The Norton Tax Bulletin

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Dear clients, family, and friends,

As we are in the final stretch of the 2020 return filing season, there are a number of topics I thought I would share with you. As reminder, the filing AND payment deadline for the personal Form 1040 (*as well as the CA form 540 and most other states*) was extended to May 17, 2021. However, the deadline for the first estimated tax payment remains April 15, 2021.

IRS Penalties – Reasonable Cause

When a taxpayer does not file a return timely, or is late on the payment of taxes, the IRS (*as well as state tax agencies*) can assess interest and one or more penalties. Getting relief from a proposed *interest* assessment is difficult and necessitates establishing that the IRS contributed to the accrual of the interest because of a ministerial act. Proving this fact is a challenge, and in my experience within the IRS for 34 years, most taxpayers fail on getting relief from an interest assessment.

Penalties are another matter. The IRS computer systems pretty much automatically throw on penalties for several violations of law such as filing late (*after the due date*) or not paying what is owed by the due date. There are avenues for seeking relief for a number of these penalties. There is a first-time penalty relief (*where you have been a model taxpayer for at least the past three years)* without a prior penalty assessment. Beyond that defense, the IRS can waive penalties it assessed against you or your business if there was *"reasonable cause"* for your actions (or inactions).

The IRS permits reasonable cause penalty relief for penalties arising in three broad categories:

1. Filing of returns (*you miss the deadline*)
2. Payment of tax (*you fail to pay in full what you owe by the due date for the payment)*
3. Accuracy of information (*most often asserted in an audit where there were errors on the return*)

Contrary to what you might think, the term "*reasonable cause*" is a term of art at the IRS. This seemingly simple phrase has a precise and detailed definition as it relates to penalty abatement.

Here are several instances where you might qualify for reasonable cause relief:

1. Your or an immediate family member's death or serious illness, or your unavoidable absence.
2. Inability to obtain necessary records to comply with your tax obligation.
3. Destruction or disruption caused by fire, casualty, natural disaster, or other disturbance.
4. You relied upon a professional's advice and acted to your detriment by following that advice.

The task of pursuing relief from a penalty based on reasonable cause can be tricky and is best left to a tax professional who is more likely to be familiar with and able to present the best-case scenario given the facts and circumstances. Often, Compliance (*the front-line employees*) will disallow a claim for abatement of a penalty based upon reasonable cause. If that occurs, then you would need timely to file a protest to have your case elevated to the Appeals function within the IRS. That is a more formal process where experience in the procedures and negotiation strategies can make a real difference in the outcome.

Here are five instances where you likely *do not qualify* for reasonable cause penalty relief:

1. You made a mistake.
2. You forgot.
3. You relied on another party to comply on your behalf.
4. You do not have the money to pay the tax due.
5. You are ignorant of the tax law.

Bottom line – before you blindly write a check to the IRS for a penalty that they have assessed against you, seek the counsel of a professional who can best advise you of the opportunity to pursue relief either as a first-time penalty assessment or based upon reasonable cause.

ARPA modifications, extension of paid sick leave and family leave credits

The American Rescue Plan Act of 2021 (ARPA), signed by President Biden on March 11, 2021, extended and significantly modified the payroll tax credits for qualifying sick leave and family leave wages. Below is a summary of the key provisions. These credits are available to employers who meet the basic requirements.

Background: Both Covid-19-related credits were initially provided by the Families First Coronavirus Response Act and first applied to eligible wages paid from April 1, 2020, through December 31, 2020. In December of 2020 the Consolidated Appropriations Act of 2021 extended the credits, with some modifications, to apply to wages paid through March 31, 2021.

Extension of both credits. ARPA further extended both the paid sick leave credit and paid family leave credit to apply to wages paid through September 30, 2021.

Modifications to both credits. Beginning with respect to wages paid on April 1, 2021, ARPA made modifications to the credits. The following are the modifications that affect non-government employers:

- The credits are applied against the *Medicare portion* of payroll taxes instead of the OASDI (Social Security) portion. The Medicare portion taxes against which the credit is applied are those of all employees, not just employees to whom qualifying leave wages are paid. Additionally, the credits continue to be refundable (and thus allowed in excess of the Medicare taxes) and advance refundable (they can be applied against any employment taxes, including income tax withholdings, for the quarter in which eligible leave wages are being paid, with any remaining credit refundable at the end of the quarter).
- Reasons for eligible leave are expanded to include obtaining or recovering from Covid-19 immunization. While I have read most people have a minor reaction to the shot, there are a number of individuals who have been laid up with complications from the injection.

