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# February Client Update Newsletter

Tax surprises are never fun, especially when they occur when you're preparing a tax return. In this month's newsletter, read about six surprising items that you may not know are taxed. Also read through several tips for improving your credit score, avoiding penalties when withdrawing from retirement accounts, and giving your brand a personal boost.

Please enjoy the information, and pass along articles of interest to all your family and friends. And as always, please call if you have questions or need help.

## Upcoming dates

- **February 14**
  - Valentine's Day
- **February 19**
  - Presidents' Day
- **Reminders**
  - Organize filing records (1099s, 1098s, W-2s, etc.)
  - Schedule tax appointment for drop off or meeting
  - Begin tax planning for 2024

## In this issue:

# Yes! You Owe Tax on That

## *6 Surprising Taxable Items*

If something of value changes hands, you can bet the IRS considers a way to tax it. Here are six taxable items that might surprise you:


**Surprise #1: Hidden treasure.** In 1964, a married couple discovered $4,467 in a used piano they purchased seven years prior for $15. After reporting this hidden treasure on their 1964 tax return, the couple filed an amended return that removed the $4,467 from their gross income and requested a refund. The couple filed a lawsuit against the IRS when the refund claim was denied. The Tax Court ruled that the hidden treasure should be reported as gross income on the couple's 1964 tax return, the year when the hidden treasure was found.

***Tip:*** *The IRS considers many things like hidden treasure to be taxable, even though they are not explicitly identified in the tax code.*

**Surprise #2: Some scholarships and financial aid.** Scholarships and financial aid are top priorities for parents of college-bound children, but be careful — if part of the award your child receives goes toward anything except tuition, it might be taxable. This could include room, board, books, or aid received in exchange for work (e.g., tutoring or research).

***Tip:*** *When receiving an award, review the details to determine if any part of it is taxable. Don't forget to review state rules as well. While most scholarships and aid are tax-free, no one needs a tax surprise.*

**Surprise 3: Gambling winnings.** Hooray! You hit the trifecta for the Kentucky Derby. But guess what? Technically, all gambling winnings are taxable, including casino games, lottery tickets and sports betting. Thankfully, the IRS allows you to deduct your gambling losses (to the extent of winnings) as an itemized deduction, so keep good records.

***Tip:*** *Know the winning threshold for when a casino or other payer must issue you a Form W-*

*2G. But beware, the gambling facility and state requirements may lower the limit.*

**Surprise 4: Unemployment compensation.** The IRS confused many by making this compensation tax-free during the COVID-19 pandemic. Unemployment compensation income has since gone back to being taxable.

***Tip:** If you are collecting unemployment, either have taxes withheld or make estimated payments to cover the tax liability.*

**Surprise 5: Crowdfunding.** A popular method to raise money is crowdfunding through websites. Whether or not the funds are taxable depends on two things: your intent for the funds and what the giver receives in return. Generally, funds used for a business purpose are taxable and funds raised to cover a life event are a gift and not taxable to the recipient.

***Tip:** Prior to using these tools, review the terms and conditions and ask for a tax review of what you are doing.*

**Surprise 6: Cryptocurrency transactions.** Cryptocurrencies like Bitcoin are considered property by the IRS. So if you use cryptocurrency, you must keep track of the original cost of the coin and its value when you use it. This information is needed so the tax on your gain or loss can be properly calculated.

***Tip:** Using cryptocurrency for everyday financial transactions is not for the faint of heart because of how much recordkeeping is involved.*

When in doubt, it's a good idea to keep accurate records so your tax liability can be correctly calculated and you don't get stuck paying more than what's required. Please call if you have any questions regarding your unique situation.

## Moves to Improve Your Credit Score


While your credit score is a three-digit number that's automatically assigned to you, this is one area of your financial life where you have quite a bit of control. The moves you make or don't make with your credit can help determine where this score falls at any time, and the impact can be dramatic.

Where good credit, a score of 670 or higher, can mean having access to financing with the best rates and terms, a low credit score can mean paying higher interest rates and more loan fees — or even being denied financing altogether. Bad credit can also mean having trouble getting an apartment or a job if your employer asks to see your credit report for hiring purposes.

The following steps can help you improve your credit this year and beyond:

**Set up bills for automatic payments.** Because your payment history is the most important factor used to determine credit scores, make every effort to pay bills on time. Set up your bills for automatic payments so they're paid no matter what, and you can avoid unnecessary credit score damage.

**Pay down existing debt.** How much you owe in relation to your credit limits is the second most important factor used for credit scores. This means avoiding carrying a balance on your credit cards and never using more than 25% of your credit line or your credit score could be impacted.

