THE TAX FILE

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In this Issue

1 2020 Changes
Here are some changes to be aware of for tax year 2020, and some information on IRS activities that may affect you.

2 Tax Tidbits
Is there an IRS audit in your future?

2020 Tax Changes

IRS has published tax inflation adjustments for 2020. These adjustments affect more than 60 tax provisions, including tax rate schedules.

The standard deduction for married filing jointly will rise to $24,800 for tax year 2020, up $400 from 2019. For single taxpayers and married taxpayers filing separately the standard deduction will rise $200 to $12,400. For head of household filers, the standard deduction will be $18,650, up $300.

The top tax rate for 2020 remains at 37%. The tax brackets will increase slightly over 2019 amounts. Similar increases will apply to the Alternative Minimum Tax exemption amount and phase-out thresholds.

Several retirement plan contribution limits will increase for 2020. The contribution limit (maximum amount you can defer from your paycheck) for employees who participate in 401(k), 403(b) and most 457 plans will increase from $19,000 to $19,500. The catch-up contribution for employees aged 50 and over who participate in these plans will increase from $6,000 to $6,500.

The limitation for SIMPLE retirement accounts for 2020 increases to $13,500 from the 2019 limit of $13,000.

There are also increases in the income ranges to determine eligibility to make deductible contributions to traditional Individual Retirement Accounts and ROTH IRAs for 2020.

The limit on annual contributions to an IRA account will remain unchanged at $6,000. Catch up contributions to IRA accounts will remain at $1,000.

HSA limits will increase for tax year 2020. The annual limit on deductible contributions will be $3,550 for individuals (up $50 from 2019) and $7,100 for family coverage (up $100).

Annual deductible limits for 2020 HSAs will also increase. The lower limits on annual deductibles on high-deductible health plans will be $1,400 for self-only coverage and $2,800 for family coverage. The upper limits for out-of-pocket costs will be $6,900 for self-only coverage and $13,600 for family coverage.

The Taxpayer First Act of 2019 provides taxpayers with some important safeguards.

The Act allows taxpayers and small businesses to challenge the IRS's position without undertaking the cost and expense of court. It makes the IRS Office of Appeals an independent body, able to review IRS decisions in a fair and impartial manner.

The Act also requires IRS to develop a comprehensive strategy for customer service. IRS is required to submit their plan to Congress within a year, and to make the plan available to the public within two years.

In addition, the Act requires several other changes in the way IRS operates. Changes will impact Innocent Spouse treatment, use of collection agencies for delinquent taxes, and many other areas.

This summer, IRS sent letters to more than 10,000 taxpayers with virtual currency transactions that may not have reported income and paid taxes resulting from virtual currency transactions.

The IRS is expanding efforts involving virtual currency transactions. The names of these taxpayers were obtained through various ongoing IRS compliance efforts. IRS announced a Virtual Currency Compliance campaign in 2018 and remains active in addressing non-compliance in this area.

The IRS website includes lots of information for taxpayers participating in “sharing economy” activities. The sharing economy refers to individuals who utilize technology advancements to arrange transactions to generate revenue. This is accomplished using assets they already possess, like cars and homes, or services they provide (like household chores). Things like Uber and TaskRabbit are examples of these types of activities.

Income from these activities is generally taxable, even if you don’t receive any documentation, like Form 1099-MISC or W-2. On the other hand, costs incurred related to this income may be deductible as business expenses.

Depending on the amount of income you generate from this type of activity, you may be required to make estimated tax payments to avoid penalties. In addition to income taxes, these activities are generally also subject to self-employment taxes.

If you participate in this type of activity, it’s important to keep good records of money coming in, and money going out. For more information on the types of records to keep, and potential tax consequences for these activities, please contact our offices.

The U.S. Treasury and IRS are working on a new Form W-4 for tax year 2020. The new form is intended to make accurate withholding easier for employees to calculate.

The revised form implements changes made following the 2017 Tax Cuts and Jobs Act, which made major revisions affecting taxpayer withholding.

IRS and Treasury received extensive feedback from payroll processors and tax professionals for the design of the new form. The new design reduces the form’s complexity by replacing complicated worksheets with more straightforward questions that make accurate withholding easier for employees.

Employees are not required to submit new Forms W-4 to their employers. However, that may be advisable for employees with large over- or under-payments on their 2019 tax returns.

Tax Tidbits

How likely is it that your tax return will be selected for an IRS audit?

Some filers believe that IRS is less likely to audit returns that are filed late in the filing season. This simply is not true.

All tax returns are processed through an IRS computer system called the Discriminant Information Function (DIF). This system is designed to detect anomalies in tax returns.

DIF looks for things like duplicated items (like deductions or dependents claimed by two or more taxpayers), and other deductions and credits that don’t make sense. Each tax return is compared to other tax returns for taxpayers who earn about the same amount of income. If an amount is outside the norm for that income level, the return is flagged by DIF, and reviewed by an IRS agent.

Far more common than an audit is an IRS notice. IRS gets copies of tax forms like W-2s and 1099s for interest and dividend income. The DIF system compares the income reported on your tax return to the tax forms it has received for your Social Security number. If any income is missing from your tax return, a tax notice proposing additional tax, and possibly interest and penalties, is generated and mailed to you for response.

Because of DIF, when IRS audits (or sends a notice), there’s a good chance that taxes are owed. The audit change rate (number of tax returns adjusted due to an audit) was 89% in 2018.

Today, most audits are done by mail, about 75% of all audits are handled this way. Mail audits typically question small amounts of deduction or credits on a tax return. In most cases, the response to IRS, including required documentation, can also be sent by mail.

Audit rates have fallen over the last decade due to reduced IRS budgets. However, assessment of penalties has increased significantly.

Most audits are for taxpayers earning at least $200,000 per year. Taxpayers earning $50,000 to $75,000 are least likely to be selected for audit.

For More Info

The articles in this newsletter are intended to present general tax information. Accounting rules and tax laws are complex. Not all ideas presented may be appropriate for your specific circumstances.

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