- The credits are increased by both the amount of the OASDI taxes paid and Medicare taxes paid with respect to eligible wages, instead of just the Medicare taxes.
- The credits are increased by the amounts of certain collectively bargained pension and apprenticeship program benefits. Under ARPA, the credits continue to be increased by qualified health plan expenses, but under clarified rules.
- Rules are provided that coordinate the credits with second draw Payroll Protection Program loans and certain government grants.
- The no-double benefit rule, which disallows claiming both:
    1. Either of the above credits, and
    2. The income tax credit for family or medical leave, is expanded to include similar coordination with certain other income and payroll tax credits.
- An employer is ineligible for the credits if, in providing paid leave, the employer discriminates in favor of highly compensated or full-time employees or on the basis of employment tenure.
- IRS is allowed an extended limitation-on-assessment period for deficiencies due to claiming either of the credits.

Modification to the paid sick leave credit.

Effective beginning with wages paid on April 1, 2021, in determining whether the 10-day limit on eligible wages is complied with, only days after March 31, 2021, are considered.

Modifications to the paid family leave credit. Effective beginning with wages paid on April 1, 2021:

- The per-employee limit of wages taken into account is raised from $10,000 to $12,000 (*but the limit continues under ARPA to be reduced by wages previously taken into account).*
- Reasons for eligible leave are expanded to include any qualifying reasons for taking paid sick leave.

SEP IRA vs Solo 401(k)

There are five main choices for the self-employed or small-business owners for a retirement plan:
- an IRA (*traditional or Roth*),
- a Solo 401(k),
- a SEP IRA,
- a SIMPLE IRA or
- a defined benefit plan.

They differ in operation, complexity of set up, reporting requirements, tax benefits, and growth potential.

In this segment, I want to discuss two of these retirement plans and provide a comparison – the SEP IRA and the solo 401(k). With both the SEP IRA and the solo 401(k) retirement plans, your investment in your tax-favored retirement creates
- tax deductions for the money you invest in the plan,
- grows tax-deferred inside the plan, and
- incurs taxes only when you take the money from the plan.

It is fairly obvious that a *tax-advantaged* investment plan can generate a larger investment portfolio than a simple CD or other form of investment. But not all plans are the same when it comes to their growth potential and providing an income stream at retirement. In this segment, I will focus on a one-person business with no employees and compare the SEP IRA with the solo 401(k). As a point of review, a one-person business can operate as a C or S corporation, single member-LLC, or proprietorship and have either the SEP IRA or the solo 401(k).

The SEP IRA option is easier to set up, but the 401(k) is not all that difficult. You do have to pay attention to the solo 401(k) requirements, as they can change, but in general, your trustee should help you stay in compliance. But one filing requirement you need to pay attention to is that once your 401(k) account reaches $250,000 in assets, *you must file Form 5500 with the IRS each year*. Generally, your trustee likely will not do this for you. Further, you may not have engaged your tax preparer to help with this. You must file the 5500 by the last day of the seventh month after the plan year ends (***July 31*** *for a calendar year plan*).

Beginning with tax years 2020 and later, the IRS has made the Form 5500 EZ mandatory for use by the solo 401(k) with $250,000 or more in assets, and it is available for either online or paper filing. Generally, the employer has no filing requirements, including the Form 5500 return.

The employer does not include **SEP** contributions on Form W-2, but the employer must check the "[x] Retirement Plan" box in box 13. A SEP IRA may be most appropriate for self-employed individuals who are interested in contributing more to their retirement savings than a traditional or Roth IRA allows but do not want the administrative responsibilities of a 401(k). A taxpayer can have a SEP IRA for their business as well as a retirement plan at another job *where they are not the owner*.

If your goal is to stash away as much cash as possible, then a solo 401(k) may be an option worth considering. With a solo 401(k), annual deductible contributions to the business owner's account can come from two sources.

