Alma V Guenther, EA
The Right Place
817 Missouri St, ste #2
Fairfield, CA 94533
Phone: 707-425-1865
Fax: 707-425-4342

This newsletter contains useful information and guidance about tax laws and how to avoid penalties. Don't procrastinate with your taxes! Waiting until the last minute may cause you to overlook potential tax savings and could increase your risk of making an error. You can also use the tax preparation checklist included in this letter to help you review your income and expenses for the year and collect the necessary documentation. I'm happy to answer your questions on these topics and other tax-related matters. Please call my office to schedule your appointment. I look forward to seeing you soon!

Human Nature Strikes Again! – Beware of Coronavirus Scams

It's not like we don't have enough to worry about during the unprecedented and historic year of 2020. But here's one more thing to add to the list. Coronavirus scams have emerged in significant numbers to defraud unwary taxpayers and consumers.

According to AARP, victims have reported losing more than $160 million dollars, with a median loss of $303 dollars. Ouch! Many scams are unique, but most are familiar to law enforcement and prior victims. Common are phishing schemes, as well as the familiar fake phone calls and emails. Some will attempt to directly swindle money from people, but even more sinister, others will attempt to place malware – the gift that keeps on giving – on your computer. And yet others will falsely claim that they have access to miracle cures or vaccines.

As a result, taxpayers and consumers should always remain cautious and use common sense. If you receive an email that sounds too good to be true, it probably is. Also, beware of any call or email that purports to be from a tax authority like the IRS. Remember, under no circumstance will the IRS call or email you to demand money. Nor will they call or email you to make financial offers or ask for personal information in order to release a refund. And never, never click on a link in an email from an unrecognized source.

Avoid Estimated Tax Penalties with the Safe Harbor Rule

Here's a quick quiz. When are federal income taxes owed? If you said April 15 following the tax year, you would be wrong. Even worse, you would possibly be subject to the estimated tax penalty! Legally, taxes are owed and must be paid when income is earned.

If you work as an employee, this process is almost seamless because the taxes you owe on current income earned are withheld from your paycheck. But maybe you have other sources of income like interest, dividends, a capital gain, or an unexpected receipt of income like winning a lottery. In these instances, withholding may not be sufficient to cover the tax. Or maybe you're self-employed, and you are responsible for current tax payments.

In any of these examples, estimated tax payments may be required to accurately pay your tax.

However, you will never be subject to the penalty if you had no tax liability for the prior year, you were a U.S. citizen or resident for the whole year, and your prior tax year covered a twelve-month period.

If this doesn't apply, you still have at your disposal a strategy that can avoid the costly penalty. In fact, you can always avoid the estimated tax penalty, whether you are self-employed or work for a W-2, by applying the Safe Harbor Rule. Here's how it works.

You will pay in the current year an amount of withholding and estimates equal to 100 percent of the prior year's liability. If it turns out that your adjusted gross income for the year is over $150,000, then that number goes up to 110 percent of last year. And, if you pay at least 90 percent of your actual current liability, you are okay. It's that simple. The downside of the Safe Harbor Rule happens when you have income in the current year that is significantly lower than the prior year. Then you are paying estimates that will appreciably overpay your eventual liability. In this instance a careful judgement should be made. I can help you with this decision.

Oh! Don't forget the 2021 estimated tax due dates:

- April 15, 2021;
- June 15, 2021;
- September 15, 2021; and
- January 17, 2022.

Please contact me if you have any questions about estimated taxes.

The Recent Changes Regarding Alimony Payments May Not Be as Simple as You Think

Recent changes in the federal tax law regarding alimony and separation maintenance payments have affected millions of taxpayers. Alimony and separation maintenance payments are amounts paid to a former spouse, or received from a former spouse, under a divorce or separation agreement.

If these separate maintenance payments were executed by legal agreement before December 31, 2018, the payer may deduct the amount from their income, and the receiver will include the payments in their income. However, beginning January 1, 2019, alimony or separate maintenance payments are not deductible by the payer, or includable by the receiver, for agreements executed after December 31, 2018.

And if this weren't confusing enough, the change also applies to those agreements executed before December 31, 2018, if that agreement is changed or modified after that date. In addition, the changes also apply if the taxpayer resides in a state where alimony or separate maintenance payments are not deductible or includible on that state's tax return.

It is also important to note that California did not conform to the new change. That means if you are a resident of California, the changes won't affect your California income tax return at all, regardless of when the agreement was established. You may still deduct alimony paid, or include it you receive it.

