Small Business
July 2021 – Special Issue
TAX STRATEGIES
Grow your profits—pay less tax
Business Management Daily

This is your **LAST ISSUE** unless you act now!
See page 8 for details.

TaxNews

QBI reduction. Under Section 199A, as authorized by the Tax Cuts and Jobs Act, a pass-through entity or sole proprietor can claim a deduction of up to 20% of qualified business income, subject to certain limits. The QBI is your allocable share of the income minus deductions from the business. In a series of frequently asked questions that has flown under the radar, the IRS says a self-employed's health insurance deduction reduces QBI.

New RMD tables. The IRS has released new life expectancy tables to be used for calculating required minimum distributions from IRAs and qualified plans like 401(k)s. The new tables, which were last updated in 2002, reflect longer life expectancies and will allow account holders to spread RMDs over a longer period of time. The tables take effect in 2022.

Review plan beneficiaries. Review the beneficiaries (primary and contingent) for your qualified retirement plans and IRAs. Regularly update any designations to reflect major changes in your life or significant events (e.g., birth, death, marriage or divorce). *Note:* These designations supersede a will.

Share and share alike. If you use an online platform to provide car rides, rent a spare room or furnish other goods or services, you're involved in the so-called "sharing economy." The IRS has posted valuable information about tax issues for these folks, as well as guidance for tax practitioners representing them, on its website (**www.irs.gov**).

INSIDE

Seize 5 new law tax breaks

The new American Rescue Plan (ARP) Act provides more pandemic relief to beleaguered taxpayers.

Alert: Below are five tax moves for individuals under the new law.

1. Collect economic stimulus payments. Previously, Congress authorized payments of up to $1,200 and then $600 per person. On this go-round, the payments are larger, but the dollar amount is phased out at lower income levels.

For a single filer, the $1,400 payment phases out between $75,000 and $80,000 of adjusted gross income (AGI). The phase-out range for joint filers is between $150,000 and $160,000. In comparison, for the last round of payments, the upper thresholds were $100,000 and $200,000, respectively.

The ARP Act also provides a $1,400 payment per dependent, including adult dependents like a child in college or an elderly relative.

Tip: If you don't receive the full amount you're entitled to, you can claim a credit on your tax return.

2. Salvage unemployment benefits. The new law extends unemployment benefits for eligible workers with a tax kicker.

The final version of the law extends weekly benefits of $300 through September 6. Those benefits were set to run out between March 14 and April 11.

More good news: The first $10,200 of unemployment benefits received in 2020 is exempted from federal income tax for folks with a household income under $150,000. Normally, benefits are fully taxable.

Tip: Unemployment benefits may still be subject to state tax.

3. Boost Child Tax Credit. The new law enhances the Child Tax

Continued on page 2

Could tax torpedo hit you?

If you're retiring soon and will be receiving Social Security benefits, or are already retired, you might be hit with an unexpected tax whammy when you file your personal tax return.

Alert: Watch out for the "tax torpedo." This is the name given to the increase in your top marginal tax rate under the complex calculation for Social Security benefits.

Frequently, the tax torpedo affects retirees who must take required minimum distributions (RMDs) from their qualified plans, like 401(k) plans and IRAs.

Here's the whole story: The tax you owe on Social Security benefits depends on the amount of your "provisional income" (PI) for the year. PI is the total of your adjusted gross income (AGI), tax-exempt interest income and one-half of the Social Security benefits received. For example, if your AGI is $80,000 and you collect $12,000 in tax-free municipal bond interest and $16,000 in Social Security benefits, your PI is $100,000 ($80,000 plus $12,000 plus $8,000).

There are two tiers for taxing Social Security benefits.

Tier #1: If your PI is between $32,000 and $44,000 ($25,000 and $34,000 for single filers), you must pay tax on the lesser of one-half of your Social Security benefits or 50% of the amount by which your PI exceeds $32,000 ($25,000 for single filers).

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5 new law tax breaks

(Cont. from page 1)

Credit (CTC) for 2021. Currently, the CTC is available for children under age 17. The maximum credit, subject to a phase-out beginning at $200,000 of adjusted gross income (AGI) for single filers and $400,000 for joint filers, is $2,000. Of this amount, up to $1,400 is refundable.

