Due to the coronavirus pandemic (COVID-19) and the enactment of legislation to offset the economic burden wrought by COVID-19, as well as a legislation passed at the end of 2019, there is a lot to consider when reviewing year-end tax planning options that may be available to reduce your 2020 tax liability.

In December of 2019, the SECURE Act was signed into law. This legislation extended several expiring deductions and tax credits and provided some taxpayer-friendly changes to retirement-related rules. In 2020, the first piece of COVID-19 tax-related legislation signed into law was the Families First Coronavirus Response Act (Families First Act), which responded to the coronavirus outbreak by providing, among other things, four types of tax credits for employers and self-employed individuals. The Families First Act was followed by the biggest piece of legislation for the year - the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). The CARES Act, as well as subsequent coronavirus-related legislation, will most likely impact your tax return in some way. The following are some of the considerations we should explore when discussing the tax breaks from which you may benefit, as well as the strategies we can employ to help minimize your taxable income and resulting federal tax liability.

Effect of CARES Act Rebate on Your 2020 Tax Return

Under the CARES Act, individuals with income under a certain level are entitled to a recovery rebate tax credit. These are direct payments (sometimes referred to as "stimulus checks") to individuals by the government. Most, but not all, of these stimulus checks have already been sent out to eligible individuals during 2020.

Single individuals and joint filers are entitled to a payment of $1,200 or $2,400, respectively, plus $500 for each qualifying child. The term "qualifying child" has the same meaning that it does for the child tax credit. Thus, a qualifying child can be no older than 16 on the last day of the tax year (December 31, 2020). The amount of the recovery rebate phases out for income over a certain level. The rebate is reduced by 5 percent of the amount by which the taxpayer's adjusted gross income exceeds (1) $150,000 in the case of a joint return, (2) $112,500 in the case of a head of household, and (3) $75,000 in the case of a single taxpayer or a taxpayer with a filing status of married filing separately.

The government issued the rebates based on 2019 income tax returns, or 2018 returns for individuals who had not yet filed their 2019 tax return. The calculation for the correct amount of the rebate will be part of your 2020 tax return. If your 2020 tax return indicates a rebate larger than your stimulus check (because, for example, your income went down or you had another child), any additional amount can be claimed as a credit against your 2020 tax bill. On the flip side, if the 2020 rebate calculation shows an amount more than what you were entitled to, you do not have to repay that excess.

Filing Status

Your tax return filing status can impact the amount of taxes you pay. For example, if you qualify for head-of-household (HOH) filing status, you are entitled to a higher standard deduction and more favorable tax rates. To qualify as HOH, you must be unmarried or considered unmarried (i.e., legally separated or living apart from a spouse) and provide a home for certain other persons. If you are in such a situation, we need to review whether you qualify for HOH filing status.

If you are married, you will either be filing your return using the married filing jointly or married filing separately filing status. Generally, married filing separately is not beneficial for tax purposes, but in some unique cases, such as when one party earns substantially less or when one party may be subject to IRS penalties for issues relating to their tax reporting, it may be advantageous to file as married filing separately. Additionally, if one spouse was not a full-year U.S. resident, an election is available to file a joint tax return where such joint filing status would otherwise not apply, and this may help reduce a couple's tax liability.

Income from Repayment of Student Loan Debt

The CARES Act excludes from income certain student loan debt repaid by an individual's employer. Thus, if an employer repaid some or all your student loan debt after March 27, 2020, and before 2021, that repayment, which would otherwise be taxable income to you, is not includible in your income.

Standard Deduction versus Itemized Deductions

The Tax Cuts and Jobs Act of 2017 (TCJA) substantially increased the standard deduction amounts, thus making itemized deductions less attractive for many individuals. For 2020, the standard deduction amounts are: $12,400 (single); $18,650 (head of household); $24,800 (married filing jointly); and $12,400 (married filing separately). If the total of your itemized deductions in 2020 will be close to your standard deduction amount, we should evaluate whether alternating between bunching itemized deductions into 2020 and taking the standard deduction in 2021 (or vice versa) could provide a net-tax benefit over the two-year period. For example, you might consider doubling up this year on your charitable contributions rather than spreading the contributions over a two-year period. If these contributions, along with your mortgage interest, medical expenses (discussed below), and state income and property taxes (subject to the $10,000 deduction limitation on such taxes that applies to both single individuals and married couples filing jointly; and the $5,000 limitation on such expenses for married filing separately returns), exceed your standard deduction, then itemizing such expenses this year and taking the standard deduction next year may be appropriate.

