Covenant CPA LLC — Tax Tips

Keeping You Informed • Winter 2019

Your Trusted Advisors

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Our mission is to partner with businesses and families to achieve financial success through Biblical principles in order to further God's kingdom.

Changes to your Form W-4— *When to file*

The IRS has redesigned the Form W-4 due to changes in the tax law that eliminated personal exemptions/allowances. The new Form W-4 should make it easier for you to make any changes to your employer tax withholding. There are several reasons to check your withholding, such as protecting against having too little tax withheld and facing an unexpected tax bill or penalty at tax time. On the other hand, if you often have a large refund, perhaps you would prefer to have less tax withheld up front and receive more money in your paychecks throughout the year.

There is no need to file a new Form W-4 merely because of the redesign. However, if you want to make changes to your withholding effective for 2020, be sure to file a new one with your employer in December.

The IRS recently added a helpful "Tax Withholding Estimator" to their website. This tool is very helpful to determine how to complete Form W-4 so you do not have too much or too little federal income tax withheld by your employer. There is a link to the estimator on our website (www.Covenant-CPA.com, Client Resources Tab—Helpful Links—Federal resources) , or *click here for the withholding calculator.*

Due Dates for 2019 Filing:

Individual Returns:

April 15, 2020

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Partnership and S-Corp Returns:

March 16, 2020

Solar Panels Are Hot—*For a Tax Credit*

The residential energy efficient property credit has been reinstated through 2021. This means you could get a tax credit for installing solar panels on your home. You can even get a credit if you shared the cost of solar panels not directly located on your home, such as at an off-site community solar array or similar arrangement that generates solar energy directly for your home. The credit is equal to 30% of the cost of qualified solar electric property made prior to December 31, 2019, 26% for expenditures made in 2020 and 22% for expenditures made in 2021. There are some limitations on the credit. Additionally, unused credit amounts may be carried to future tax years.

As with any tax law, there are many variables that come into play for this credit. If you are thinking about making energy efficient improvements, let's get together and make improvements not only for our planet but for your taxes as well!

Tax-Saving Strategies— *Make a move now*

It is always a good idea to look for ways to minimize your tax liability. Taking advantage of opportunities before the year comes to a close is a smart move. Here are a few things to think about:

- **Are you making the maximum contribution to your §401(k), IRA or other retirement plans?** If the answer is no, think about increasing your contribution percentage between now and the end of the year. Not only will this increase your retirement savings, but it could also potentially lower your taxable income. If you are age 50 or older, you are eligible to make additional "catch-up" contributions. Contributions to retirement plans must be made by December 31. IRA contributions can be made up to the due date of your tax return, generally April 15.
- **Are you age 70 ½?** Do not forget that you must start taking regular minimum distributions (RMDs) from your traditional IRA by April 1 following the year in which you reach age 70½. Failing to do so triggers a painful 50% IRS penalty on the amount you should have withdrawn. Each year thereafter, you must take your RMD by December 31 to avoid the penalty. Consider asking your IRA custodian to withhold tax from the payment; this could prevent you from having to make estimated tax payments. Another option is to make a Qualified Charitable Distribution (QCD) from your IRA directly to a qualified charity. A QCD can be counted towards your RMD and can lower your taxable income.
- **Did you have any capital gains during the year?** If so, now may be a good time to consider selling some under-performing investments in order to generate a capital loss. Capital losses can offset capital gains. In addition, generally up to an additional $3,000 of capital losses may be deducted against your ordinary income per year with any additional losses carried to future years.
- **Did you know that you can give a tax-free gift to a beneficiary of any age by putting money into a §529 education savings plan account?** Generally, you can make a gift up to $15,000 per beneficiary per year or up to $30,000 for married couples, and you do not even have to file a federal gift tax form! Under new tax laws, §529 plans can also be used to pay up to $10,000 of tuition annually for the beneficiary's enrollment or attendance at a public, private or religious elementary or secondary school. Let's plan ahead for those little ones!
- **Do you have a favorite charity?** Donations are still tax deductible if you itemize, but not if you take the standard deduction. If you give regularly to charities, consider putting several years' worth of gifts into a donor-advised fund for the current year. This strategy may make it worthwhile for you to itemize this year while giving you the ability to spread out the giving over the next several years. Another way to boost a charitable deduction is to donate appreciated stock or property, rather than cash, to charity. If you have owned the asset for more than one year, you get a double tax benefit from the donation! You can deduct the asset's fair market value on the date of the gift and you circumvent paying capital gains tax on any appreciation in value.