The first source is from yourself. For 2021, you can contribute to your solo 401(k) account up to $19,500 *($26,000 if age 50 or older*) of ;

- your W-2 income if you are employed by your own C or S corporation, or
- your net self-employment income if you operate as a sole proprietor or as a single-member LLC that is treated as a sole proprietorship (*and files a Schedule C*) for tax purposes.

The second source is from your business itself. *On top of your own elective deferral contribution*, the solo 401(k) arrangement permits an *additional* employer contribution of up to 25 percent of your corporate salary or 20 percent of your net self-employment income. *This is important:* For purposes of calculating the employer contribution, your compensation or net self-employment income is not reduced by your elective deferral contribution. In other words, if your salary is $80,000 and you contribute the full $19,500 as your elective deferral, the employer can contribute up to 25% of the full $80,000 of salary – not the net of $60,500 *($80,000 minus the deferral of $19,500*).

With a corporate plan, your corporation makes the employer contribution on your behalf. With a plan set up for a sole proprietorship or a single-member LLC, you are effectively treated as your own employer. Therefore, you make the employer contribution on your own behalf. In effect, the one-person business is both *an employee and an employer* for the purpose of solo 401(k) contributions.

With the SEP IRA, you look at the employer contribution only—which is up to 25 percent of your W-2 wages if you operate as a corporation or 20 percent of your self-employment income, as adjusted. As an example, John Smith earns $19,000 from freelance work performed as an independent contractor. Under the solo 401(k) rules, John could contribute almost all this $19,000 in net earnings to a solo 401(k). Under the SEP IRA rules, he could contribute only up to $3,800 ($19,000 x 20%).

There is an overall maximum for contributions to a 401(k) retirement plan or a SEP IRA. If you are under age 50 and your income is on the higher side, the 2021 ceiling on contributions is $58,000. But if you are age 50 or older, the solo 401(k) has a catch-up provision that allows you to contribute another $6,500, resulting in a maximum 2021 potential of $64,500. The SEP IRA does not allow a catch-up contribution. However, the 401(k) catch-up contribution must come from an *employee deferral*.

For example, Susie Smith, age 53, operates a very profitable C corporation that pays her a big W-2 wage of $300,000. The C corporation contributes $58,000 to Susie's 401(k). ***That is the employer's maximum***—the lesser of $58,000 or 25 percent of Susie's W-2 wages *($300,000 x .25 =$75,000 in this example*). Because Susie is over age 49, she may make an employee elective deferral of $6,500 that reduces her taxable income for the year and adds to her retirement fund, making $64,500 ($58,000 + $6,500) the total contributions to her solo 401(k) for the year.

The SEP IRA contribution can be made only by the employer—*employee contributions are not allowed!* The solo 401(k) plan allows both employer and employee contributions.

Here is another example. Tom Turner, a self-employed engineer under the age of 50 has an annual net profit of $100,000. With the SEP IRA, Tom can contribute a maximum of $20,000. With the solo 401(k), Tom can contribute a maximum of $39,500 ($19,500 as an employee and $20,000 ($100,000 net profit x 20%) as the employer).

The key to big retirement plan savings is to start early and invest well. Obviously, the more money you can invest, the more your retirement nest egg grows.

As a side note, you can contribute to both a SEP IRA and either a traditional IRA or Roth IRA (*presuming you meet income limitation requirements*) in the same year. However, the deductibility of traditional IRA contributions may be impacted by the SEP IRA contribution. The rules for withdrawal from a SEP IRA are the same as for a traditional IRA. Assets in the account can be withdrawn at any time, however a 10% early withdrawal penalty may apply if you are under the age of 59 ½, unless one of the penalty waivers applies.

To wrap up this topic, I made a comparison between the SEP IRA and the Solo 401(K) strictly for the business owner with no employees other than him or herself (*if incorporated*). The SEP IRA is typically easier and cheaper to set up than a solo 401(k). With the solo 401(k), you must file form 5500EZ annually once your plan assets exceed $250,000. In most cases, the owner of a one-person business can sock away more money for retirement with the solo 401(k) than with the SEP IRA because the solo 401(k) allows both the employee elective deferral *and* the employer contribution.

