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MARCH 2022

TAX-DEFERRED OR TAX FREE?
(AND WITH ASSET PROTECTION)

Some of the many aspects of tax-deferred savings are discussed in the accompanying *Tax & Business Alert* emphasizing the availability of 2021 deductible contributions made in 2022 for 2021 to a traditional IRA. We generally suggest that early and full funding of all tax-deferred savings opportunities is a priority for achieving financial security.

Taxation

Savers who fully fund available tax-deferred savings plans will compound their disposable income portion (the contribution less tax saving) of the contribution free of income tax rather than only deferring the income tax on the contribution. For example, consider a 40-year-old saver who is in the 30 percent marginal tax bracket and who expects to be at or near that bracket into retirement and thereafter. Such a saver on contributing $1,000 to a tax-deferred (traditional) IRA, 401(k), etc. is placing $300, which would have gone to the tax authorities, and $700 of disposable income, "the saver's share of the contribution," into a tax shelter. The $700 "saver's share" will grow over 25 years, assuming a seven percent return, to $3,800, and the $300 of "tax savings" will grow to $1,628 (total account $5,428). The taxpayer will pay the total tax if the $5,428 is withdrawn on the final day of the 25 years, which, at a 30 percent tax rate, would be $1,628. In other words, the income accumulation of $3,100 ($4,428 x 70%) on the saver's $700 contribution is, in one sense, tax-free because the income of $1,328 ($4,428 x 30%) on the deferred tax plus the original deferred tax of $300 will pay the tax on the distribution of the entire $5,428 account of $1,628 ($5,428 x .30 = $1,628).

The entire contribution to a traditional IRA is tax-deferred. But for increases and decreases in the tax liability related to changes in tax rates, the saver's portion of the contribution and accumulated income is tax-free – not merely tax-deferred. Accordingly, the full and early funding of all available tax accounts, IRAs, 401(k)s, profit-sharing plans, etc. is almost always in the best interest of savers.

Asset Protection

Pension Plans, Profit-Sharing Plans, 401(k) Plans (including rollover IRAs from such plans) are generally exempt, regardless of the account total, from seizure by creditors and other non-governmental judgement holders. Generally, federal law only exempts a total of $1,362,800 for traditional and Roth IRAs and allows seizure for back taxes and penalties. However, Louisiana law exempts all "tax-deferred arrangements" including all IRAs from all liability for any debt except alimony and child support. Accordingly, the savings of those utilizing rollover IRAs, traditional and Roth IRAs are, in Louisiana, exempt from seizure for all but child support, alimony, and back taxes and penalties due.

IRS v. Crypto

The Internal Revenue Service (IRS) continues to view cryptocurrency (crypto) as an enforcement concern. It perceives crypto as property – not as currency. It persists in requiring the recognition of gain or loss on a purchase use, conversion to cash, on a sale or exchange, etc. The 2021 U.S. Individual Income Tax Return, Form 1040, requires (in a prominent position just under the name and address) an answer to the following yes or no question: "*At any time during 2021, did you receive, sell, exchange, or otherwise dispose of any financial interest in any virtual currency?*"

Additionally, the IRS has crypto enforcement efforts underway including court approved summonses requiring crypto exchanges to turn over records of all customers with more than $20,000 of transactions in a year. With the rapidly increasing popularity of cryptocurrencies (consider the volume of Super Bowl ads) increased scrutiny of crypto transactions seems assured.

The Financial Crimes Enforcement Network (FinCEN), a Treasury Department unit separate from the IRS, has announced that it may require U.S. taxpayers holding more than $10,000 of crypto off shore to file a FinCEN form.

Taxpayers considering investing in crypto should be aware of the potential increase in their tax compliance responsibilities and related cost.

