- Business Use
- Elected § 179
- Adj. Basis = \$ 0
- 2020 Mudslide
- Federally declared disaster area
- Insurance Proceeds \$ 32,000
- Gain = \$ 32,000 (Insurance Proceeds – Adj. Basis)
- Ordinary Gain - § 1245 Recapture
- Form 4797, Part III

Example 9.14
Basis of
Replacement
Property pg 313

FIGURE 9.7 Samantha Saunders's Form 4797, Part III

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255
(see instructions)

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)				
A 2019 FORD F350	2/01/2019	2/10/2020				
B						
C						
D						
These columns relate to the properties on lines 19A through 19D. ▶			Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20		32,000			
21 Cost or other basis plus expense of sale	21		46,500			
22 Depreciation (or depletion) allowed or allowable	22		46,500			
23 Adjusted basis. Subtract line 22 from line 21.	23		0			
24 Total gain. Subtract line 23 from line 20	24		32,000			
25 If section 1245 property:						
a Depreciation allowed or allowable from line 22	25a		46,500			
b Enter the smaller of line 24 or 25a	25b		32,000			
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.						
a Additional depreciation after 1975. See instructions	26a					
b Applicable percentage multiplied by the smaller of line 24 or line 26a. See instructions.	26b					
c Subtract line 26a from line 24. If residential rental property or line 24 isn't more than line 26a, skip lines 26d and 26e	26c					
d Additional depreciation after 1969 and before 1976	26d					
e Enter the smaller of line 26c or 26d	26e					
f Section 291 amount (corporations only)	26f					
g Add lines 26b, 26e, and 26f	26g					
27 If section 1252 property: Skip this section if you didn't dispose of farmland or if this form is being completed for a partnership.						
a Soil, water, and land clearing expenses	27a					
b Line 27a multiplied by applicable percentage. See instructions	27b					
c Enter the smaller of line 24 or 27b	27c					
28 If section 1254 property:						
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, mining exploration costs, and depletion. See instructions	28a					
b Enter the smaller of line 24 or 28a	28b					
29 If section 1255 property:						
a Applicable percentage of payments excluded from income under section 126. See instructions	29a					
b Enter the smaller of line 24 or 29a. See instructions	29b					
Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.						
30 Total gains for all properties. Add property columns A through D, line 24	30		32,000			
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31		32,000			
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32					0

- Same facts as 9.14
- Replaces truck by 2020
 - Any tangible business property
 - Postponed gain
- Adj. Basis of replacement property = purchase price – insurance proceeds
 - New truck \$ 48,000
 - Adj. Basis = \$ 16,000 (\$ 48,000 – 32,000)
- If NOT Federally declared disaster area – replacement property = similar property

Example 9.15

pg 315

Loss of Inventory
pg 315

Reporting Method 1:

- Record loss as increased COGS
- Gross Income = insurance proceeds, sales, reimbursements
- Cannot claim Casualty Loss

Reporting Method 2:

- Deduct loss separately
- Form 4684
- Removes from COGS
- Form 4684 = Reimbursements received

Example 9.16
pg 315

- Business in Federally declared disaster area
- Kitchen cabinets = \$ 38,000
- Storm damage = \$ 6,500
- Labor & Material cost = \$ 6,500
- Sold cabinets for \$ 18,000
- Net loss = \$ 26,500 ($\$ 18,000 - 38,000 - 6,500$)
- Report on Form 1040, Schedule C
 - COGS = \$ 44,500 ($\$ 38,000 + 6,500$)
 - Income = \$ 18,000
- OR Report on Form 4684, Section B
 - Nothing on Schedule C
- Practitioner Note: Timing Differences

Issue 3: Disaster Relief

Pg. 316

- Federal Emergency Management Agency (FEMA) – administers relief
- 2020 Nationwide Emergency -- § 501(b)
 - Due to COVID-19

Robert T. Stafford
Disaster Relief &
Emergency
Assistance Act
(Act 42 U.S.C.
Chapter 68)

Casualty Loss NOT in Book

- **Michigan federally declared disaster in 2020**
- **Flooding & Severe Storms**

EM-3525-MI Midland & Gladwin

DR-4547 Midland, Gladwin, Arenac, Iosco, Saginaw

Michigan Disasters 2020

- [Michigan SEVERE STORMS AND FLOODING \(DR-4547-MI\)](#)
 - Incident Period: May 16, 2020 - May 22, 2020 Major Disaster Declaration declared on July 9, 2020
- [Michigan SEVERE STORMS AND FLOODING \(EM-3525-MI\)](#)
 - Incident Period: May 16, 2020 and continuing Emergency Declaration declared on May 21, 2020
- [Michigan COVID-19 PANDEMIC \(DR-4494-MI\)](#)
 - Incident Period: January 20, 2020 and continuing
 - Major Disaster Declaration declared on March 27, 2020
- [Michigan COVID-19 \(EM-3455-MI\)](#)
 - Incident Period: January 20, 2020 and continuing
 - Emergency Declaration declared on March 13, 2020

Polling Question 1

A Federally Declared Disaster Area may be due to:

- a. Tornado
- b. Flood
- c. Economic
- d. All of the above

Disaster Relief Payments

pg 317

Grants

Loan
Cancellation

Qualified
Disaster
Relief

Qualified
Disaster
Mitigation

Stimulus
Payment

Practitioner Note – Relief Programs

Small Business Administration Programs

Paycheck Protection (PPP) Chap. 16

Economic Disaster Relief Loans (EIDL)

EIDL Advance

- Under Disaster Relief Act –
NO COD on forgiveness
 - Reimbursement for the loss
 - Reduces casualty loss deduction

Federal Loan
Canceled
pg 316

- Not included in income
- Eligible expense
 - Reasonable and necessary personal, family, living, or funeral expenses incurred as a result of the qualified disaster
 - Reasonable and necessary expenses for repair or rehabilitation of a personal residence (rented or owned) to the extent the need for repair or rehabilitation is attributable to the qualified disaster
 - Reasonable and necessary expenses for repair or replacement of the contents of a personal residence to the extent the need for repair or replacement is attributable to the qualified disaster
- Payments to promote the general welfare by federal, state or local governments
- Practitioner Note: COVID-19 Employer Relief

Qualified Disaster Relief Payments

Qualified Disaster Mitigation Payments

Excludable from income
AND no basis adjustment

Does not apply to amounts
from sale or disposition

- 2020 FEMA Grant to elevate the house
- Form 1099 received – “other income”
- Excludable income
- No basis Adj. of the home