New Tax Act Highlights

The American Rescue Plan Act of 2021 (ARPA), signed by President Biden on March 11, 2021, is the latest major legislation that provides economic relief and stimulus, both tax and non-tax, during the Covid-19 pandemic. Below are brief summaries of the key aspects of the tax provisions in ARPA. A few of the items

below may be a repeat of what I discussed earlier, but I wanted to keep them in the right category (*individual vs business*).

Provisions Affecting Individuals

Recovery rebate credits (stimulus checks). ARPA provides a third round of nontaxable stimulus checks directly payable to individuals. The payments are structured as refundable tax credits against 2021 taxes but will paid in 2021 (not 2022). The first two stimulus payments – *the first made in early 2020 and the second in or around February 2021* - both applied to the 2020 return.

The maximum payments are $1,400 per eligible individual *($2,800 for married joint filers*) and $1,400 for each dependent (*which, unlike the first two stimulus payments,* includes *older children and adult dependents*). The payment phases out proportionally between $75,000 and $80,000 AGI for single filers, $112,500 and $120,000 for head of household filers, and $150,000 and $160,000 for married joint filers.

Rules for identification, for payments made notwithstanding no filing of 2019 and 2020 returns, and for limitations on offsets apply. Eligibility is based on information from 2020 income tax returns (*or 2019 returns, if 2020 returns have not been filed when the advanced credit is initially issued*). For households whose payment was based on 2019 income data, and who would be eligible to receive a larger payment based on 2020 data, IRS is directed to issue a supplementary payment.

Child tax credit.

For 2021,

1. Qualifying children include 17-year-olds,
2. The credit is increased to $3,000 per child *($3,600 for children under six years of age*), but the increase is subject to modified AGI phase out rules (and the existing modified AGI phase out rules for eligibility for any credit at all continue to apply),
3. The credit is refundable (*meaning, if the credit plus withholding and estimated payments exceed the tax liability, a refund will be issued*), and
4. IRS will make periodic advance payments totaling 50% of its estimate of the credit in the last half of 2021.

Earned income tax credit (EITC).

1. For 2021, the credit is increased for taxpayers with no qualifying children and age restrictions for those taxpayers are relaxed.
2. After 2020 taxpayers that have a qualifying child but can't meet the identification requirements for the qualifying child are nevertheless allowed the credit.
3. Taxpayers may use the greater of their 2019 or 2020 earned income in calculating the credit for 2021.
4. After 2020, the amount of investment income that a taxpayer can have and still earn the credit is increased; and
5. After 2020, there is broadening of the existing exception to the credit's joint filing requirement under which separated married people eligible to file jointly are allowed the credit even if they do not file jointly.

Child and dependent care credit.

For 2021,

1. The credit is refundable;
2. The amount of qualifying expenses taken into account for the credit is increased from $3,000 to $8,000 if there's one qualifying care recipient and from $6,000 to $16,000 if there are two or more;
3. The maximum percentage of qualifying expenses for which credit is allowed is increased to 50% from 35%; and
4. Phase-down rules, based on AGI, are changed.

The increased *dependent care assistance program exclusion amount* (see below) under Code Sec. 129 will also affect the child and dependent care credit, as the amount of expenses taken into account for the credit is reduced by the amount excludable from the taxpayer's income under Code Sec. 129.

Dependent care assistance programs. For 2021, the amount excludible under a dependent care assistance program is increased to $10,500 (*or $7,500 for a married taxpayer filing a separate return*). Retroactive plan amendments can facilitate the increase.

Health care premium assistance credit. For 2021 and 2022, the credit will be available for a larger percentage of insurance premiums, and individuals whose income is greater than 400% of the poverty line will be eligible for (*rather than barred from*) the credit. For 2020, individuals who were provided advances of the credit under the Patient Protection and Affordable Care Act more than the credits to which they are entitled are not obligated to pay back the excess. And, notwithstanding any other rules, individuals who receive unemployment compensation during 2021 are eligible for the credit (*and under rules that increase the amount of the credit).*

Income exclusion for unemployment benefits. For 2020, taxpayers with modified AGI less than $150,000 can exclude from gross income $10,200 of their unemployment benefit. The exclusion is available to each spouse if a joint return is filed. For taxpayers who already filed 2020 returns and did not exclude unemployment benefits, the IRS will make the modifications automatically (*discussed later in this newsletter)*. As a side note, the $150,000 AGI limitation is per single OR married couple. In other words, married filing joint filers *do not get to use $300,000 as the AGI limitation!*

Student loan forgiveness. Beginning in 2021 and continuing through 2025, the forgiveness of many types of loans for post-high school education will not result in income inclusion for the forgiven amounts.

