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Bookkeeping and Tax Service

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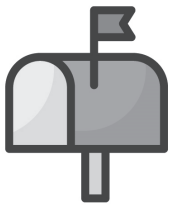
2022 YEAR-END TAX LETTER

INSIDE THIS ISSUE:

IT'S TAX TIME AGAIN…

Your mailbox should be filling up with the information you will need to get the job done.

This letter is full of information designed to help you prepare your tax documents so you pay only the tax that you rightfully owe.



Time to get organized:

This checklist will help you collect the documents needed to file your tax return.

☐ **Your last 3 years' tax returns** *(new clients only)*.

☐ **Social Security numbers and dates of birth** for taxpayers, spouses and dependents.

☐ **Copy of Driver's License** for taxpayer and spouse.

☐ **Noncustodial parents claiming children** need a signed IRS Form 8332 to claim the child.

☐ **W-2 Forms.**

☐ **Your last paycheck stub of the year** (for each job).

☐ **1099 Forms** for interest, dividends, sales, retirement, Social Security, self-employment, unemployment, etc. ★ *Remember to download and print statements from online accounts that don't send paper tax forms.*

☐ **Property tax statements.**

☐ **Forms 1098 for mortgage interest.**

☐ **Foreign accounts.** Bring statements. Such assets must be disclosed even if they do not generate income.

☐ **Purchase and sale information,** including dates, relating to anything sold.

☐ **Stock options**. Forms 1099-B and supplemental statements showing income reported on form W-2.

☐ **Cryptocurrency**. Bring details including dates, proceeds, and original cost.

☐ **Forms W2-G** for gambling winnings. Bring a log of gambling sessions (if available).

☐ **Child care provider information** (name, address, tax ID#, amount paid). Required *even if you have a daycare flex account at work.*

☐ **Names, addresses, and Social Security numbers** from whom you received interest, or to whom you paid interest.

☐ **Bankruptcy or divorce papers** (if applicable).

☐ **Alimony** paid or received. Provide dollar amount, SSN of recipient and date of divorce.

☐ **If you paid an individual $600 or more for services in connection with your business,** please provide their name, address, and tax ID#.

☐ **Records showing income and expense for business and/or rental property you own**. Records of business and personal mileage are required for automobile deductions.

☐ **Form K-1** if you have an interest in a Partnership, S-Corporation, Estate or Trust.

☐ **IRA** (traditional, Roth, SEP, Simple) year-end statements and forms 5498.

☐ **Bring details for <u>all</u> other income,** whether you think it's taxable or not. Examples may include foreign income, barter, hobby, settlements, awards/prizes, etc.

☐ **Forms 1098-T** for post-secondary tuition payments are sent to the student. If the student is your dependent you must get it from them.

☐ **Forms 1099-Q** for education savings plan distributions.

☐ **Student loan interest forms 1098-E.**

☐ **Estimated taxes paid** (include amount and date).

☐ **Adoption costs** if applicable. Also bring the legal adoption documents.

☐ **Charitable donations.** Bring separate totals for cash and noncash contributions. Bring receipts. For noncash donations totaling over $500 include date, place, fair market value, and original cost.

☐ **Form 1098-C** for donations of automobiles or boats.

☐ **If you purchased a new electric plug-in vehicle,** bring the year, make, VIN and purchase date.

☐ If you installed **solar or geothermal systems** for your home or cabin bring receipts.

☐ If you installed **other energy efficient home improvements** (e.g. furnace, AC, windows, doors, insulation, metal roof, etc.) bring receipts.

☐ **If debts were forgiven,** bring Form 1099-C or 1099-A.

☐ **If you bought, sold, or refinanced a home** bring the closing papers.

☐ **Forms 1099-K for internet or credit card sales.**

☐ **Health Savings Account (HSA) contributions and distributions.** Bring forms 5498-SA and 1099-SA.

☐ **Form 1095-A** for health insurance purchased on healthcare.gov (or your state's ACA insurance marketplace).

☐ **Out of pocket medical expenses** may be deductible (if large). Bring details.

☐ **Form 1099-LTC** for long-term care policy benefits paid.

☐ **Employee Retention Credits.** Bring details. You may have to amend a return for the tax year the credits were paid.

☐ **Bring a voided check for direct deposit** of any refunds you expect to receive.

__Caution__: the IRS is very attentive to taxpayers who write off local travel costs.

A daily log of business use is essential. Also, don't forget to record the beginning and the year-end odometer readings.

Need help? There are plenty of smartphone apps that can help with tracking mileage.

DEDUCTING MILEAGE?

Did you drive for charity? If so, you can deduct **14¢** for every mile you drove.

If your medical expenses are substantial, you may want to calculate a mileage deduction. Medical miles for 2022 are **18¢** (1/1/22 - 6/30/22) **or 22¢** (7/1/22 - 12/31/22) **per mile.**

If you drove for business purposes, the situation is a little more complicated: First decide which miles qualify.