Example 9.17 Flood Hazard Mitigation

Practitioner

Note —

Grants to
Business
pg 317

- NOT excludable
- I.R.C. § 139 – applies only to individuals
 - not for general welfare
- I.R.C. § 1033 – elect to defer gain realized

Principal Residence in a Disaster Area – Gain Recognition

pg 318

No recognized gain – unscheduled
personal property

Single item of property, similar or related
in use

Replacement period 4 years after end of
year gain realized

- Principal residence
- 2020 flood – federally declared disaster
- Insurance proceeds = \$ 200,000
- Unscheduled personal property proceeds = \$ 25,000
- Scheduled personal property proceeds = \$ 5,000 Jewelry & \$ 10,000 stamp collection
- No gain on unscheduled personal property
- Postponed gain \$ 215,000

Example 9.18 Insurance Gain in Disaster Area

pg 318

Polling Question 2



The replacement period for a taxpayer's main home destroyed in a federally declared disaster area is:

- a. 2 years
- b. 3 years
- c. 4 years
- d. There is no replacement period on a main home

- 1 year for most affected by federally declared disaster area
- Abatement of interest & penalties
- If qualify write reason in margin of tax return, ex. “Texas Tornadoes”
- Affected Taxpayers:
 - Main home in covered disaster area
 - Business entity or sole proprietorship principal place of business in covered disaster area
 - Relief worker assisting victims in covered disaster area
 - Individual, business entity or sole proprietorship whose records were in covered disaster area
 - Estate or trust whose records were in covered disaster area
 - Spouse on a joint return with a taxpayer who is eligible for postponements
 - Any other person who the IRS determines to be affected

Postponed Tax Deadlines pg 318

COVID-19 Postponements

pg 319

- July 15th
- Rev. Proc. 2018-58,
2018-50
- I.R.B. 990
- Notice 2020-23



PRACTITIONER NOTE

State Income Tax

This relief applies only to certain federal tax filing and payment deadlines. State filing and payment deadlines vary and are not always the same as the federal filing and payment deadline. Thus, the tax practitioner should check with his or her state tax agencies for information about deadlines.

CROSS-REFERENCE

Employment Taxes

See the "New Legislation: Part 2" chapter in this book for discussion of relief that allows employers to delay the deposit of certain employment taxes.

Timing of Loss Deduction

pg 319



YEAR OF LOSS



PRECEDING YEAR



ELECT PRIOR YEAR – 6
MONTH AFTER DUE
DATE

Issue 1: Health Care Deduction

Medical & Dental Expense

pg 294

- Itemized deduction subject to 7.5% of AGI
 - ~~January 01, 2019 thru~~
 - ~~December 31, 2020~~
- Health Savings Account (HSA) Contributions
- Flexible Spending Arrangements (FSA) Contributions
- Health Reimbursement Arrangement (HRA)

Example 9.1 Calculating the Deduction

- Henry & Wanda are married with one dependent child
- AGI = \$ 300,000
- Medical Expenses of \$ 30,000
- \$ 5,000 Insurance Reimbursement

How much is their eligible medical expenses if they itemize?

- \$ 25,000

How much is their allowable medical deduction if they itemize?

- \$ 2,500 ($\$ 25,000 - 300,000 \times 7.5\%$)



Definition of Medical Care

1. for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body;
2. for transportation primarily for and essential to medical care described in (1):



Definition of Medical Care

3. For qualified long-term care services [as defined in I.R.C. § 7702B(c) and discussed later]: OR
4. For insurance (including amounts paid as Medicare Part B premiums) covering medical care described in (1) or (2), or for any qualified long-term care insurance contract [as defined in I.R.C. § 7702B(b) and discussed later].



Other eligible
medical
expenses
pg 295

- Lodging
 - Away from home for essential medical care
 - Medical care provided by physician in licensed hospital (or equivalent)
 - No significant element of personal pleasure
 - \$ 50 per night per person maximum
- Prescribed Drugs
 - Prescribed by physician
 - Drug or biological used by an individual
 - I.R.C. § 216(b)
 - Not Controlled substances like Marijuana

NOT IN THE CHAPTER

Practitioner Pointer

Medical Marijuana

- Rev. Rul. 97-9. 1997-1CB77 – controlled substances are ineligible prescription drug
- Treas. Reg § 1.213-1(e)(2) – prescription must be legally procured
- Pub 502 – illegal/controlled substances are ineligible
- INFO 2010-0080 Chief Counsel Letter to Senator Schumer
 - Naturopathic care, including herbs, can qualify as medical care
 - Dickie v. Commissioner, T.C. Memo. 1999-138
 - Crain v Commissioner, T.C. Memo. 1986-138
 - Tso v Commissioner, T.C. Memo 1980-399

Capital Expenditures

pg 295

- Eye glasses
- Seeing eye dog
- Artificial teeth & limbs
- Durable medical equipment – wheelchair, crutches, inclinators or air conditioners detachable from property
- Permanent improvement or betterment of property
> increased value of the related property

Example 9.2 – Improvement to Property

- Cindy has heart disease
- Physician advises her to install an elevator
- Cost of elevator = \$ 20,000
- Increased value of residence = \$ 10,000
- Eligible medical expense = \$ 10,000 ($\$ 20,000 - 10,000$)
- Cost of installation separate from cost of elevator = 100% medical expense because it does not increase the value of the residence

Long-Term Care

pg 295

§ 213(d) – define medical services	Medically necessary diagnostic	Preventive
Therapeutic	Curing	Treating
Mitigating	Rehabilitative services	Maintenance or personal care services

Chronically Ill Individual

pg 295

- Is unable to perform (without substantial assistance from another individual) at least 2 ADL's (eating, bathing, or dressing) for a period of at least 90 days due to a loss of functional capacity;
- Has a level of disability similar to the level of disability described in (1); OR
- Requires substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment

Institution
Expenses
pg 295-296

Treas. Reg. § 1.213-
1(e)(1)(v)

Inpatient hospital care

Non-hospital Care –
Facts & Circumstances

Example 9.3 Meals & Lodging

pg 296

Patricia, 80 years old

```
graph TD; A[Patricia, 80 years old] --> B[Moved to nursing home]; B --> C[Medication management only]; C --> D[Meals & lodging are NOT medical care];
```

Moved to nursing home

Medication management only

Meals & lodging are NOT medical care

Baker v. Commissioner, 122 T.C. 143

- Independent living facility
- Percentage method to total monthly service fees
 - Allocable to medical care

Education Expenses

pg 296

- Special school for special needs individual
- Cost include:
 - Meals & lodging
 - Ordinary education
 - Medical care – cost of care and supervision, or of treatment & training, of a mentally or physically handicapped person at a school etc.