Burden of Proof

The current extreme Internal Revenue Service (IRS) backlog of unprocessed paper returns and correspondence has greatly increased the possibility of taxpayers having to furnish proof of timely filing, payment, etc. In her 2021 Annual Report to Congress last month, the IRS's National Taxpayer Advocate, Erin M. Collins, wrote "There is no way to sugarcoat the year 2021 in tax administration. . . . 2021 provided no shortage of taxpayer problems." Ms. Collins further explained that "Paper is the IRS's Kryptonite, and the agency is still buried in it." Consistent with that report, we know of several instances of the IRS cashing the payment check that was mailed with a timely-filed return and thereafter mailing to the taxpayer a notice asserting that the tax return has not been filed. In some cases, the IRS notice has stated that if the return is not filed, the payment might be forfeited.

Generally, an item mailed to the IRS (tax return or payment by check) is deemed timely filed or paid when it is timely mailed with proper postage and a proper address. If the return or payment is misdirected or lost and then later discovered with a legible postmark showing timely mailing, no problems should arise. If the postmark shows a date after the due date of the payment or if the postmark is illegible, the Internal Revenue Service considers the return filed or payment made when it is received.

A Registered or Certified Mail receipt stamped by the Post Office showing a timely date of mailing and a canceled check will suffice to prove timely payment. A timely dated check that clears the payers' bank a few days after the due date of the payment will not prove timely payment. The failure-to-pay penalty (one-half of one percent per month up to 25 percent) is much smaller than the failure-to-file penalty, which is usually five percent of the tax owed for each month or part of a month that a return is late, up to a maximum of 25 percent. It is, then, more significant to be able to prove timely filing than timely payment.

One might prudently use routine mailing for relatively small payments where the penalty for a late payment would be minimal. However, we suggest that all significant payments by check (and paper-filed tax returns and other documents, if applicable) be mailed to the Internal Revenue Service via U.S. Postal Service Certified Mail with the "Return Receipt Requested" and that taxpayers have the Post Office stamp the mailing date on their receipt. Saving that receipt with the return or payment will minimize the problems if the IRS asserts that a tax return or a payment was not timely made.

Unfortunately, timely action in a tax matter is not enough. The taxpayer is all too often required to spend time and money to prove timeliness or suffer unjust and, in some cases, significant penalties.

In Remembrance

of

M. Alton Evans, Jr.

The Firm and our Community lost one of its finest with the passing of Al Evans on January 3, 2022.

The Partners and staff of Cole, Evans & Peterson were blessed by their association with Al; beyond measure and in countless ways. Al was associated with the Firm for 65 years; first as a Partner, 37 years, and then as Partner Emeritus for 28 years. All of us benefited from the values that Al demonstrated in his life, imbued in the culture of the Firm, and inspired and nurtured in those with whom he worked. To work with Al was to confront some great ideas about professionalism, personal responsibility, and life in general.

Al was committed to quality. He wanted the Firm to attract and develop the best of talent and thereby provide clients with the highest quality of service. Accordingly, he sought and was a good judge of intellect and potential. He had the courage to trust competent beginners to grow to handle complex work and responsibility. He wanted us to be among the best of firms, not the biggest.

We are grateful for our time with him.

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MARCH 2022

SLIM YOUR 2021 TAX BILL BY FATTENING YOUR IRA

If you didn't get around to contributing to an IRA in 2021 and you're looking for ways to lower your tax bill, you may still have an option. Qualified taxpayers can make deductible contributions to traditional IRAs until the tax filing date of April 18, 2022, and claim the benefit on their 2021 returns.

WHO IS ELIGIBLE?

You can make a deductible contribution to a traditional IRA if:

- You (and your spouse) aren't active participants in an employer-sponsored retirement plan, or
- You (or your spouse) are active participants in an employer plan, but your modified adjusted gross income (AGI) doesn't exceed certain levels that vary from year to year by filing status.

For 2021, joint tax return filers who are covered by an employer plan have a deductible IRA contribution phaseout range of $105,000 to $125,000 of modified AGI. For taxpayers who are single or a head of household, the phaseout range is $66,000 to $76,000. For married filing separately, the phaseout range is $0 to $10,000. For 2021, if you're not an active participant in an employer-sponsored retirement plan, but your spouse is, the deductible IRA contribution phaseout range is $198,000 to $208,000 of modified AGI.