Provisions Affecting Businesses

Payroll tax credits. The paid sick leave and family leave credits are extended to apply to wages paid through September 30, 2021 (*instead of March 31, 2021*).

There are also changes to these credits, including:

- One major change is that during the two-quarter extension period the credits are applied against the employer Medicare portion of payroll taxes instead of the OASDI (Social Security) portion. The Medicare taxes taken into account are those for all employees, not just employees to whom qualifying leave wages are paid. But the credits continue to be refundable (*and, thus, allowed in excess of the Medicare taxes)* and advance refundable (they can be applied against any

employment taxes, including income tax withholdings, for the quarter in which eligible leave wages are being paid, with any remaining credit refundable at the end of the quarter).

- An additional major change is that the allowable credit can be increased by both by both the amount of the OASDI taxes paid and Medicare taxes paid with respect to eligible leave wages, instead of just the Medicare taxes.
- Rules are provided that coordinate the leave credits with second draw Payroll Protection Program loans and certain government grants.
- The no-double benefit rule, which disallows claiming both
    1. Either of the above credits and
    2. The income tax credit for family or medical leave is expanded to include similar coordination with certain other income and payroll tax credits.
- An employer is ineligible for the leave credits if, in providing paid leave, the employer discriminates in favor of highly compensated or full-time employees or based on employment tenure.
- IRS is allowed an extended limitation-on-assessment period for deficiencies due to claiming either of the leave credits.
- ARPA allows employers who voluntarily provide 80 hours of emergency paid sick leave and 12 weeks of emergency family leave beginning after March 31, 2021 to claim the leave credits, thereby resetting the leave bank regardless of whether the employee used leave previously or has exhausted leave.
- The employee retention credit is extended to apply to wages paid before January 1, 2022 (*instead of July 1, 2021*). The result is that as a rule (*but see below)* there is allowed a maximum per employee credit for 2021 of $28,000 ($10,000 of wages considered per quarter multiplied by the credit rate of 70%).
- Also, there are modifications to this credit. A major change is that for the last two calendar quarters of 2021 there is allowed a maximum $50,000 credit per quarter to certain small start-up businesses (and under relaxed eligibility rules). This change makes a limited credit available to some businesses that could not qualify for the credit at all because they can't meet either the full/partial suspension or 20% drop-in-gross-receipts requirements. And, during those two quarters certain distressed businesses will be able to treat all wages as eligible (up to the $10,000 per quarter limit), enabling employers with more than 500 employees, who can ordinarily treat only wages paid to laid-off workers as eligible, to treat any wages as eligible.
- Another of the major changes is that the change to applying the credit to Medicare taxes (discussed above for the paid sick and family leave credits) also applies (along with the continuing refundability and, for employers with no more than 500 employees, advance refundability of the credit).
- Under related rules, the relieved amounts are not included in the income of the individuals and there is imposed by the Internal Revenue Code a penalty on individuals that fail to report the end of their eligibility.

Self-employment sick and family leave credits[1]. These credits, which are creditable against the income tax, have been extended to apply to eligible days through September 30, 2021 (*instead of March 31, 2021*).

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[1] Eligible self-employed individuals, including partners in partnerships with SE income, are entitled to claim qualified sick and family leave equivalent credits under the Families First Coronavirus Response Act. To be an eligible self-employed person, both the following must be true.

1. You must have regularly carried on a trade or business within the meaning of section 1402.
2. You would have been:

- Eligible to receive qualified sick leave wages under the Emergency Paid Sick Leave Act if they had been an employee of an employer (other than the taxpayer) and/or

A major change is that both credits treat as reasons for eligible leave the obtaining of or recovering from Covid-19 immunization. And, for the family leave credit, reasons for eligible leave are expanded to include all qualifying reasons for taking sick leave.