At-Home Care Expenses

pg 296-297

- I.R.C. § 262 – disallows a deduction for personal living & family expenses that are not medical
- Estate of Marantz v. Commissioner, 39 T.C.M. 515 (1979)
 - 40% Medical expense for caregivers

PRACTITIONER NOTE

Employment Taxes

In Rev. Rul. 57-489, 1957-2 C.B. 207, the IRS ruled that the FICA tax paid on an expenditure that qualifies as a medical expense is also a deductible medical expense under section 213.

Rev. Rul. 76-106, 1976-1 C.B. 71

- At-home Caregiver
- Pd wages, meals & lodging
- Apportion time between nursing-type services and other
- Portion of wages not attributed to Medical are NOT deductible
- **Example 9.4**

Qualified Long-Term Care Insurance Contract

I.R.C. § 7702B

1. The only insurance protection provided under the contract is coverage of qualified long-term care services
2. The contract does not pay or reimburse expenses incurred for services or items to the extent that such expenses are reimbursable under title XVIII of Social Security Act or would be so reimbursable but for the application of a deductible or coinsurance amount
3. The contract is guaranteed renewable
4. The contract does not provide for a cash surrender value or other money that can be paid, assigned, or pledged as collateral for a loan, or borrowed, other than certain allowed refunds
5. All refunds of premiums (other than refunds due to death of the insured or a complete surrender or cancellation of the policy), and all policy holder dividends or similar amounts, under the contract are to be applied as a reduction in further premiums or to increase future benefits
6. The contract provides certain consumer protection provisions specified in §7702B(g)

FIGURE 9.1 Maximum Deductible Long-Term Care Premiums

	2018	2019	2020
40 or less	\$420	\$420	\$430
More than 40, less than 51	780	790	810
More than 50, less than 61	1,560	1,580	1,630
More than 60, less than 71	4,160	4,220	\$4,350
More than 70	5,200	5,270	\$5,430
Maximum excludable long-term care per diem	360	370	380

Limitations on Deductible Premiums

Medical & Dental Expenses of Dependent

I.R.C. § 152
– defines
dependent

• Treas. Reg. §
1.151-2 –
income >
\$ 4,300

• Tie-breaker
rules apply

Multiple
Support
Agreements
– designee
for that
year

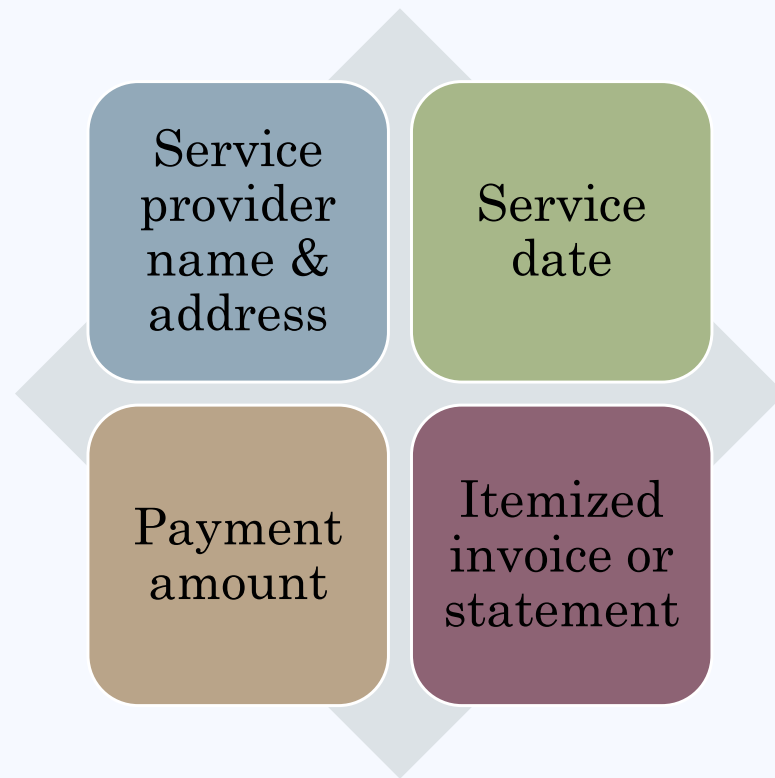
PLANNING POINTER

Medical Expense Election

Generally, unpaid medical expenses are not allowed as a deduction on the decedent's individual income tax return but are allowed as a deduction on the estate tax return. With the increased estate tax exemption amount (\$11,580,000 in 2020), most taxpayers no longer have an estate tax liability. In these cases, the executor of the estate can elect to treat any medical expenses paid from the estate within 1 year of the date of death as an itemized deduction [I.R.C. § 213(c)].



Substantiation of Deductions



Health Savings Account (HSA) pg 299

- Pretax contribution
- Rolls over to next year
- High-deductible Health Plan (HDHP)
- NO Medicare
- Not a Dependent

PLANNING POINTER

Medicare Recipient

Taxpayers enrolled in Medicare cannot contribute to an HSA, but they can use HSA contributions made prior to age 65 to pay the premiums for Medicare Part B, Part D, and Medicare Advantage plans.

HSA Contributions

pg 299

Non-taxable fringe benefit if Employer contributes

- Or Above-the-line deduction

\$ 3,550 self-only coverage

\$ 7,100 family coverage

Over age 55 = \$ 1,000 additional

Distributions from HSA

pg 299



Used exclusively for qualified medical



Non-medical expense =
20% added tax

Exceptions may apply

High-deductible Health Plan

Annual Deductibles

- \$ 1,400 Self-only
- \$ 2,800 Family
- Notice 2019-45, 2019-32 I.R.B. 593 – expands list of preventative care
 - Specified Medical Care Services – treated as preventative care for chronic condition

Flexible Spending Arrangements



EMPLOYER-
SPONSORED



USE IT OR LOOSE
IT



PRE-TAX
CONTRIBUTION



\$ 2,750 MEDICAL



\$ 5,000
DEPENDENT
CARE

CROSS-REFERENCE

Health Reimbursement Arrangements

I.R.C. § 105 allows for the reimbursement of medical expenses under an employer-sponsored health plan. Under an HRA, the employer contributes to the plan. The contributions are excluded from the employee's income. There is no limit on the employer's contribution. Distributions must be paid to reimburse the employee for qualified medical expenses of the employee and his or her spouse and dependents. Unused amounts can be carried over to the next year. See the "Business Tax Issues" chapter in this book for a discussion of HRAs.

