# TaxTips

Keeping you informed summer 2018

## Renting your home

### A hidden source of tax-free income

Have you ever thought of your home as a source of untapped income? Consider this: Your home is located in an area that has a lot of tourism or large events that attract many people. Sometimes hotel space is limited or fills quickly. You prefer to be out of town while these events are taking place. If you rent your home for less than 15 days during the year, you just earned some tax-free income.

If you itemize deductions, your mortgage interest and real estate taxes are deducted on your Schedule A. None of the income you collect is taxable, nor is it reported on your tax return. The key to keeping the income tax-free is the number of days you rent your home. You must keep it to less than 15 days during the year. If you rent your home for 15 days or more, tax reporting becomes a bit more complex. Since you also use your home for personal purposes—meaning you live there—you must divide your expenses between the rental use and the personal use based on the number of days used for each purpose. If, after you reduce your rental income by allowed expenses, you have a profit, that profit is taxable. Deductions are limited to rental income.

If you are considering renting your home to others, regardless of the number of days, consult with me first so we can discuss all potential tax consequences.

## Home equity loan interest

New law eliminates deduction

For many of you, finding the money to pay for a new car, boat or dream vacation was as easy as tapping the equity in your home. Prior to 2018, you could use the equity in your home to make large purchases, pay expenses or consolidate debt and deduct the interest on up to $100,000 of debt.

After 2017 and before 2026, this tax savings strategy is gone. While you can still use the equity in your home to borrow needed funds, the interest is no longer deductible unless you use the money to buy, construct or improve your home. The elimination of this deduction applies regardless of when the home equity debt was incurred.

## Did you repay income?

If so, the IRS may allow a deduction

There may come a time when you receive income only to find out later that you have to repay it. This can happen for any number of reasons, and often the repayment is made in a later tax year. For example, when this happens, a deduction or credit for the repayment may be allowed in the year of repayment. The deduction is taken as an itemized deduction on Schedule A. A credit will result in a dollar-for-dollar reduction of your tax liability.

If the repayment was $3,000 or less, you are out of luck. Prior to 2018, this amount was generally deducted as a miscellaneous itemized deduction on Schedule A.

However, recent tax law changes suspended all miscellaneous itemized deductions subject to 2% of your total adjusted gross income until after 2025.

If the repayment was more than $3,000, you have two choices. You can either deduct the total amount you repaid as an itemized deduction, or you may choose a tax credit for the year of repayment equal to the difference in the tax you paid on the income and the amount you would have paid if the income were not included on your tax return in the prior year.

## Donating noncash items to charity

How to reap the full tax benefit

You've done your spring cleaning and now you have boxes of outgrown clothing and unused household items. Should you toss them, have a garage sale or keep them?

If you opt for a garage sale, you have to devote time to making everything presentable, marking prices, setting up tables, advertising and running the actual event. The benefit is instant money for all your hard work, but generally at far less than what it's really worth.

A better option might be to donate that property to a qualified charity such as Goodwill, the Salvation Army or your local church. If you are able to itemize your deductions, you can deduct the fair market value (FMV) of the property you donate. Here are the three most common mistakes that people make when donating property:

- Failure to document what was actually donated to the charity. Say you donated six men's shirts, two pairs of children's shorts, three blouses and five pairs of men's pants. Chances are you just put everything in a bag and told your preparer that you donated a bag full of clothing and you have no documentation. Keep a detailed list of the items you donate and their condition.
- Undervaluing the property that was given to the charity. This is always a subjective area but the law states the deduction is equal to the FMV of the property given. What do you use as the FMV? If you give used clothing to Goodwill, for example, the FMV would be the price that typical buyers actually pay Goodwill for clothing of this age, condition, style and use. Along with a detailed list of the items you donate, establish a value for each item. Local thrift stores often have a list of items with suggested values.

- Failure to obtain documentation that the charitable organization received the property. Charitable organizations will provide you with a receipt acknowledging your contribution.

If you can establish these three areas, you are in complete compliance with the law and are allowed to deduct the value of all property you donate to a charity.

## Children and their money

### What you should know about kiddie tax

Is your child the next Warren Buffet? As a young boy at the age of 11, Warren Buffet invested the money he earned delivering newspapers into some farmland. He continued to invest and reinvest his money; now he is worth an estimated $85 billion. His parents didn't have to worry about kiddie tax, but you might.

Special rules apply to the unearned income of certain children. Generally, your child is subject to kiddie tax if the following apply:

- The child is under age 19 by the close of the tax year, or is a full-time student under age 24 with earned income less than half of his or her support;
- The child's unearned income exceeds a certain inflation-adjusted amount ($2,100 for 2018); and
- The child isn't married filing a joint return.