Another major change is that in determining whether the 10-day per tax year limit for the sick leave credit is complied with, only days after December 31, 2021, are considered (*thus restarting the count and often increasing the cumulative number of eligible days*). *And*, a major change to the family leave credit is that the maximum number of eligible days per tax year is increased from 50 to 60, again with only days after March 31, 2021 taken into account (*resetting the count and often increasing the cumulative number of eligible days*).

Excess business losses. In a revenue raiser, the disallowance of excess business losses is extended to run through 2026 instead of 2025.

Deduction disallowance for over $1 million employee remuneration . In another revenue raiser, for tax years beginning after calendar year 2026, the $1 million annual cap on the deductibility of remuneration paid to certain categories of employees of publicly held corporations is expanded to include as a new category the five highest compensated employees not included in other categories.

Tax treatment of certain non-tax relief. ARPA provides favorable tax consequences for targeted Economic Injury Disaster Loan (EIDL) advances made by the SBA under the Economic Aid to Hard-hit Small Businesses, Non-Profits and Venues Act. The advances aren't included in income and the income exclusion does not result in deduction disallowances, denial of basis increases or reduction of other tax attributes. The same treatment applies to SBA Restaurant Revitalization Grants.

Pension plans. ARPA relaxes some funding standards and other IRC or ERISA rules for multiple employer pension plans. For single employer plans, IRC or ERISA rules are relaxed for amortizing funding shortfalls and the pension funding stabilization percentages are changed. Also changed are the special rules that apply to community newspaper plans.

Reporting by third party settlement organizations. ARPA tightens the de minimis exception to tax reporting by third party settlement organizations (TPSOs, e.g., PayPal) by excluding from reporting only transactions that don't exceed $600 (and eliminating the 200-transaction threshold). ARPA also clarified that TPSO reporting obligations are limited to transactions involving goods and services.

Foreign tax. In a revenue raising provision, IRC section 864(f), which provided a one-time election under which, effectively, corporate groups could allocate some interest expense from foreign to domestic corporations and reduce the effect of limits on the foreign tax credit, is repealed. The repeal is retroactive to the election's effective date *(i.e., for tax years beginning after Dec. 31, 2020*).

- Eligible to receive qualified family leave wages under the Emergency Family and Medical Leave Expansion Act if they had been an employee of an employer (other than the taxpayer).

Each eligible self-employed individual must file a separate Form 7202 with their Federal individual income tax return. If a taxpayer is filing a joint tax return and both spouses are eligible self-employed individuals, each must attach a separate Form 7202 to their joint Federal income tax return.

Originally both credits could be claimed until December 31, 2020, but with the passing of the Consolidated Appropriations Act of 2021, the credits have been extended until March 31, 2021. In terms of this blog and reporting the credit on the 2020 tax return, the reference period will be April 1, 2020 through December 31, 2020. The time period of January 1, 2021 through March 31, 2021 would be reported on a 2021 tax return.

Economic Impact Payment #3

This latest round of stimulus payments (EIP3) was authorized by the American Rescue Plan Act (ARPA, PL 117-2). The EIP3 is $1400 per qualified individual and qualified dependent. Individuals with adjusted gross income of $80,000 ($160,000 for married filing jointly) are not eligible for an EIP3. There is a different cutoff for head of household filers.

The April 7 date applies to Social Security, Supplemental Security Income (SSI) and Railroad Retirement Board (RRB) beneficiaries ("federal beneficiaries") who didn't file a 2019 or 2020 tax return, or didn't use the Non-Filers tool, who are receiving their EIP3 electronically. The IRS will update the "Get My Payment" tool the weekend of April 3-4 for federal beneficiaries whose payments will be issued this week.

The IRS estimates that EIP3s for non-filer Veterans Affairs (VA) beneficiaries could be issued by mid-April. Information on payments to VA beneficiaries will be available in the "Get My Payment" tool when those payments are ready to be issued.