PRACTITIONER NOTE

Self-Employed Persons

Self-employed persons are not eligible for an FSA or HRA. For fringe benefit purposes, an S corporation is treated as a partnership, and a 2% shareholder is treated as a partner of the partnership. A 2% shareholder is one that directly or constructively owns more than 2% of the corporation's outstanding stock on any day during the S corporation's tax year. Therefore, greater-than-2% shareholders of S corporations receiving W-2 wages are ineligible to participate in an FSA or HRA.

COVID-19
Plan
Relief
pg 300

- Telehealth: Notice 2020-29 & 2020-22, I.R.B. 864-- service retroactive to January 01, 2020
- HSA can pay for Over-the-Counter Medication: The CARES Act § 3702
- COVID-19 Testing & Treatment
 - Covered under plan
 - Meets HDHP minimum deductible
 - Notice 2020-15 – retroactive January 1, 2020

Polling Question 3

Funds from an HSA can be used to pay for over-the-counter medications.

True or False

Cafeteria Plan Midyear Elections pg 301

Make	Make a new election on a prospective basis, if the employee initially declined to elect employer-sponsored health coverage;
Revoke	Revoke an existing election and make a new election to enroll in different health coverage sponsored by the same employer on a prospective basis; AND
Revoke	Revoke an existing election on a prospective basis, provided that the employee attests in writing that the employee is enrolled, or immediately will enroll in other health coverage not sponsored by the employer.
Make	Make new election, decrease or increase an existing election applicable to a health FSA on a prospective basis; OR
Revoke	Revoke an election, make a new election, decrease or increase an existing election applicable to dependent care assistance on prospective basis.

Grace Period for Unused Amounts

Thru December 31, 2020

- FSA
- Dependent Care
- Carryover \$ 550

***New Law Carryover until 2022**

2020 NATIONAL INCOME TAX WORKBOOK

CHAPTER 5: IRS ISSUES

PAGES 149-192



IRS ISSUES

P. 149

Issue 1: Income Tax Withholding

Issue 2: The Gig Economy

Issue 3: Virtual Currency

Issue 4: Cybersecurity

Issue 5: Tax Transcripts

Issue 6: IRS Information Sources

NEW TAXPAYER RELIEF INITIATIVES

Issued November 2, 2020

- Short-Term IA extended from 120 days to 180 days to full pay
- IRS will incorporate some new liabilities into existing IA
- Individuals can now acquire an IA without providing financial statements as long as they owe less than \$250K and the balance will be paid within CSED
- IRS will allow individuals an IA without filling a tax lien if the balance is only for 2019 and balance is under \$250K
- Taxpayers can alter their DDIA on-line if they owe less than \$50K and want to adjust payment amounts or dates

*These only apply to cases that are not assigned to a Revenue Officer (RO)

CHAPTER 5 – POLLING QUESTION 4

Individual taxpayers that owe less than \$250K, for 2019 only, can obtain an IA without the IRS filing a Federal Tax Lien.

- A. True
- B. False

CHAPTER 5 – POLLING QUESTION 4

Individual taxpayers that owe less than \$250K, for 2019 only, can obtain an IA without the IRS filing a Federal Tax Lien.

A. True

B. False

IRS will allow individuals an IA without filling a tax lien if the balance is only for 2019 and balance is under \$250K

NEW FORM W-4

PP. 150 -151

- New hires and rehires after 2019
- May ask for new W-4 but must say it's not required
- No W-4: Single, no adjustments

Form W-4: Figure 5.1, Page 151

1. Personal information + filing status
2. Multiple jobs or spouse works: 3 options
3. Claim dependents (+ other credits)
4. Other adjustments – income, deductions, extra withholding
5. Signature

WITHHOLDING AND ESTIMATED TAXES

P. 480

Anticipated Filing Status: REG-132741-17, I.R.C. §§ 3401, 3402

- Proposed regulations provide guidance for employers on the amount of federal income tax to withhold from an employee's wages. The proposed regulations reflect that the TCJA replaced withholding exemptions with withholding allowances.
- The proposed regulations clarify that employers using the percentage method of withholding must compute the tax withholding amount based on the entry for the employee's anticipated filing status or marital status.
- To select the MFJ status on Form W-4, the employee must meet four requirements; see list
- The proposed regulations define a withholding allowance but otherwise intend to use forms, instructions, and publications to provide computational details. There are seven factors that determine the withholding allowance; see list.

NEW FORM W-4

P. 152

STEP 2: Option (a) – Most accurate, greater privacy

Use TWE to calculate additional w/h'g needed if

- Expect to work only part of the year,
- Large balance due/refund in prior year and is into the current year,
- Subject to additional taxes (e.g. additional Medicare tax)
- Has SE income, or
- Prefers the most accurate withholding

NEW FORM W-4

P. 152

STEP 2: Option (b)

Use Multiple Jobs Worksheet in Form W-4 instructions

- Table - Withholding at intersection of column and row of wage \$
- If 3 jobs → table used twice
- > 3 jobs or one with wages of > \$120,000 → Pub 505 tables

STEP 2: Option (c)

- Total of two jobs
- Standard deduction and tax brackets cut in half for each
- More withholding than needed if pay not similar

NEW FORM W-4

P. 153

STEP 3: Claim Dependents

- Child tax credit and credit for dependents
- Include other credits in line 3 total
- Complete on only one W-4

STEP 4: Other Adjustments – entered on only one W-4

4(a) Additional taxable income (not SE or other wages)

4(b) Deductions: Figure 5.2 worksheet (Item. > standard, Sch. 1 deds.)