Unearned income for purposes of the kiddie tax rules is income other than amounts received as compensation for personal services actually rendered (wages, etc.) and distributions from qualified disability trusts.

## Unreimbursed expenses

### Many common employee business expenses are no longer deductible

Are you an employee who incurs unreimbursed expenses? Beginning in 2018 and continuing through 2025, some expenses you could previously claim as itemized deductions won't be allowed. Here's a list of the more common items that are no longer deductible:

- Uniforms and certain work clothes
- Safety shoes and other safety equipment
- Tools needed for your job
- Union dues
- Job-seeking expenses
- Professional dues and licenses
- Home office deductions
- Subscriptions to professional journals
- Continuing education
- Work-related travel, meals and lodging
- Rural mail carrier vehicle expenses
- Passport for a business trip

Now may be a great opportunity to negotiate an accountable plan with your employer.

## Quick Tips

Up to $2,500 of interest you paid on a student loan is deductible if your income is below $65,000 if single ($135,000 for joint filers).

Beginning in 2019, the penalty under the Affordable Care Act for failing to have minimum essential health care coverage is suspended.

In 2018, the estate and gift tax exemption has been increased to roughly $11.2 million ($22.4 million for married couples).

Deductions for personal exemptions for yourself, a spouse and any dependents are no longer allowed.

Charitable contributions of cash to certain charities are limited to 60% of your income.

Once you convert a regular IRA contribution to a Roth IRA, it can no longer be converted back into a regular IRA contribution. In other words, you can no longer undo a Roth conversion.

State and local income tax, property tax and sales tax are limited to an aggregate $10,000 deduction.

In 2018, medical expenses are allowed as an itemized deduction to the extent they exceed 7.5% of adjusted gross income for all taxpayers.

The deduction for job-related moving expenses and the exclusion for moving expense reimbursements have been eliminated, except for certain military personnel.

For post-2018 divorce decrees and separation agreements, alimony will not be deductible by the paying spouse and will not be taxable to the receiving spouse.

## Saving for college

Qualified tuition plans provide options

Many of you are already aware that contributing to a qualified tuition plan, commonly referred to as a 529 plan, can be a tax-free way to save for your child's college education. But did you know that the Tax Cuts and Jobs Act added a provision that also allows you to use a 529 plan to pay for the enrollment costs for your child to attend an elementary or secondary public, private or religious school?

There is one catch, however. While distributions from a 529 plan for college expenses are unlimited provided they are used to pay for qualified educational expenses, distributions for elementary or secondary education expenses are limited to $10,000 per year per designated beneficiary.

## Casualty losses

New rules deny losses to many

Beginning in 2018 and continuing through 2025, casualty losses are no longer allowed as an itemized deduction for many taxpayers. If you suffer a personal loss to property as the result of a storm, fire, flood, theft or some other unforeseen incident, your loss is not deductible unless the loss occurred in a federally declared disaster area announced officially by the President.

Losses incurred in federally declared disaster areas are still allowed as an itemized deduction and are subject to the $100 per casualty and 10% of adjusted gross income limitations. However, if you have personal casualty gains, your casualty losses can still be offset against those gains, even if the losses aren't incurred in a federally declared disaster. Also, any gain resulting from a casualty can be deferred into replacement property.

## Did you receive an e-mail from the IRS?

Hit the delete button

There were various e-mail and phone scams circulating this past year that appeared as though they were from the IRS. The e-mails claim you may owe additional tax or have a refund waiting for you, and all you need to do is provide some information, such as your name, address, Social Security number and filing status. Some of the e-mails even went so far as to ask for your bank account information so they could deposit your refund.

For starters, the IRS never initiates correspondence with taxpayers via e-mail, nor does it ask for your bank account information. The scam is a ruse to collect your personal information and steal your identity. Don't fall for it. Delete the e-mail and keep your personal information safe.

If someone claiming to be from the IRS calls you, hang up. If the IRS needs your attention, they will send you a letter.

## IRS notices

Don't panic

No one likes to receive a letter in the mail from the IRS. The assumption is that if you aren't expecting a refund of some sort, it can't be good news. Don't worry. Often there is no reason to panic. More importantly, don't make matters worse by ignoring the notice and hoping it will go away.

If you receive a notice from the IRS claiming that you may owe additional tax, don't assume that it is correct and automatically pay the amount shown. Many notices just require you to give the IRS additional information to show why you do not owe the additional taxes or penalties. If something was omitted from your return and you are required to pay additional tax, do so right away. In any event, contact me as soon as you receive a notice from the IRS so we can quickly resolve the issue.