Alimony, always a complicated issue for tax purposes, has become even more confusing for many divorced and separated individuals. For more information this subject, contact my office.

Penalty Relief for Partnerships that File Late

Bill is a partner in a general partnership and is responsible for the accounting and tax aspects of the firm. For several reasons beyond Bill's control, he was not able to file the entity's federal tax return on time. What happens now, and how much trouble is Bill in?

Bill is not happy to hear that federal penalties on partnerships who late file their information return, Form 1065, can be the most severe in the entire tax law. Generally, filing late, or not filing at all, can result in penalties of $205 for each month the return is late, per partner, up to a period of twelve months, plus $270 assessed for failure to provide a partner with a Form K1, times the number of partners. So, let's say Bill is three months late with filing the partnership return and providing K1s. There are six partners in Bill's firm. The penalty is $2850 (6*205) + (6*270). Yikes! Even worse, this is before interest charges!

But Bill is not ready to acquiesce. After consulting with an Enrolled Agent, he discovers that there are two possible remedies for relief of these penalties.

First, does the partnership have a filing requirement? This may seem overly simplistic, but it is possible that a business is dormant for an entire tax year. This may become more common than we think with the advent of the coronavirus. A partnership must file an information return, Form 1065, whenever it has any items of income, deductions, or credits. Is it possible that Bill's firm was not active during the tax year in question? If it had no income or deductions, the firm is not required to file, and penalty relief should be granted.

In this case, Bill's firm was active during the year, and thus had a filing requirement. However, Bill has a second option for penalty relief. It turns out that Bill's firm is defined as a small partnership under the tax law. A partnership is considered a small partnership when it has ten or fewer partners. Each partner is either an individual, or the estate of a deceased partner. Each partner's items of income, deductions, and credits are allocated in the same proportion as all other items of income, deductions, and credits. And each partner has reported their share of partnership income on their own timely filed return.

Voilà! If the partnership meets these requirements it is considered to have reasonable cause, and penalty relief should be granted under the reasonable cause provision of the tax code. Bill is off the hook!

If you are curious about this or other areas of partnerships and taxation, contact my office.

What Were the Most Litigated Tax Issues Reported by the Taxpayer Advocate Service?

Did you know that the Internal Revenue Code requires the National Taxpayer Advocate to identify in their Annual Report to Congress, the 10 tax issues most litigated in federal court? In fact, the Advocate studies these issues carefully and makes recommendations in developing legislative recommendations to mitigate these kinds of disputes in the future.

By employing commercial legal research databases, the Advocate identified the 10 most litigated issues starting June 1, 2018 through May 31, 2019. Here they are, in order from most to least:

1. Trade or Business Expenses;
2. Collection Due Process (CDP) Hearings;
3. Accuracy-Related Penalty;
4. Gross Income;
5. Summons Enforcement;
6. Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax;
7. Failure to File Penalty, Failure to Pay Penalty, and Failure to Pay Estimated Tax Penalty;
8. Schedule A Deductions;
9. Charitable Contribution Deductions; and

10. Frivolous Issues Penalty.

Interestingly, the total number of cases identified in the most litigated area decreased this year compared to the prior year by 16 percent. And this reduction is not unusual, but seems to be the trend for the past few years.

The Advocate concluded by stating, "Taxpayers in the cases analyzed this year presented the same arguments raised and repeated year after year, which the courts routinely and universally reject ... the U.S. Courts of Appeals have shown their willingness to uphold the penalties imposed by the Tax Court without fail in the cases analyzed for the period between June 1, 2018, and May 31, 2019, continuing a trend of upholding all penalties in cases we have analyzed since June 1, 2005."

For more information on this subject, see taxpayeradvocate.irs.gov.

Business Clients – watch out for AB5 regulations, CalSavers and Partnership/LLC basis calculations

California AB5 has complicated our lives: In prior years you issued independent contractors a 1099Misc for their services. But now you must determine if they are still independent contractors or California employees. Which do you file in January: W2, 1099Misc or 1099NEC?

CalSavers affects those employers who do not offer a retirement plan to their employees. Any employer in California who has 5 or more employers must register with CalSavers to assist those employees who want to contribute to CalSavers Roth IRA.

Partnerships & LLC are now required to provide their partners/members with a tax basis worksheet along with their K-1.

For more information on this, contact my office.

Business Clients – California Minimum Wages increases January 1, 2021

$13 (25 or fewer employees)

$14 (26 or more employees)