4(c) Extra withholding: From Step 2(a) or (b), or other additional amount

NEW FORM W-4

P. 154

NOTE: Form W-4V for voluntary withholding

- May include income in 4(a) of W-4 or
- May include additional \$ in 4(c) of W-4 to cover

Exemption from withholding

- May claim exempt from withholding if:
 - No tax liability in prior year (tax = 0 or tax < certain credits) and
 - No tax liability expected in current year
- “Exempt” in space below step 4(c) + 1(a), 1(b), 5
- Must submit yearly

NONRESIDENT ALIENS – NOTICE 1392

P. 154

Step 1: Requires SSN, check single or MFS

Step 2: Only if individual has > 1 job

- Option (a) – N/A
- Option (b) - Multiple jobs worksheet for only 1 W-4
- Option (c) - Check the box on both W-4s
- “NRA” below step 4(c)

Step 3: Limited application – Pub 519 (only on 1 W-4)

Step 4: Optional (only on 1 W-4)

Exemption under tax treaty claimed on Form 8233

TAX WITHHOLDING ESTIMATOR

P. 155

- W-4/W-4P entries, paycheck checkup
- No sensitive info used, no info saved
- LTCG, AMT, qualified dividends → Use worksheets in Pub 505

Input steps (see tips):

1. Filing status, # dependents, # jobs, other income ?
2. Enter wages, other income, withholding
3. Adjustments to income
4. Deductions
5. Tax credits

TAX WITHHOLDING ESTIMATOR

PP. 155-156

- Determines EITC
- Capital gains o.k. but reduced rates not applied
- Soc sec & unemployment income if to withhold from wages
- Includes additional Medicare tax

Results:

- Estimate of tax owed/overpaid
- Downloadable Form W-4 with Step 3 and 4 entries
 - Need more w/h'g? Step 3 may show reduced credit \$
 - Need less w/h'g? Step 3 will show created credit \$

TAX WITHHOLDING ESTIMATOR

PP. 156-157

Example 5.1

Family of 4, 2 < 17 years old

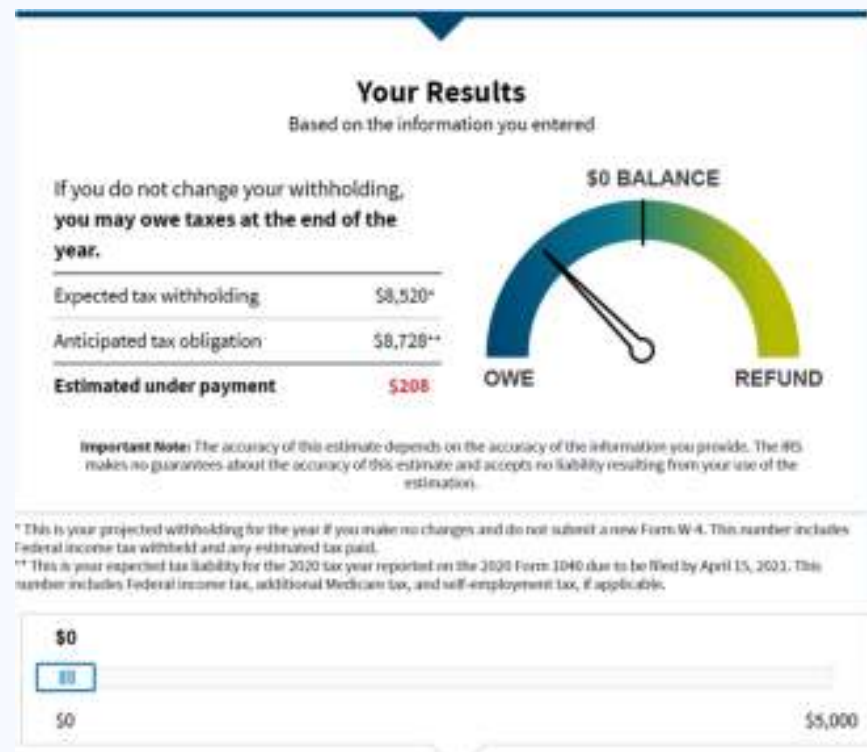
\$10,000/month, \$710 w/h'g

\$900 interest income

Running TWE in late March

Figure 5.3 – Results

Figure 5.4 – Refund option



TAX WITHHOLDING ESTIMATOR

P. 158

Figure 5.5 – TWE recommendation

- Child tax credit 3(c): \$3,727 (\$273 annual reduction)
(\$208 short/9 remaining pay periods = \$23/pay)
- Downloadable pre-filled Form W-4

INCOME TAX WITHHOLDING ASSISTANT P. 158

For employers calculating withholding using Pub 15-T

Figure 5.7 - Downloadable Excel Spreadsheet – file for each EE

Using 2020 W-4

The screenshot shows the 'Income Tax Withholding Assistant For Employers' interface. It is designed for use with both 2020 and earlier Forms W-4. The interface is divided into two main sections: input fields on the left and a results section on the right.

Input Fields (Left Side):

- Pay frequency:** Monthly
- Employee's taxable wage or salary amount this paycheck:** \$10,000
- Which version of Form W-4 did the employee use?:** 2020 or later
- Information from the employee's most recent Form W-4 if used 2020 or later version:**
 - Step 1. c. Filing status:** Married Joint
 - Step 2. Did the employee check the box in (c)?** No
 - Step 3. Total amount on line 3:** \$3,727
 - Step 4. Other adjustments:**
 - a. Other income amount:
 - b. Deductions amount:
 - c. Extra withholding amount:

Results Section (Right Side):

- RESULT**
- Amount of Federal income tax to withhold from this paycheck:** \$753
- Without no federal income tax: If on the Form W-4 the employee claimed to be exempt from withholding.*

Footer Note: This Assistant implements the 2020 IRS Publication 15-T, Federal Income Tax Withholding Methods. Enter the three items requested in the upper left corner. Fill in the relevant information from the employee's Form W-4. The amount of Federal income tax to withhold from this paycheck is provided in the lower right corner. You may save a separate copy of this calculator for each employee (to avoid having to re-enter the W-4 information each pay period).

INCOME TAX WITHHOLDING ASSISTANT

P. 160

Figure 5.8 – Using 2019 W-4

IRS Income Tax Withholding Assistant For Employers		(For use with both 2020 and earlier Forms W-4)	
Pay frequency:	<input type="text" value="Monthly"/>	RESULT	
Employee's taxable wage or salary amount this paycheck:	<input type="text" value="\$10,000"/>	Amount of Federal income tax to withhold from this paycheck:	<input type="text" value="\$747"/>
Which version of Form W-4 did the employee use?	<input type="text" value="Before 2020"/>	<i>Withhold no federal income tax if on the Form W-4 the employee claimed to be exempt from withholding.</i>	
		Please enter the W-4 information in the data fields below	
		Information from the employee's most recent Form W-4 if used a 2019 or earlier version	
		3 Filing status:	<input type="text" value="Married"/>
		5 Number of withholding allowances:	<input type="text" value="7"/>
		6 Additional amount to withhold:	<input type="text"/>

This Assistant implements the 2020 IRS Publication 15-T, *Federal Income Tax Withholding Methods*. Enter the three items requested in the upper left corner, then fill in the relevant information from the employee's Form W-4. The amount of Federal income tax to withhold from this paycheck is provided in the upper right corner. **You may save a separate copy of this calculator for each employee** (to avoid having to re-enter the W-4 information each pay period).