**Look over your credit reports for errors.** Check your credit reports from all three credit bureaus — Experian, Equifax and TransUnion. You can do this once a year for free at AnnualCreditReport.com. If you find any errors or information you don't recognize, take steps to dispute this information with the credit bureaus.

**Build credit with new financial products.** If you need to build credit from scratch or repair credit after mistakes made in the past, look for new credit products that are easy to obtain. Your best options are secured credit cards that require a cash deposit as collateral and credit-builder loans.

**Use a free app to build credit.** You can use a free app like Experian Boost to get credit for payments you're already making like utility bills, subscription services and even your rent. All you have to do is connect your accounts to this app to have your payments reported to the credit bureaus.

You don’t have to live with a low credit score for another year, especially since so many things can help you improve it. By never missing a payment, paying down debt, checking over your credit reports and getting creative when it comes to building new credit, you can end 2024 in much better shape.

## Avoid a Penalty and Tax Surprise when Withdrawing from Retirement Accounts

Retirement accounts that provide tax breaks have very specific rules that must be followed if you want to enjoy the financial rewards of those tax breaks.

One of these rules defines WHEN you're allowed to


pull money from your retirement accounts. If you pull money too soon, you're at risk of being levied with a penalty by the IRS. There are several exceptions to this rule, such as paying for qualified higher education expenses or paying for expenses if you become permanently disabled. In general, though, if you withdraw retirement funds before you reach age 59½, you'll be hit with a 10% penalty in addition to regular income taxes. In the April 2023 court case Magdy A. Ghaly and Laila Ryad v. Commissioner, the taxpayers learned this rule the hard way.

## The Facts

In 2018, Mr. Ghaly took two distributions from his retirement account.

**Distribution #1: Withdrawal**

Mr. Ghaly was laid off from his job, and in 2018, he withdrew money from his retirement account to provide for his family. He requested and received a withdrawal of $71,147 from his retirement account. His retirement company provided him with a Form 1099-R indicating the withdrawal was taxable.

**Distribution #2: Deemed Distribution**

In 2015, Mr. Ghaly took a loan from his retirement account. Because the loan followed certain IRS-approved guidelines, it was not considered a taxable distribution from his account that year. However, when Mr. Ghaly failed to repay that loan when it came due in 2018, it became a taxable distribution. His retirement company provided him with a 1099-R tax form for the deemed distribution.

Mr. Ghaly had not yet reached age 59½ before either amount was distributed.

## The Findings

In an attempt to restore those distributions to his account to avoid both the tax on the distributions and the early withdrawal penalty, he opened two retirement accounts in 2020 and made the maximum contributions allowed for each account.

The Tax Court ruled against the taxpayers, stating that the contributions Mr. Ghaly made in 2020 were irrelevant when determining if his 2018 distributions were taxable. Mr. Ghaly was required to pay income taxes on the amounts withdrawn (to the extent those distributions were taxable) and was assessed an additional 10% early withdrawal penalty.

### The Lesson

If you are planning an early withdrawal from a retirement account, understand before making the withdrawal whether the 10% penalty applies to you. In Mr. Ghaly's case, he could have explored the substantially equal periodic payment exception or withdrawn money penalty free if used as hardship to pay for his health insurance while unemployed. The lesson: please call if you have questions about an early withdrawal you may be planning before you make it!

## Give Your Personal Brand a Boost

The idea of building a personal brand might seem intimidating, but the benefits can be career altering. Not only does your brand promote you to the entire market, it solidifies your standing within your network where most new career opportunities come from. Here are some steps to consider for building a brand that promotes your strengths and showcases your value.

**Do a personal evaluation.** Start by reflecting on your personal and career experiences. Write down a list of traits and accomplishments that are good portrayals of the value you bring to people and organizations. Ask yourself questions such as, “How would others describe me?” or “In what situations would people look to me for help?” Also take an inventory of your social network presence. You can even try googling yourself to see what comes up. Understanding the current state of your brand, both online and offline, is imperative before taking the next step.

**Be authentic.** As you do your self-evaluation, the shape of your persona will start to emerge. Maybe you’re a go-to person for complex problems, or someone people confide in for advice, or a trusted leader that isn’t afraid of making the big decision. Odds are you’re a combination of a lot of different things, but try to nail down the main ideas so you can narrow your focus. The key here is to be authentic and genuine. There’s no sense building a brand based on something that you’re not — this only causes problems for you and everyone around you.

**Build your online profile.** More than ever, people and businesses are looking to learn about you by researching online. You should try to match your online profile to your in-person qualities. This comes more naturally to some than others, but even some simple steps can enhance your online persona. Start by choosing a profile picture that displays who you are in the best possible light. On LinkedIn, for example, your career industry will dictate the style you choose. This photo will be your first impression, so make sure it conveys the look you are going for.