The Home Office Deduction— *Qualifying for a tax deduction*

Entrepreneurs who work from home can write off a portion of their housing and utility expenses. A sole proprietor who uses 25% of her house as an office, for example, can deduct 25% of her rent or mortgage interest, property tax, homeowners or renters insurance, and utilities.

To qualify for the home office deduction, entrepreneurs must have a dedicated space in their home that they use exclusively and regularly for business. IRS agents often focus on these two factors when auditing tax returns claiming the home office deduction. So, it is important you know what each of these factors mean.

- Dedicated space used exclusively for business. A home office does not have to be an entire room. It could be a desk and file cabinet sitting in a corner of a room. But this area of the house must be used only for business, and nothing else. Using the room for recreation or having the kids do their homework at the desk means that the space is not exclusively used for business. And that would result in no home office deduction for that space.

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- Regularly and consistently use the space for business. You do not have to work in your home office every single day. But you do need to use the space for business on a regular basis. Working from home only occasionally is not sufficient. A dentist who sees clients in her home office only in emergencies, for example, might not be using the space regularly enough to qualify for the deduction.
- Storage of inventory. If you run a wholesale or retail business, you can also take a home office deduction for the area used to store your inventory and product samples. This storage area does not need to meet the exclusive use test. As long as you use the storage area on a regular basis, we can deduct the storage area in addition to the space you use for conducting business. This is a valuable deduction for eBay sellers and other merchants whose home is the only fixed location for their business.
- Childcare, senior care, and adult daycare. Day care providers can deduct the area of the home used for providing daycare services. The area does not have to be used exclusively for business. Instead, we take a deduction based on the amount of time the area is used for business.

Let us know if you work from home. We want to be armed with facts in case the IRS decides to ask any questions.

Safe Harbor for Rental Properties— *Getting a qualified business income deduction*

Landlords who spend at least 250 hours a year managing and maintaining their rental properties may be eligible for the Qualified Business Income (QBI) deduction. That averages out to just under five hours a week.

Unlike other deductions, the qualified business income deduction does not require that you spend money. Instead, it is a straight deduction, for up to 20% of net rental income for the year. For clients who qualify, this deduction allows rental property owners to pay tax on as little as 80% of their net income from qualifying rental properties. We even have the option of grouping several rental properties together to meet the 250-hour requirement.

Qualifying for this deduction can be tough. Here are the three factors we are looking for:

- 250 hours per year spent managing and maintaining your rental properties.
- You did not live in the rental property for any part of the year.
- The property is not rented under a triple-net lease.

To reach the 250-hour threshold for the QBI deduction, we add up the hours you spend managing the rental property, and also time spent by your property manager, landscapers, repair contractors, and any other people you hire to maintain or manage the rental properties. Rental services that count toward the 250-hour test include:

- Advertising
- Negotiating leases
- Verifying rental applications from prospective tenants
- Collecting rents
- Maintenance and repairs
- Purchasing materials
- Supervising contractors and employees

Keep meticulous records of all the time spent managing your rental properties. Reviewing your time logs is how we—and the IRS—will be able to figure out if you qualify for the QBI deduction for the year.

You will need to keep track not only of the time you spent yourself, but also time spent by any other people you hire to work on your rental properties. Your time log will need to track four data points:

- The dates rental property services were performed.
- Number of hours spent.
- Who performed the work.
- A description of all the work done on that day.