THE GIG ECONOMY

PP. 161-162

Gig Service Provider

- Pros: More flexibility/control – when, where, for whom, career path
- Cons: Taxes, recordkeeping, lack of benefits, less job security

Gig Service Recipient

- Pros: No benefit costs, no training cost, more flexibility
- Cons: Worker reclassification, lack of reliable/qualified workers

Gig Service Coordinator (Online Platform)

- Fee for bringing worker and consumer together
- Potential of EE treatment of service provider

THE GIG ECONOMY – TAX ISSUES

PP. 162-163

Survey of gig workers by Nat'l. Assoc. of Self-Employed found:

- 34% - had no knowledge of quarterly estimated tax rules
- 36% - had no idea of records needed for tax purposes
- 43% - had no \$ set aside for taxes & did not know how much owed
- 69% - received no tax info from platform they used

IRS Gig Economy Tax Center

- Guidance for both provider and coordinator
- Emphasis that all income taxable
- Link to IRS webinar “Understanding the Gig Economy”

THE GIG ECONOMY – TAX ISSUES WORKER CLASSIFICATION

PP. 163-164

Common-Law Rules

- Behavioral
- Financial
- Type of Relationship

Form SS-8 Determination of Work Status

- Determination applies only to worker(s) requesting it
- Not an examination – cannot compel business to change treatment

THE GIG ECONOMY – TAX ISSUES

WORKER CLASSIFICATION

P. 164

Liability if misclassified

- 100% of taxes not withheld or
- Reduced rates under §3509

FAQs on misclassification in Pub. 4341

Section 530 Relief – business will not owe employment taxes if:

- Timely filed all tax documents consistent with IC treatment
- Business/predecessor treated workers and any similar workers as IC
- Had reasonable basis for treatment – must be able to document

Worker may file SS-8 for determination even if ER has section 530 relief

THE GIG ECONOMY – TAX ISSUES

WORKER CLASSIFICATION

P. 165

Voluntary Classification Settlement Program

- Announcement 2012-45
- Treat as EE for future periods, limited tax for past
- Must not be currently under exam
- Application: Form 8952

Misclassified Worker files Form 8919 if:

- Performed services for a firm
- Believed not an IC
- Firm did not withhold soc. sec. or Medicare
- SS-8 letter or in process, other IRS stmt., W-2 & 1099 from firm

THE GIG ECONOMY – TAX ISSUES ESTIMATED TAX PAYMENTS

PP. 165-166

1. Expects to owe at least additional \$1,000 and
2. Withholding and refundable credits to be < smaller of:
 - 90% of tax to be shown on return, or
 - 100% of tax shown on prior year return (if 12-month return)
(110% if AGI > \$150,000, \$75,000 for MFS)

Determine payment needed by:

- Worksheets in Form 1040-ES
- If an EE, include in TWE calculation & adjust withholding

Direct pay (online, phone, IRS2Go), EFTPS, check or money order, cash

THE GIG ECONOMY – TAX ISSUES

RECORDKEEPING

P. 166

- Any system o.k if clearly shows business income and expenses
- Pub 583, *Starting a Business and Keeping Records*
- Retain records for:
 - At least 3 years from later of filing or due date
 - If files claim for credit or refund:
 - Later of 2 years from date tax paid or 3 years from filing
 - 7 years if worthless securities or bad debt deduction
 - Forever if fraudulent return filed

THE GIG ECONOMY – TAX ISSUES

INCOME AND SELF-EMPLOYMENT TAXES

P. 166

- All income reportable net of related expenses
- Gig worker may qualify for QBI deduction
- Self-employment tax (see IRS Self-Employed Individuals Tax Center)
 - If net income from SE \geq \$400
 - Rates applied on 92.35% of net SE income
 - 12.4% soc. sec. on up to max earnings of \$137,700 (2020)
 - 2.9% Medicare on all earnings
 - + .9% Medicare if wages + SE > \$250K (MFJ), \$125K (MFS), \$200K (others)
- **2020: Defer 50% of SE Tax: Pay $\frac{1}{2}$ by 12/31/21, other $\frac{1}{2}$ by 12/31/22

THE GIG ECONOMY – TAX ISSUES INFORMATION REPORTING

P. 168

- Form 1099-NEC : New Form to report Nonemployee Compensation
- Ceased using in 1982
- PATH Act of 2015 reintroduced need for the 1099-NEC
- Form 1099-MISC, Box 7 no longer used

CORRECTED (if checked)

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.

OMB No. 1545-0116

2020

Form 1099-NEC

Nonemployee Compensation

**Copy B
For Recipient**

This is important tax information and is being furnished to the IRS. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported.

		1 Nonemployee compensation \$	
PAYER'S TIN	RECIPIENT'S TIN	2	
RECIPIENT'S name		3	
Street address (including apt. no.)		4 Federal income tax withheld \$	
City or town, state or province, country, and ZIP or foreign postal code			
	FATCA filing requirement <input type="checkbox"/>		
Account number (see instructions)		5 State tax withheld \$ \$	6 State/Payer's state no.
			7 State income \$ \$

Form **1099-NEC**

(keep for your records)

www.irs.gov/Form1099NEC

Department of the Treasury - Internal Revenue Service

THE GIG ECONOMY – TAX ISSUES INFORMATION REPORTING

P. 168

Form 1099-NEC, Nonemployee Compensation beginning 2020

- Payments of \geq \$600

Form 1099-K, Payment Card and Third Party Network Transactions

- Issued by payment settlement entities if:
 - Gross reportable payments $>$ \$20,000 AND
 - $>$ 200 total transactions
- FAQs about Form 1099-K on IRS website

THE GIG ECONOMY – TAX ISSUES INFORMATION REPORTING

P. 168

- Should be issued when:
- Payment of \$600 or more for services in course of trade or business to someone other than an employee
- Payment to individual, partnership, estate and some corporations
- Due out by 1/31 to IRS and Recipient

CHAPTER 5 – POLLING QUESTION 5

A business that has paid Non-Employee Compensation of \$650 can choose to report it on a 1099-MISC or a 1099-NEC this year.