Medical Expenses, Health Savings Accounts, and Flexible Savings Accounts

For 2020, your medical expenses are deductible as an itemized deduction to the extent they exceed 7.5 percent of your adjusted gross income. To be deductible, medical care expenses must be primarily to alleviate or prevent a physical or mental disability or illness. They do not include expenses that are merely beneficial to general health, such as vitamins or a vacation. Deductible expenses include the premiums you pay for insurance that covers the expenses of medical care, and the amounts you pay for transportation to get medical care. Medical expenses also include amounts paid for qualified long-term care services and limited amounts paid for any qualified long-term care insurance contract. Depending on what your taxable income is expected to be in 2020 and 2021, and whether itemizing deductions would be advantageous for you in either year, you may want to accelerate any optional medical expenses into 2020 or defer them until 2021. The right approach depends on your income for each year, expected medical expenses, as well as your other itemized deductions.

You may also want to consider health saving accounts (HSAs) if you do not already have one. These are tax-advantaged accounts which help individuals who have high-deductible health plans (HDHPs). If you are eligible to set up such an account, you can deduct the amount you contribute to the account in computing adjusted gross income. These contributions are deductible whether you itemize deductions or not. Distributions from an HSA are tax free to the extent they are used to pay for qualified medical expenses (i.e., medical, dental, and vision expenses). For 2020, the annual contribution limits are $3,550 for an individual with self-only coverage and $7,100 for an individual with family coverage.

In addition, if you are not already doing so and your employer offers a Flexible Spending Account (FSA), consider setting aside some of your earnings tax free in such an account so you can pay medical and dental bills with pre-tax money. The maximum amount that the IRS will allow to be set aside in 2021 is expected to be $2,750. Since you do not pay taxes on this money, you will save an amount equal to the taxes you would have paid on the money you set aside. FSA funds can be used to pay deductibles and copayments, but not for insurance premiums. You can also spend FSA funds on prescription medications, as well as over-the-counter medicines, generally with a doctor's prescription. Reimbursements for insulin are allowed without a prescription. And finally, FSAs may also be used to cover costs of medical equipment like crutches, supplies like bandages, and diagnostic devices like blood sugar test kits.

Several CARES Act provisions affect health care related rules. For example, under the CARES Act, an HDHP temporarily can cover telehealth and other remote care services without a deductible, or with a deductible below the minimum annual deductible otherwise required by law. The CARES Act also modified the rules that apply to various tax-advantaged health-related accounts so that additional health-related items are "qualified medical expenses" that may be reimbursed from those accounts. Under the new rules, which apply to amounts paid after 2019, over-the-counter products and medications are now reimbursable without a prescription.

Charitable Contributions

While the tax benefits of making charitable contributions and taking an itemized deduction for such contributions were tamped down because of the increase in the standard deduction in the TCJA, the CARES Act modified the charitable contribution rules for 2020 tax returns. As a result, an eligible individual can claim an above-the-line deduction of up to $300 for qualified charitable contributions made during 2020. The above-the-line deduction is not available for contributions made after 2020. An eligible individual is an individual who does not elect to itemize deductions. Thus, absent this provision, anyone taking the standard deduction would be ineligible to take a charitable contribution deduction. A qualified charitable contribution is a cash contribution paid in 2020 to an eligible charitable organization. Contributions of noncash property, such as securities, are not qualified contributions.

In addition, if you are itemizing your deductions and have substantial charitable contributions, the CARES Act modified the percentage limitation rules that could otherwise limit your charitable contribution deduction. Under the provision, for charitable contributions made during 2020, any qualified contribution is allowed as a deduction to the extent that the aggregate of such contributions does not exceed the excess of your charitable contribution base over the amount of all other charitable contributions. Excess contributions are eligible for a five-year carryover.

As in prior years, you can reap a larger tax benefit by donating appreciated assets, such as stock, to a charity. Generally, the higher the appreciated value of an asset, the bigger the potential value of the tax benefit. Donating appreciated assets not only entitles you to a charitable contribution deduction but also helps you avoid the capital gains tax that would otherwise be due if you sold your stock. For example, if you own stock with a fair market value of $1,000 that was purchased for $250 and your capital gains tax rate is 15 percent, the capital gains tax you would owe is $113 ($750 gain x 15%). If you donate that stock instead of selling it, and are in the 24 percent tax bracket, your ordinary income deduction is worth $240 ($1,000 FMV x 24% tax rate). You also save the $113 in capital gains tax that you would otherwise pay if you sold the stock; that amount goes to the charity. Thus, the after-tax cost of the gift of appreciated stock is $647 ($1,000 - $240 - $113) compared to the after-tax cost of a donation of $1,000 cash which would be $760 ($1,000 - $240). However, it is important to also keep in mind that tax deductions for contributions of appreciated long-term capital gain property may be limited to a certain percentage of your adjusted gross income depending on the amount of the deduction.