Use the following three scenarios to determine how many miles you can deduct:

Keep in mind the following: ***In general, commuting is not deductible.***

Scenario #1: If you have an office or regular place of business outside your home, you may not deduct miles commuting to and from work or to your first or from your last stop, but you may deduct mileage to drive to a *temporary work place* (less than one year's duration) and mileage to and from different work locations during the day.

Scenario #2: If you have an office in your home that qualifies for a home office deduction, all of your business-related mileage is deductible (see below for home office deduction qualifiers).

Scenario #3: If you work out of your home but do not qualify for the home office deduction, the distance between home and your first stop and between your last stop and home are nondeductible commuting miles. You should carefully plan to have your first and last stops close to home to maximize the mileage deduction. A trip to the bank, post office, or a supplier can help increase deductible business miles.

Once you have determined which miles to count, you need to decide whether to use the *standard mileage* rate or actual expenses.

The ***standard mileage rate*** *for qualified business use* for 2022 is **58.5¢** (1/1/22 - 6/30/22) **or 62.5¢** (7/1/22 -12/31/22) **per mile**.

Which method is best? In general, the standard method works best if your business miles are high or your vehicle is economical to run.

The actual expense method works best if your vehicle weighs over 6000 pounds, is costly to run, or you do not have that many miles in total.

DO YOU WORK AT HOME?

If you are self-employed, you may qualify for the home office deduction if you use a portion of your home **exclusively** as your principal place of business, to store inventory, or to conduct substantial management or administrative activities. There can be no other fixed location where the above activities can be done.

The office space still needs to be **used regularly and exclusively for business**. You can not have any other usage of the area whatsoever. Using your office for personal or investment reasons eliminates the deduction as far as the IRS is concerned, so be careful to keep your office space all business.

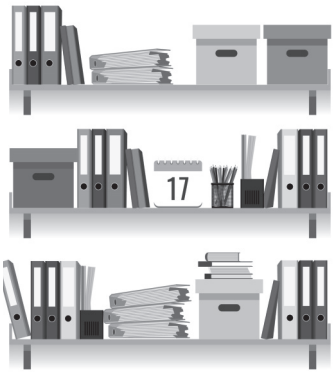
Having a deductible home office means you can deduct all of your local business travel as described earlier.

If your office qualifies, you will need additional information: Measure the business space and the total space. You will also need your mortgage interest, taxes, insurance, association fees, repairs, maintenance, utilities, garbage, security, and rent paid. Also, provide an accounting of the total investment in your home.

The IRS has provided a simplified home office deduction, if you choose. Instead of calculating all of the above information, $5 per square foot can be deducted (maximum $1,500). The IRS estimates that the simplified home office method saves taxpayers 1.6 million hours per year.

To avail yourself of tax deductions, you need to be organized and well documented.

Save proof of all tax deductible purchases.



COMPUTER & CELLPHONE GUIDELINES

Did you buy a computer that you would like to deduct? You can use the following guidelines to determine what is deductible.

If you are self-employed, the business percentage of computer usage, measured by time, is deductible.

If you are a student, the use of a computer is not deductible, but you can tap your 529 plan for a computer purchase.

Keep a log of computer usage to support your deduction.

Cell phone deductions are as follows:

Employers providing cell phones do not have to require records of use to provide tax-free cell phones to employees.

Self employed individuals can deduct business cell phone usage. The IRS, however, still has a hard time believing a cell phone is 100% for business. It's wise to keep a log of use.

EMPLOYEE BUSINESS EXPENSE DEDUCTIONS ARE NOT ALLOWED ON THE FEDERAL RETURN

The Tax Cuts & Jobs Act eliminated federal deductions for employee work expenses. As such, most of the deductions discussed on this page are for business owners only.

WHAT'S NEW FOR '22?

It's been another big year for tax changes.

Expired: **Enhanced Child Tax Credit and Advance Payments**

The 2022 Child Tax Credit (CTC) goes back to the way it was for tax years 2018-2020.

- The maximum CTC is reduced to $2000 per child (ages 0-16). In 2021 the maximum was $3600 per child (ages 0-5) and $3000 (ages 6-17).
- The CTC was not paid in advance like it was in 2021.
- The maximum credit amount for 'other' dependents stays the same ($500).

Expired: **Enhanced Child and Dependent Care Credit**

The 2022 Child and Dependent Care Credit (CDCC) goes back to pre-2021 levels.

- The maximum daycare expenses that count for determining the credit is reduced from $8000 to $3000 per qualifying dependent.
- The amount of the credit is reduced for low/middle income taxpayers. For example, the credit decreases from $8000 to $1200 for a taxpayer with an AGI below $125,000 and 2 kids in daycare at a combined cost of greater than $16,000 (and no pre-tax flex spending).
- Pre-tax dependent care flex spending contributions are limited to $5,000 (down from $10,500).