- A. True
- B. False

CHAPTER 5 – POLLING QUESTION 5

A business that has paid Non-Employee Compensation of \$650 can choose to report it on a 1099-MISC or a 1099-NEC this year.

A. True

B. False

False. Beginning in 2020 Non-Employee Compensation paid of \$600 or more, in the course of a business, must be reported on a Form 1099-NEC.

THE GIG ECONOMY – TAX ISSUES

P. 169

Other IRS Resources

- Small Business Taxes: The Virtual Workshop (IRS video portal)
- IRS Publication 5369, *Gig economy and your taxes; things to know*
- Webinar: “Understanding the Gig Economy” (IRS video portal)

VIRTUAL CURRENCY

P. 169

IRS Virtual Currency Campaign

- Educational letters to taxpayers began in 2019
- 45 FAQs on IRS website

Virtual Currency

- “Digital representation of value that functions as a medium of exchange, a unit of account and/or a store of value”
- Equivalent value in legal tender of any country’s currency
- Used for goods or services or held for investment
- No intrinsic value or physical form – not backed by a central bank

VIRTUAL CURRENCY

PP. 169-170

Benefits

- Transfers can be immediate
- Fees may be less than credit card fees
- No payment info to merchant → less chance of identity theft
- No exchange rates (facilitates worldwide transactions)

Obtaining virtual currency

- Purchase and sell through centralized exchanges
- Purchase in a peer-to-peer exchange
- Transfers through digital wallet
- Keys (passwords) may be stored online or offline

VIRTUAL CURRENCY TERMS

P. 170

Cryptocurrency

- Uses cryptography to secure transaction – recorded digitally
- Blockchain – example of network storing encrypted data

Coins and tokens

- Digital money created thru encryption techniques
- Token = subset of virtual currency = representation of value
- Security token → generally a share in a virtual currency company
- Utility token → grants owner access to product or service

VIRTUAL CURRENCY TERMS

P. 170

Miners

- Use of high-powered computers to solve complex equations
- Solving & validating a transaction yields digital token of the mined currency

Bitcoin ATM

- Kiosk allowing purchase of Bitcoin

Initial Coin Offering

- Offer of coin/token for fiat currency/other virtual currency
- Generally through a crowd-funding process

VIRTUAL CURRENCY TERMS

P. 170

Airdrop

- Virtual currency distribution procedure
- Tokens/coins distributed free to promote
- Reward customers of exchange/trading platforms
- Distributed on pro-rata basis to customers

Giveaway

- Fixed virtual currency amount given for account creation

VIRTUAL CURRENCY TAX RULES – NOTICE 2014-21

PP. 170-171

Virtual currency = property (rules for receipt/payment by property apply)

Currency as payment for goods or services, property – Seller

- Income = FMV of virtual currency @ time of receipt (time recorded)
 - Exchange rate used if determined by market supply and demand
 - No exchange rate → FMV of property or services exchanged
- Basis in currency received = FMV of currency used
- Gain/loss = FMV of currency less basis in property exchanged
- For services → subject to SE tax
- If investment property → ST or LT capital gain/loss
- If not investment property → ordinary income/loss

VIRTUAL CURRENCY TAX RULES – NOTICE 2014-21

P. 171

Currency as payment for goods or services – Buyer

- Gain/loss = Value received less basis in currency
 - Currency basis = FMV on date received if from a property exchange
 - Currency basis = \$ paid + acquisition costs if purchased
 - Holding period for currency used begins day after received
- Capital gain/loss (LT or ST) if currency held for investment
- Ordinary gain/loss if currency held as inventory

VIRTUAL CURRENCY TAX RULES – NOTICE 2014-21

P. 172

Identifying Units for Basis Purposes

- Can choose if can specifically identify units used in exchange
 - Unique digital identifier such as private key, public key, address
 - Records showing transaction info for all units in account, wallet, address
- If cannot identify, FIFO applies
- Must be able to show:
 - Date and time each unit acquired
 - TP's basis and FMV of each unit at time acquired
 - Date and time each unit sold, exchanged or otherwise disposed of
 - FMV of each unit when sold, exchanged, or disposed of and amount of \$ or property received for each unit

VIRTUAL CURRENCY TAX RULES – NOTICE 2014-21

P. 172

Virtual currency paid by ER as wages

- Subject to Federal and state withholding, FICA, FUTA

Gifts

- No recipient income until disposed of
- Gain: Basis = donor's basis + gift tax paid
- Loss: Basis = lesser of donor's basis or FMV @ date of gift
- No documentation of donor basis → basis = \$0
- Carryover holding period
 - No proof of donor acquisition date → period begins date after gift

VIRTUAL CURRENCY TAX RULES – NOTICE 2014-21

PP. 172-174

Third-Party Reporting

- Virtual currency and cash payments aggregated for reporting
 - 1099-NEC if \geq \$600
 - 1099-K if $>$ \$20,000 and $>$ 200 transactions

Tax Return Reporting

- Transactions reported same as if a cash transaction
- Sched 1 – Virtual currency question to be answered by all

Virtual currency payments subject to backup withholding

Same recordkeeping/penalty rules as other transactions

VIRTUAL CURRENCY

PP. 174-175

TAX RULES – REVENUE RULING 2019-24

Hard Fork

- Currency permanently diverted from legacy/existing distributed ledger
- May result in creation of a new cryptocurrency
- Legacy currency on legacy ledger, new currency on new ledger
- Income only if TP receives units of new currency (Ex. 5.5)

Airdrop

- Distribution of currency to distributed ledger addresses
- Generally received on date recorded on the distributed ledger
- TP has receipt when able to transfer, sell, exchange
- Income to TP if units of new currency received

VIRTUAL CURRENCY TAX RULES

P. 175

Donations of Virtual Currency

- Rules for donation of noncash property apply
- No gain or loss to TP
- Deduction
 - Held > 1 year = FMV date of donation
 - Held ≤ 1 year = lesser of adjusted basis or FMV
- Form 8283 filed with return
- Form 8282 filed if charity disposes of currency