Finally, if you have an individual retirement account and are 70 1/2 years old and older, you are eligible to make a charitable contribution directly from your IRA. This is more advantageous than taking a distribution and donating to the charity that may or may not be deductible as an itemized deduction. If your itemized deductions, including the contribution, are less than your standard deduction, then you receive no tax benefit from making the donation in this manner. By making the donation directly from your IRA to a charity, you eliminate having the IRA distribution included in your income. This in turn reduces your adjusted gross income (AGI). And because various tax-related items, such as the medical expense deduction or the taxability of social security income or the 3.8 percent net investment income tax, are calculated based on your AGI, a reduced AGI can potentially increase your medical expense deduction, reduce the tax on social security income, and reduce any net investment income tax.

Expenses Incurred While Working from Home

Although more people have been working from home this year due to the pandemic, related expenses are **not** deductible if you are an employee. TCJA eliminated the deductibility of such expenses when it suspended the deduction for miscellaneous itemized expenses that was available before 2018. However, if you are self-employed and worked from home during the year, tax deductions are still available. Thus, if you have been working from home as an independent contractor, we should discuss what expenses you have incurred that might reduce your taxable income.

Mortgage Interest Deduction

If you sold your principal residence during the year and acquired a new principal residence, the deduction for any interest on your acquisition indebtedness (i.e., your mortgage) could be limited. The mortgage interest deduction on mortgages of more than $750,000 obtained after December 14, 2017, is limited to the portion of the interest allocable to $750,000 ($375,000 in the case of married taxpayers filing separately). If you have a mortgage on a principal residence acquired before December 15, 2017, the limitation applies to mortgages of $1,000,000 ($500,000 in the case of married taxpayers filing separately) or less. However, if you operate a business from your home, an allocable portion of your mortgage interest is not subject to these limitations.

Interest on Home Equity Indebtedness

You can potentially deduct interest paid on home equity indebtedness, but only if you used the debt to buy, build, or substantially improve your home. Thus, for example, interest on a home equity loan used to build an addition to your existing home is typically deductible, while interest on the same loan used to pay personal expenses, such as credit card debt, is not.

Sale of a Home

If you sold your home this year, up to $250,000 ($500,000 for married filing jointly) of the gain on the sale is excludible from income. However, this amount is reduced if part of your home was rented out or used for business purposes. Generally, a loss on the sale of a home is not deductible. But again, if you rented part of your home or otherwise used it for business, the loss attributable to that portion of the home is deductible.

Discharge of Qualified Principal Residence Indebtedness

If you had any qualified principal residence indebtedness which was discharged in 2020, it is not includible in gross income.

Deductions for Mortgage Insurance Premiums

You may be entitled to treat amounts paid during the year for any qualified mortgage insurance as deductible qualified residence interest if the insurance was obtained in connection with acquisition debt for a qualified residence.

Deductions for Excess Business Losses

The CARES Act removed the loss limitation deduction applicable to non-corporate taxpayers who incurred excess business losses in 2018, 2019, and 2020. An excess business loss for the tax year is the excess of aggregate deductions attributable to your trades or businesses over the sum of your aggregate gross income or gain plus a threshold amount. The threshold amount for 2020 is $259,000 or $518,000 for joint returns. If this provision affects you, we can file amended returns and claim refunds for the years affected.

Qualified Business Income Passthrough Tax Break

Under the qualified business income tax break, a 20 percent deduction is allowed for qualified business income from sole proprietorships, S corporations, partnerships, and LLCs taxed as partnerships. If you qualify for the deduction, which is available to both itemizers and nonitemizers, it is taken on your individual tax return as a reduction to taxable income. This tax break is subject to some complicated restrictions and limitations, but the rules that apply to individuals with taxable income at or below $163,300 ($326,600 for joint filers; $163,300 for married individuals filing separately) are simpler and more permissive than the ones that apply above those thresholds.

Child and Dependent Tax Credit

For 2020, you may claim as much as a $2,000 credit for each child under age 17. The amount of the credit is reduced for taxpayers with modified adjusted income over $200,000 ($400,000 for married filing jointly) and eliminated in full for taxpayers with modified adjusted gross income over $240,000 ($440,000 for married filing jointly). In addition, you may be eligible for a $500 credit for certain dependents. The $500 credit applies to two categories of dependents: (1) qualifying children for whom a child tax credit is not allowed (because, for example, you do not have a social security number for that child), and (2) certain qualifying relatives.