Expired: **Certain Parts of the Earned Income Tax Credit**

Key provisions of the EITC expired for tax year 2022:

- The 2022 'childless' EITC reverts back to taxpayers age 25-64. In 2021, taxpayers age 19+ without qualifying children could claim the EITC (depending on income).
- The maximum dollar amount of the 'childless' EITC decreases from $1502 (in 2021) to $560 for tax year 2022.
- Taxpayers can no longer use pre-pandemic income levels (from 2019) to determine their current year EITC.

Some of the 2021 EITC enhancements did not expire.

- More taxpayers with investment income (interest, exempt interest, dividends, & gains) are able to claim the EITC. That's because the increased investment income limit (now $10,300, adjusted for inflation) was kept intact (up from $3,650 for tax years prior to 2021).
- Certain married taxpayers that file separately from their spouse can claim the EITC (if they lived apart for greater than half the year and the qualifying child lived with the EITC claimant for greater than half the year).

Expired: **Above-the-line Charitable Contributions**

Taxpayers that don't itemize can no longer deduct up to $300 ($600 if filing jointly) of monetary charitable contributions.

Extended: **Affordable Care Act (ACA) Health Insurance Credits**

The Inflation Reduction Act (signed on 8/16/22) extended enhancements to the ACA for 3 more years (through tax year 2025). Roughly 13 million low/middle income people will buy subsidized health insurance on Healthcare.gov (or their state's ACA marketplace).

Some ACA provisions got extended and others did not. Here's what got extended:

- More generous health insurance subsidies (a.k.a. Premium Tax Credits) for low and middle income taxpayers.
- Qualifying taxpayer's with income greater than 400% of the federal poverty level can claim a Premium Tax Credit. This essentially caps the cost of insurance at 8.5% of household income (with limitations based on the cost of a benchmark plan in their area).

What didn't get extended?

- Not having to pay back excess subsidies (which was the rule for tax year 2020).
- Higher credits for those on unemployment (which was the rule for tax year 2021).

Extended: **Energy Efficient Home Improvement Credits**

The $500 (lifetime limit) credit for qualifying windows, doors, insulation, furnace, AC, etc. was extended for 2022. However, if you wait until 2023 it gets better:

- The $500 lifetime limit becomes a $1200 annual limit.
- The percentage of cost for figuring the credit increases to 30% (up from 10%).
- More improvements will qualify in 2023, including certain biomass stoves, electric panels, and home energy audits.

As always, get assurances that what you are buying in 2023 will qualify for the tax credit.

Extended & Enhanced: **Solar and Alternative Energy**

Tax credits for qualifying residential solar, wind, geothermal, and biomass fuel have been increased to 30% of installed cost (up from 26%) for tax year 2022. Plus:

- The 30% credit is extended through 12/31/32.
- Qualifying battery storage technology now counts for the credit.

Extended & Changed: **Plug-In Electric Vehicle Credits**

The new rules for electric vehicle (EV) tax credits are complicated. Here is the gist:

The old rules apply if you entered into a purchase agreement for a qualifying EV prior to 8/16/22.

For EVs purchased between 8/16/22 and 12/31/22 the credit is limited to vehicles with final assembly in North America.

Entirely new rules begin 1/1/23. The details are beyond the scope of this newsletter. In short:

- Vehicle production caps are eliminated (good news if you want a Tesla or GM model).
- North American assembly is required.
- The sticker price must be less than $55,000 (cars) or $80,000 (trucks/SUVs).
- Buyer's income (modified AGI) must be less than $150,000 (single), $225,000 (HH), or $300,000 (MFJ).
- The battery assembly and raw material components have several new qualifiers.

Final Year! **100% Business Meal Deduction**

Business meals from restaurants remain 100% deductible for tax year 2022. They go back to 50% deductible in 2023.

New Rules for Form 1099-K

All 3rd party payment processors (e.g. Venmo, PayPal, Cash App, Square, Stripe, etc.) are now required to issue form 1099-K for "goods and services" transactions exceeding $600. The previous threshold was $20,000 in transactions.

Vehicle Mileage Rate Changed Midway Through 2022

If you deduct vehicle mileage you must report separate totals for the first half (before 7/1/22) and 2nd half (starting 7/1/22) of 2022 .

2022 was another year of change.

Many of the 2021 enhancements for low/middle income taxpayers with dependent children reverted back to pre-2021 levels (including the Child Tax Credit and Child and Dependent Care Credit).

However, some of the 2021 enhancements are still intact for 2022 (including some provisions of the Earned Income Tax Credit and Premium Tax Credit).

Of course, there are plenty of entirely new rules too.