CYBERSECURITY

TYPES OF CYBERATTACKS

P. 176

Types of Cyberattacks

- Unauthorized Access
- Phishing
 - Common Phishing Techniques
 - Two-Stage Phishing
- Denial of Service Attacks
- Malicious Code

CYBERSECURITY

TYPES OF CYBERATTACKS

P. 177

Phishing (report to phishing@irs.gov)

- Attempt to obtain confidential information
- Appear to be from trusted source (spear phishing)
- Pose as software or data storage provider, IRS, prospective client
- Link to fake site that looks familiar to obtain username & password
- Attachment contain malware (affects computer and network system)
- Practitioner resources (list p. 177)

Two-stage Phishing

- First: solicitation email
- Second: embedded web address or PDF attachment

CYBERSECURITY

TYPES OF CYBERATTACKS

P. 178

Denial of Service Attacks (DoS)

- Prevents access of computer system, devices
- Flood of simultaneous requests to view a web page → server crashes

Malicious Code (Malware)

- Destructive instructions to computer
- Damage, disrupt, steal, keystroke logger
- Connecting to infected external device, emails, compromised websites
- Viruses, worms, trojan horses, ransomware, spyware, adware

CYBERSECURITY PRACTITIONER DUTIES

PP. 178-179

Safeguards Rule (FTC)

- Applies to accountants, enrolled agents, other tax return preparers
- Requirements:
 - Designate employee(s) to coordinate information security program
 - Identify internal and external risks and assess current safeguards
 - Design & implement information safeguards and monitor effectiveness
 - Use service providers that can maintain safeguards – contracting for the maintenance of such safeguards
 - Evaluate and adjust security program based on circumstances
- Per violation: Fine, prison time, license revocation

CYBERSECURITY PRACTITIONER DUTIES

P. 179

Revenue Procedure 2007-40

- IRS e-file provider must have security system in place
- Mandates compliance with all IRS publications and notices re: e-file
- Diligent in recognizing, preventing, and reporting fraud and abuse
- Cooperate with IRS investigations

Information Security Plan (requirements listed p. 179)

- Employee management and training
- Information systems
- Detecting and managing systems failures

CYBERSECURITY PRACTITIONER DUTIES

PP. 179-181

IRS checklist for protecting information

1. Antivirus Software - Scan computer & attached devices for malware
2. Firewalls - Protects against outside attacker, malicious traffic
3. Two-Factor Authentication – Beyond initial username & password
4. Backup Software/Services – Encrypted with strong passwords
5. Drive Encryption – Strong passwords
6. Virtual Private Networks (VPN) – Connections over the internet

CYBERSECURITY STRONG PASSWORDS

P. 181

- Minimum of 8 characters
- Combo of letters, numbers, symbols
- Avoid personal information
- Change default/temporary passwords
- Do not reuse or update passwords
- Do not use email addresses as usernames
- Secure physical password list / password manager program
- Do not disclose passwords to anyone

CYBERSECURITY SIGNS OF DATA THEFT

PP. 181-182

- More returns filed with EFIN or PTIN than submitted
- Receive transcripts never requested
- Properly filed returns rejected because SSN already on filed return
- Authentication letters received by clients who have not filed
- Refunds received when no return filed
- Notice of online account access or account disabled
- Notice of online account when client did not create one
- Response to emails that practitioner never sent
- Office network computers running slower than normal
- Office network computers locking out tax practitioners

CYBERSECURITY

P. 182

Monitor PTIN Accounts

- Find number of returns filed (if > 50)
- Through PTIN account
 - “Additional Activities”
 - “View My Summary of Returns Filed”

Monitor EFIN Accounts

- Find number of returns filed
- Through E-Services account
 - Name – “Application” – “e-File Application”
 - Name – “EFIN Status”

CYBERSECURITY

P. 182

Data Recovery Plan

- Inventory – hardware, software applications, data
- Backup – routinely backup critical data, periodically validate
- Reinstall – maintain copies of program software
- Security Expert – consult as needed on breaches
- Testing – test plan periodically
- Reporting – report any data breach

CYBERSECURITY DATA BREACH REPORTING

PP. 182-183

- Local IRS stakeholder liaison
- Local FBI office (if directed by IRS)
- Local Secret Service office (if directed by IRS)
- Local police
- State agency where returns filed
- State attorney general
- Insurance company
- FTC at identitytheft.gov
- Three major credit bureaus

CYBERSECURITY TAXPAYER IDENTITY THEFT

PP. 183-185

- Respond immediately to any IRS notice
- Complete IRS Form 14039 (see page 184)
- Continue to file and pay taxes
- If not getting resolution: contact IRS (800) 908-4490
- Obtain the 6-digit identify protection pin (IP PIN)
 - Used for filing paper or electronic return
 - If lost/not received: “Get an IP PIN” too
 - **Can opt-in and request in IP PIN (nationwide by Jan 2021)**
(requires account on IRS.gov)

IRS Identify Theft Central at www.irs.gov/identity-theft-central

TAX TRANSCRIPTS

PP. 186-188

Masked Transcripts (Figure 5.12, p. 187)

- Personally identifiable information partially masked
- Financial data fully visible
- Currently individuals – will be business transcripts by 12/13/2020
- Can be requested through Transcript Delivery System

Figure 5.13 (p. 188) – Getting transcripts

Unmasked Transcripts

- Wage and income transcripts only
- Mailed to TPs address if requested by TP or 3rd parties
- Tax Pros – thru PPS line or Secure Object Repository mailbox (SOR)

TAX TRANSCRIPTS

P. 189

Customer File Number

- Replaces use of full SSN on 4506 series forms to enable match to a TP
- Designed for use by 3rd parties but TP & tax professional may also use
- If SSN used in number, transcript will reflect 9999999999

Transcript Delivery

- FAX to TPs, 3rd parties, Tax Pros ended 6/28/2019
- Mailing to 3rd parties ended 7/1/2019
- Mailings continue to TP's address of record
- TP: Get Transcript Online
- Tax Pros: Mail to TP, TDS for masked transcript, call IRS for SOR
- Lenders/3rd parties: Income Verification Express Service (IVES)

IRS INFORMATION SOURCES

P. 190-193

Social Media

- YouTube
- Twitter
- Facebook
- LinkedIn
- Instagram

IRS2Go – check refunds, make payment, tax help, links to social media

Podcasts (iTunes or IRS Multimedia Center)

e-News Subscriptions – 21 free registration-based (p. 192-193)

QUESTIONS???