Education-Related Deductions and Credits

Certain education-related tax deductions, credits, and exclusions from income may apply for 2020. Tax-free distributions from a qualified tuition program, also referred to as a Section 529 plan, of up to $10,000 are allowed for qualified higher education expenses. Qualified higher education expenses for this purpose include tuition expenses in connection with a designated beneficiary's enrollment or attendance at an elementary or secondary public, private, or religious school, i.e., kindergarten through grade 12. It also includes expenses for fees, books, supplies, and equipment required for the participation in certain apprenticeship programs and qualified education loan repayments in limited amounts. A special rule allows tax-free distributions to a sibling of a designated beneficiary (i.e., a brother, sister, stepbrother, or stepsister). As a result, a 529 account holder can make a student loan distribution to a sibling of the designated beneficiary without changing the designated beneficiary of the account. In addition, if your modified adjusted gross income level is below certain thresholds, the following are also available for 2020: a deduction of up to $4,000 for qualified tuition and related expenses, an exclusion from income for education savings bond interest received; a deduction for student loan interest; and a lifetime learning credit of up to $2,000 for tuition and fees paid for the enrollment or attendance of yourself, your spouse, or your dependents for courses of instruction at an eligible educational institution.

Credit for Sick Leave for Self-Employed Individuals

Under the Families First Act, if you are considered an eligible self-employed individual, you may be eligible for an income tax credit for a qualified sick leave equivalent amount. You are an eligible self-employed individual if you regularly carry on any trade or business and would be entitled to receive paid leave during the tax year under the Emergency Paid Sick Leave Act added by the Families First Act. The calculation of the qualified sick leave equivalent amount is quite complicated but is generally equal to the number of days during the tax year that you could not perform services for which you would have been entitled to sick leave, multiplied by the lesser of two amounts: (1) $511, or (2) 100 percent of your average daily self-employment income. The number of days considered in determining the qualified sick leave equivalent amount may not generally exceed 10 days. Your average daily self-employment income under this provision is an amount equal to the net earnings from self-employment for the year divided by 260. In addition, if you have appropriate documentation, the credit is refundable.

Credit for Family Leave for Certain Self-Employed Individuals

Another income tax credit that may be available to you under the Families First Act is a credit for a qualified family leave equivalent amount. The qualified family leave equivalent amount is an amount equal to the number of days (up to 50) during the tax year that you could not perform services for which you would be entitled, if you were employed by an employer, to paid leave under the Emergency Family and Medical Leave Expansion Act, which was added by the Families First Act, multiplied by the lesser of two amounts: (1) 67 percent of your average daily self-employment income for the tax year, or (2) $200. Your average daily self-employment income under the provision is an amount equal to your net earnings from self-employment for the year divided by 260. This credit is also refundable.

CARES Act and SECURE Act Changes

Several taxpayer-favorable changes were made in the CARES Act and the SECURE Act with respect to retirement plans and distributions from those plans including the following:

(1) The required minimum distribution rules for 2020 are waived so no one is required to take such a distribution and include it in taxable income in 2020.

(2) The age limit for making contributions to a traditional individual retirement account (IRA), previously 70 ½ years old, was repealed in 2020. Thus, anyone who is otherwise eligible may contribute to a traditional IRA.

(3) A new type of retirement plan distribution was added to the list of early distributions that are excepted from the 10-percent penalty for early withdrawals. You can now receive a distribution from an applicable eligible retirement plan of up to $5,000 without penalty if the distribution is either a qualified birth or adoption distribution.

(4) Taxpayers impacted by the coronavirus (which is essentially anyone) can withdraw up to $100,000 from a retirement plan without penalty and is generally includible in income over a three-year period and, to the extent the distribution is eligible for tax-free rollover treatment and is contributed to an eligible retirement plan within a three-year period, is not includible in income.

(5) The required beginning date for required minimum distributions has been increased to 72 years old from 70 ½ years old. The former rules apply to employees and IRA owners who attained age 70½ prior to January 1, 2020. The new provision is effective for distributions required to be made after December 31, 2019, with respect to individuals who attain age 70½ after December 31, 2019.

Retirement Plan Contributions

If you can afford to do so, investing the maximum amount allowable in a qualified retirement plan will yield a large tax benefit. If your employer has a 401(k) plan and you are under age 50, you can defer up to $19,500 of income into that plan for 2020. Catch-up contributions of $6,500 are allowed if you are 50 or over. If you have a SIMPLE 401(k), the maximum pre-tax contribution for 2020 is $13,500. That amount increases to $16,500 if you are 50 or older. The maximum IRA deductible contribution for 2020 is $6,000 and that amount increases to $7,000 if you are 50 or over.

Life Events

Life events can have a significant impact on your tax liability. For example, if you are eligible to use head of household or surviving spouse filing status for 2019 but will change to a filing tax status of single for 2020, your tax rate will go up. If you married or divorced during the year and changed your name, you need to notify the Social Security Administration (SSA). Similarly, the SSA should be notified if you have a dependent whose name has been changed. A mismatch between the name shown on the tax return and the SSA records can cause problems in the processing of tax returns and may even delay tax refunds. Let me know if you have been impacted by a life event, such as a birth or death in your family, the loss of a job or a change in jobs, or a retirement during the year. All of these can affect you tax situation.

Impact of Future Legislation

Because it is unclear what, if any, tax legislation may be coming next year, we will need to base our year-end planning on existing law.