These are only the highlights of the new laws affecting tax year 2022. Ask for help to determine how these (and other tax rules) apply to your specific situation.

YEAR-END TAX TIPS

Consider the following before 2022 comes to an end:

Lower Your Taxable Income:
Employees still have time to increase pre-tax deductions (e.g. 401(k), 403(b), etc.) from their paycheck (unless already maxed). Self-employed folks can lower their taxable income too by making business purchases before the end of the year or contributing to a SEP IRA before the filing deadline (including extensions).

Why consider this? Not only can it reduce tax, but there are plenty of credits and surtaxes that are sensitive to income levels. Each income threshold is calculated differently and there are other limiting factors, so ask for help if you need to figure out precisely how much extra to contribute. With that in mind, here are some of the most common examples:

Do you have kids in college or pay tuition for yourself? The American Opportunity Credit (first four years of college) and Lifetime Learning Credit (for other degree programs including grad school) begins to phase out at an income of $80,000 (single) and $160,000 (married).

Do you own a business? The QBI deduction begins to phase out for many business owners starting at a taxable income of $170,050 (single) and $340,100 (married).

Do you have a modest income? The Earned Income Credit phases out at varying income levels between $16,480 (single with no qualifying children) and $59,187 (Married with 3+ children).

Do you have a larger income? The phase-out of the Child Tax Credit begins at $200,000 (single) and $400,000 (married). Medicare and investment surtaxes begin at $200,000 (single) or $250,000 (married).

Do you put money in a Roth IRA? Contributions to a Roth IRA begin to phase-out at $129,000 (single) or $204,000 (married filing jointly). Roth conversions, however, are still allowed at any income level.

Do you own rental property? Your ability to deduct most rental losses incurred during the current tax year phases out between $100,000 and $150,000 of income.

Are you paying student loans? Your ability to deduct the interest begins to phase out at $70,000 (single) and $140,000 (married filing jointly).

Do you buy ACA health insurance on healthcare.gov (or state run exchange)? Your premium contribution is limited to 8.5% of household income. As such, lower incomes might result in a higher Premium Tax Credit.

Charity:
Roughly 85%+ of taxpayers will not itemize this year. If that's you, consider the following charity strategies:

- **Volunteer**. The value of your time was never a tax deduction. As such, you're not missing out on anything. Plus, people need your help now more than ever.
- **Plan ahead for a QCD:** Qualified Charitable Distributions (QCDs) from an IRA are allowed for taxpayers over age $70^{1/2}$. The contribution must be made directly from the IRA to the charity. Seniors that use this strategy can take the deduction even if they don't itemize.

Selling investments?
If your taxable income is likely to fall below $41,675 (single) or $83,350 (married filing jointly) consider selling long term investments that have gained in value. You will not pay any federal tax on the gain if you keep your taxable income below those thresholds.

Conversely, it might be wise to check your portfolio for losses. You can offset up to $3,000 of other income with investment losses. If you wish to repurchase the stock again, wait at least 31 days to avoid a wash-sale that disallows the loss.

If you are planning on deducting worthless stock, remember that it's not deductible until it's completely worthless.

Roth conversions:
The deadline to convert funds from a traditional IRA to a Roth IRA is 12/31/22. Remember, the amount converted is taxable income. Also remember that you can no longer undo Roth conversions at a later date.

Health insurance:
If you choose a health plan that is compatible with **Health Savings Accounts (HSA)** you should start funding your HSA right away. That's because medical expenses do not count as a "qualified" for tax free distributions if they occur before the HSA was funded. The maximum amount you can shelter per year is $3,650 (single) or $7,300 (married). You should contribute the maximum if you can afford to. That's because HSAs have three tax benefits;

1. Contributions are a tax deduction.
2. Distributions for qualified medical expenses are tax free.
3. You can invest the funds and reimburse yourself for qualified medical expenses after the account has grown in value.

Employee fringe benefits:
Aside from HSAs, look into other pre-tax spending options that your employer offers such as; insurance, daycare, commuting, parking, education, etc.

Looking Ahead...
The IRS received an increase in funding to help solve some of their most pressing problems, including but not limited to:

- Backlogs of paper-filed returns to process.
- Inability to handle call volumes and long wait times to speak to an agent.
- Low audit rates and lost tax revenue due to lack of enforcement.
- Identity theft and fraudulent tax refunds being paid to criminals.

The proposed increase in enforcement hasn't been without controversy. Naturally, many taxpayers fear that they will be audited. The US Treasury Secretary has instructed the IRS not to increase audit rates (relative to historical levels) for small businesses or households making less than $400,000 per year.

The basic strategy for year-end tax planning can be summed up in the following two statements:

- *Channel your income into the year where it will be taxed at a lower rate.*
- *Channel your deductions to the year where your income will be taxed at a higher rate.*

If you need year-end tax planning a consultation would be wise.