For those receiving their EIP3 by mail, the IRS urges federal beneficiaries to watch the mail for their payment, which could include a paper Treasury check or a special prepaid debit card ("EIP Card"). Federal beneficiaries should note that they may receive a different form of payment for their EIP3 than they did for their other payment(s).

Most federal beneficiaries don't need to take any action to receive an EIP3. However, some federal beneficiaries may need to file a 2020 tax return, even if they don't usually file, to provide the IRS with the information it needs to send payments for qualified dependents. Federal beneficiaries with qualified dependents should file a 2020 tax return as soon as possible.

FYI -eligible individuals who didn't get a first or second Economic Impact Payment, or got less than the full amount(s), may be eligible for the 2020 Recovery Rebate Credit. These individuals will need to file a 2020 tax return to claim the credit.

New IRS Extensions

The IRS has now extended to May 17, 2021 deadlines for the following:

IRAs and Roth IRAs. Making contributions to IRAs and Roth IRAs, the time for reporting and paying the 10% additional tax on 2020 distributions from IRAs or workplace-based retirement plans. Note though that the deadline for filing Form 5498 (IRA Contribution Information) series returns related to these accounts is extended to June 30, 2021.

Health and education accounts. Making contributions to health savings accounts (HSAs), Archer Medical Savings Accounts (Archer MSAs) and Coverdell education savings accounts.

2017 Refunds. Making refund claims for the 2017 tax year, which are normally due April 15. Taxpayers must properly address, mail, and ensure the refund claim (e.g., return) is postmarked on or before May 17, 2021.

The IRS has **not** extended the April 15, 2021 estimated tax payment due date. These payments are still due on April 15.

2020 Unemployment Payments Exclusion (*Not Claimed on Previously Filed Return*)

The IRS announced that starting next month and continuing through the summer, it will automatically issue refunds to eligible people who already filed a tax return reporting unemployment payments before the recent changes made by the American Rescue Plan Act. Under this process, most eligible taxpayers will not have to file amended returns to receive a refund.

The American Rescue Plan Act, enacted on March 11, allows taxpayers with modified adjusted gross income of less than $150,000 on their tax return to exclude unemployment payments up to $20,400 if married filing jointly and $10,200 for all others, but only for 2020 unemployment benefits. The $150,000 AGI limitation is calculated considering all income except the unemployment payments.

This law change occurred during the 2020 return filing season. Taxpayers who were anxious to get their returns filed to get their refunds or have the lower 2020 income used for the second stimulus payment used software that likely treated all unemployment payments as taxable. The concern was that amended returns would have to he filed for all those taxpayers so that the refunds could be further increased (*or tax balance reduced)* by excluding the non-taxable portion of the unemployment payments received.

We now have good news!! For those taxpayers who already have filed and figured their tax based on the full amount of unemployment payments, the IRS will determine the correct tax amount of unemployment payments and income tax liability. Any resulting overpayment of tax will be either refunded or applied to other outstanding taxes that may be owed.

The IRS will do these recalculations in two phases, starting with those taxpayers eligible for up to the $10,200 exclusion and then moving on to returns for those married filing jointly taxpayers who are eligible for up to the $20,400 exclusion and others with more complex returns.

There are a few situations in which a taxpayer may have to file an amended return. For example, when reducing a taxpayer's total income (AGI) would entitle him or her to a larger earned income credit (EITC), the IRS will automatically adjust the return to increase the credit. However, if excluding part or all the unemployment compensation would now qualify the taxpayer to claim EITC, they will have to file an amended return if they did not originally claim the EITC or other credits but now are eligible because the unemployment benefit exclusion changed their income. Taxpayers who had their returns prepared professionally or used computer software will need to contact their preparer or update their software to see if they are impacted in a way that requires an amended return (*such as now qualifying for EITC that was not claimed on the original return)*.

I hope that you find the information in this newsletter of value to you. Above all else, please get your shots (*or shot*) as soon as possible and stay safe.

Very truly yours,

Dick Norton

This newsletter is not intended or written by me to constitute written advice that you may rely upon to avoid penalties that may be imposed by any taxing authority. Selection of a tax entity may have considerations beyond simply its tax treatment. Therefore, I advise clients to always first consult with an attorney who is intimately familiar with business forms and their relevance to potential future tax and financial issues.