Deductible IRA contributions reduce your current tax bill, and earnings within the IRA are tax deferred. However, every dollar you take out is taxed in full (and subject to a 10% penalty before age 59½, unless an exception applies).

IRAs are often referred to as "traditional IRAs" as opposed to Roth IRAs. You also have until April 18 to make a Roth IRA contribution, though unlike traditional IRA contributions, Roth IRA contributions aren't deductible. Withdrawals from a Roth IRA are tax-free if the account has been open at least five years and you're age 59½ or older. (Contributions to a Roth IRA are subject to income limits.)

WHAT'S THE CONTRIBUTION LIMIT?

For 2021, if you're eligible, you can make deductible traditional IRA contributions of up to $6,000 ($7,000 if you're 50 or over). In addition, small business owners

TWO ALTERNATE IRA STRATEGIES FOR POSSIBLE TAX SAVING

1. Turn a nondeductible Roth IRA contribution into a deductible IRA contribution. Did you make a Roth IRA contribution in 2021? That's helpful in the future when you take tax-free payouts from the account, but the contribution isn't deductible. If a deduction is important now, you can convert a Roth IRA contribution into a traditional IRA contribution using a "recharacterization" mechanism. Assuming you meet the requirements, you may then take a traditional IRA deduction.

2. Make a deductible IRA contribution, even if you don't work. Generally, you must have wages or other earned income to make a deductible traditional IRA contribution. An exception applies if your spouse is the breadwinner and you're a homemaker. If so, you may be able to take advantage of a spousal IRA.

can set up and contribute to a Simplified Employee Pension (SEP) plan up until the due date for their returns, including extensions. For 2021, the maximum contribution you can make to a SEP is $58,000.

For more information about how IRAs or SEPs can help you save the maximum tax-advantaged amount for retirement, contact us — or ask during your return preparation appointment. ■

HIRING? YOU MAY BE ELIGIBLE FOR A VALUABLE CREDIT

Are you a business owner who needs to hire? Be aware that a law enacted at the end of 2020 extended through 2025 a credit for employers that hire individuals from one or more targeted groups, listed below. Employers can qualify for a tax credit known as the Work Opportunity Tax Credit (WOTC) that's worth as much as $2,400 for each eligible employee. For certain veterans, the credit can be up to $4,800, $5,600 or $9,600, and for "long-term family assistance recipients," up to $9,000 (more about these later). Employees who qualify for the credit must begin working for the employer before January 1, 2026.

Generally, an employer is eligible for the credit only for qualified wages paid to members of a targeted group. These groups are:

1. Qualified members of families that receive assistance under the Temporary Assistance for Needy Families program,
2. Qualified veterans,
3. Qualified ex-felons,
4. Designated community residents,
5. Vocational rehabilitation referrals,
6. Qualified summer youth employees,
7. Qualified members of families in the Supplemental Nutritional Assistance Program (SNAP),
8. Qualified Supplemental Security Income recipients,
9. Long-term family assistance recipients, and
10. Long-term unemployed individuals.

EMPLOYERS MUST MEET CERTAIN REQUIREMENTS

Many conditions must be fulfilled before employers can qualify for the credit. Each employee must have completed a minimum of 120 hours of service for the employer. Also, the credit isn't available for employees who are related to the employer or who previously worked for the employer.

The rules and credit amounts differ for specific employees. The maximum credit available for the first year's wages is $2,400 for each employee, or $4,000 for a recipient of long-term family assistance. In addition, for those receiving long-term family assistance, there's a 50% credit for up to $10,000 of second-year wages.

The maximum credit available over two years for these employees is $9,000 ($4,000 for year one and $5,000 for year two).