Finally, the IRS requires that you maintain separate books and records for each rental property. We can help you set up your bookkeeping, records and time logs so that you can claim this valuable deduction.

Employer Identification Number— *Does my business need one?*

An Employer Identification Number (EIN) is a nine-digit number that the IRS assigns to identify tax accounts. It is also referred to as a Federal Tax Identification Number.

When deciding if your business needs to obtain an EIN, consider the following questions:

- Will you have employees?
- Will you operate your business as a corporation or partnership?
- Will you file employment, excise, or alcohol, tobacco and firearms tax returns?
- Will you withhold taxes on income, other than wages, paid to a non-resident alien?
- Will you have a retirement plan?
- Will you be involved with: (1) trusts, except certain grantor-owned revocable trusts, IRAs, exempt organization business income tax returns; (2) estates; (3) real estate mortgage investment conduits; (4) non-profit organizations; (5) farmers' cooperatives; or (6) plan administrators?

If you answered "yes" to any of these questions, then you need to obtain an EIN.

Generally, businesses need a new EIN when their ownership or structure has changed. And it is important to note that if you are applying for tax-exempt status, be sure that your organization is formed legally before applying for an EIN.

Applying for an EIN is a free service offered by the IRS. An EIN can be obtained online, by fax, mail or telephone. All EIN applications must disclose the "responsible party". This is the person or entity who controls, manages or directs the applicant entity and the disposition of its funds and assets. Unless the applicant is a government, the responsible party must be an individual, not an entity.

Thinking of starting a new venture? Let's start by tackling the EIN application together.

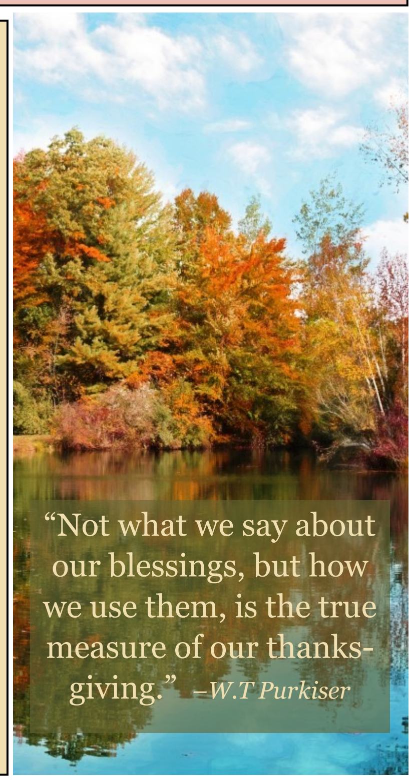
PA Tax Changes—*Highlighting some of our favorites*

FARMERS: Purchases of building material for agricultural animal housing will now be sales ***tax exempt*** in Pennsylvania. Animal housing is defined as "a roofed structure or facility, or portion of the facility, used for occupation by livestock or poultry". Before purchasing materials to repair or build your chicken house or dairy barn, be sure to complete a PA Exemption certificate (REV-1120) to save your 6% sales tax. Also, there is a brand new ***tax credit*** for those who rent land or equipment to *new* farmers.

FIREFIGHTERS: Volunteer fire companies will be ***exempt*** from PA Sales tax on food sales. This measure was enacted to give fire companies freedom to fundraise without the burden of calculating and remitting sales tax to the state.

INHERITANCE: Transfers of property from a deceased parent to a child age 21 or younger will no longer be subject to inheritance tax.

EDUCATION CREDITS: The PA EITC program will expand by $25 million in the next tax year. This program allows business owners to donate to scholarship funds for private schools in their area. With a two year commitment, a business can get a 90% tax credit on these contributions. To receive this credit for the first time, a business must submit an application with the DCED on the first of July. Please contact our office if you would like more information on this credit for 2020. Or visit the website: dced.pa.gov/programs/educational-improvement-tax-credit-program-eitc



"I love the convenience of my portal." — Have you visited your portal yet?

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