**Engage and network.** Networking is extremely important to your brand. A LinkedIn study shows that 85% of professionals believe networking is important for finding your next role, while 70% of job changes happen because of a connection at the new company. To increase your online presence, consider posting on a consistent basis. You can start simple by sharing an article you thought was interesting. Then take it a step further by sharing a story that taught you something. The more you do it, the more comfortable you'll be, and the more that your authentic personality will start to show.

**Tell your story.** Don't be afraid to share things about your personality and experiences that helped shape who you are as a person. This will draw people to you and start to build trust. And you don't have to get deeply personal...even the smallest little details about something unique about your day or an experience can make you more interesting.

Building a brand is a lifelong process, so keep at it and don't be afraid to evolve as you go and learn. And who knows, you might even learn something about yourself in the process.

## Reasons to File Your Tax Return Early

*When it makes sense to file a tax return as soon as you can*

The 2024 tax season for 2023 tax returns is now officially underway. Here are several reasons to consider filing your tax return early.


**To get your refund.** There's no reason to let the government hold onto your funds interest-free, so file early and get your refund as soon as possible. While legislation delays receiving refunds for tax returns claiming the Earned Income Tax Credit and the Additional Child Tax Credit until after February 15th, the sooner your tax return is in the queue, the sooner you will receive your refund.

**To minimize your tax identity fraud risk.** Once you file your tax return, the window of opportunity for tax identity thieves closes. Tax identity thieves work early during the tax filing season because your paycheck's tax withholdings are still in the hands of the IRS. If thieves can file a tax return before you do, they may be able to steal these withholdings via a refund that should have gone to you!

**To avoid a dependent dispute.** One of the most common reasons an e-filed return is rejected is when you submit a dependent's Social Security number that has already been used by someone else. If you think there is a chance an ex-spouse may do this, you should file as early as possible.

**To deliver your return to someone who needs it.** If you are planning to buy a house or anticipate any other transaction that will require proof of income, you may wish to file early. This is especially important if you are self-employed. You can then make your filed tax return available to your bank or other financial institution.

**To beat the rush.** As the tax filing deadline approaches, the ability to get help becomes more difficult. So get your documentation together and schedule a time to get your tax return filed as soon as you can. It can be a relief to have this annual task in the rear-view mirror.

While it may make sense to file early, for others it may be better to file later. It's best to be deliberate if you wish to file early, and plan accordingly.

## File Your Business Return on Time or Pay the Price!

March 15th is the tax-filing due date for 2023 calendar year S corporations and partnerships. While this filing deadline does not require making a tax payment, missing the due date could cost you a hefty penalty.

### The penalty

The penalty is calculated based on each month the tax return is late multiplied by each shareholder or partner. So a business tax return with no tax due, filed the day after the March 15th due date, could cost a married couple who jointly own an S corporation $490 in penalties!*

### Take action

Here are some ideas to help you avoid penalties:

**File on time.** If you are a partner in a partnership or a shareholder in an S corporation, file your company's tax return on or before March 15th. In addition to the penalties, filing late shortens the time you have to file your individual tax return and pay any taxes due by this year's April 15th filing deadline.

**Consider an extension.** If you cannot file the tax return by the due date, file an extension on or before March 15th. This gives you an extra six months to file your business return. Remember, you pay the taxes for your flow-through business on your Form 1040 tax return at this year's April 15th filing deadline.

**Your personal tax return may be delayed.** Do not file your Form 1040 tax return until you receive all Form K-1s from each of your S corporation and partnership business activities. But be prepared — if your business files an extension, it's possible you may also need to extend your personal tax return while you wait for the K-1s. Remember that an extension to file doesn't mean an extension to pay your taxes. You'll need to estimate how much your 2023 tax bill will be so you can make a payment, if necessary, by April 15th.

**Challenge the penalty.** If your business does get hit with an IRS penalty for filing late, ask to have the penalty abated. This is especially important if you file and pay your personal taxes on time. Kindly remind the U.S. Treasury it is still receiving the taxes owed to them in a timely manner.

If you haven't filed your S corporation or partnership return for 2023, there's still time to get it done or file an extension. Please call if you need assistance.

**The penalty calculation for 2023 S corporations and partnerships is $245 for each month or part of a month (up to 12 months) the return is late, multiplied by the number of shareholders or partners.*

As always, should you have any questions or concerns regarding your tax situation please feel free to call.


## PAST ISSUES



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| January 2024 | December 2023 | November 2023 | October 2023 |



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