For some veterans, the limits are $4,800, $5,600 or $9,600. For summer youth employees, the wages must be paid for services performed during any 90-day period between May 1 and September 15. The maximum WOTC credit available for summer youth workers is $1,200 per employee.

Employers of all sizes are eligible to claim the WOTC. This includes both taxable and certain tax-exempt employers located in the United States and in some U.S. territories. Taxable employers can claim the WOTC against income taxes. However, eligible tax-exempt employers can only claim the WOTC against payroll taxes and only for wages paid to members of the qualified veteran targeted group.

A CREDIT WORTH PURSUING

Additional rules and requirements exist. In some cases, employers may elect not to claim the WOTC. And in limited circumstances, the rules may prohibit the credit or require an allocation of it. However, for most employers that hire from targeted groups, the credit can be valuable. Contact us with questions or for more information about your situation. ■

WHAT TO DO ABOUT FRAUDULENT CREDIT OR DEBIT CARD CHARGES

It's an awful feeling to learn that someone has used your credit or debit card to make fraudulent charges. Whether you're liable for charges typically depends on the type of card, whether you still possess the card and when you alert the issuer.

CREDIT CARDS

If your credit card is lost or stolen and you report it to the card provider before it's used in a fraudulent transaction, you can't be held responsible for any unauthorized charges. If you report it after unauthorized charges have been made, you may be responsible for a specified dollar amount in charges. Some card issuers have decided not to hold their customers liable for any fraudulent charges regardless of when they notify the card company. And if your account number is stolen but not the actual card, your liability is $0. But either you or the card issuer must identify the fraudulent transactions for them to be removed.

When reporting a card loss or fraudulent transaction, contact the issuer via phone. Then follow up with a letter or email. This should include your account number, the date you noticed the card was missing (if applicable), and the date you initially reported the card loss or fraudulent transaction.

DEBIT CARDS

If you report a missing debit card before any unauthorized transactions are made, you aren't responsible for any unauthorized transactions. If you report a card loss within two business days after you learn of the loss, your maximum liability for unauthorized transactions is $50.

But if you report the card loss after two business days but within 60 calendar days of the date your statement showing an unauthorized transaction was mailed, liability can jump to $500. Finally, if you report the card loss more than 60 calendar days after your statement showing unauthorized transactions was mailed, you could be liable for all charges.

What if you notice an unauthorized debit card transaction on your statement, but your card is still in your possession? You have 60 calendar days after the statement showing the unauthorized transaction is mailed to report it and avoid liability.

SAFEST CHOICE

If you're unsure about the specific conditions that trigger liability for unauthorized charges, contact your card issuer. ■

ACT FAST AND YOU MAY AVOID FORFEITING FSA FUNDS

Do you have a tax-saving flexible spending account (FSA) with your employer to help pay for health care expenses? For 2021, FSA participants could contribute up to $2,750 of pre-tax dollars to pay for medical expenses that might not otherwise be deductible (the amount rises to $2,850 for 2022). FSA contributions are also not subject to FICA taxes. Upon request, the plan reimburses participants for qualifying expenses, tax-free.

WHAT IF YOU DON'T SPEND IT ALL?

FSAs generally have a "use-it-or-lose-it" rule, which means you must incur qualifying medical expenditures by the end of the plan year (December 31 for a calendar year plan). Unused amounts when the plan year ends are generally forfeited — that is, unless the plan includes an optional grace period of up to 2½ months to incur qualifying expenses. For a 2021 calendar year FSA plan that has a grace period, that period will end on March 15, 2022. To avoid forfeiting FSA funds after March 15, participants in a calendar year plan will need to act fast to use their available funds for qualifying medical expenses.

GOOD NEWS!

In 2021, the IRS added COVID-19-related expenses to the list of qualifying FSA expenses. That includes COVID-19 home tests and personal protective equipment such as masks, hand sanitizer and sanitizing wipes purchased for the primary purpose of preventing the spread of COVID-19. Participants can ask their employers for a list of qualifying expenses and the documentation required for reimbursement. ■