Under the new law, the CTC for 2021 is increased to $3,600 for each child under age six and $3,000 for each child who is at least age 17. Plus, the entire amount is refundable. But the phase-out begins at $75,000 of AGI for single filers and $150,000 for joint filers.

Tip: The new law provides for advance payments of the CTC starting in July.

4. Raise dependent care credits. Currently, a couple with an AGI above $43,000 who pay qualified childcare expenses can claim a maximum credit of up to $600 for one child; $1,200 for two or more children. Lower-income taxpayers are entitled to a higher credit.

The ARP Act increases the maximum credit for many families to $4,000 for one child; $8,000 for two or more children. This higher credit would be fully available to households with an AGI of up to $125,000. However, the maximum credit would be further reduced for a family with an AGI of more than $400,000.

Tip: These changes are effective only for the 2021 tax year.

5. Reward student loan forgiveness. Generally, forgiveness or cancellation of a loan results in taxable income to the debtor. But prior legislation carved out tax exemptions for student loan forgiveness in certain situations. Now the new law opens the floodgates. No tax may be imposed on forgiveness of both public and private student loans made from 2021 through 2025.

Tip: The exemption doesn't apply if the discharge is made in return for services.

Tax torpedo

(Cont. from page 1)

Tier #2: If your PI is above $44,000 ($34,000 for single filers), you must include in taxable income 85% of the amount by which PI exceeds $44,000 ($34,000 for single filers) plus the lesser of the amount determined under the first tier or $6,000 ($4,500 for single filers). *Caveat:* In no event can more than 85% of your benefits be taxed. The aforementioned thresholds aren't indexed for inflation, so you must cope with these relatively low thresholds year after year. And, if that wasn't bad enough, here's—

Another problem: You're a prime target of the tax torpedo once you start taking RMDs from qualified plans and IRAs. Generally, you must begin taking RMDs after age 70½.

Example: For simplicity, let's say you're a single filer who is normally in the 22% tax and you are required to withdraw a $1,000 RMD for the 2020 tax year. First, the tax on the RMD is $220, but the $1,000 addition to PI can cause up to an extra $850 of your Social Security benefits to be subject to tax.

As a result, the effective incremental federal income tax on your $1,000 RMD is $407 (22% of $1,850). So, the tax torpedo increases your marginal tax rate from 22% to 40.7%—almost double! How can you fend off the tax torpedo?

- **Assess your current exposure.** Determine if the tax torpedo could blow up your tax return.
- **Look ahead.** Before you start taking RMDs, you might convert a traditional IRA to a Roth where future payouts are tax free five years after the conversion. In the same vein, you might arrange other no-tax or low-tax payouts.
- **Consider your Social Security status.** The tax torpedo is a key factor in determining when to begin receiving benefits, but it's not the only one.

Tip: Meet with your tax professional to determine the best approach for your situation (*see box*).

Timing is everything

When should you start taking Social Security benefits? It depends.

Alert: You're entitled to receive 100% of the benefits based on your earnings history at full retirement age (FRA). FRA ranges from age 66 for folks who reach that age this year to age 67 for those born after 1959.

But you can elect to begin taking benefits as early as age 62, although your monthly benefits will be reduced. The monthly reduction can be up to 25% of the FRA amount. The closer you apply to FRA, however, the lesser the reduction.

Conversely, if you choose to delay benefits, you'll receive a higher monthly amount than the FRA amount. Essentially, benefits are increased by 8% for each year you delay taking benefits until age 70. But the cost is that you give up years' worth of benefits. There's a breakeven point if you live long enough, but there's obviously no guarantee that you will. Once you reach age 70, your benefit maxes out and is only increased for inflation.

Real estate

Lock in home sale gain exclusion

The home sale gain exclusion might be the "biggest and best" federal income tax break on the books. If you qualify, you can pocket up either a quarter or a half a million dollars of profit tax free from the sale of your home—no strings attached.

Potential problem: The seemingly generous home sale exclusion might not be enough to shelter your gain if your home has appreciated significantly since you bought it. You may have to pay a king-sized tax bill after selling your castle for a whopping big profit.

Strategy: Keep detailed records of home improvements. These expenditures increase your tax basis for home sale gain calculation purposes (*see box*). So, when you finally do sell your home, the higher basis reduces the taxable amount of the gain. Without detailed records, you're just taking a shot in the dark at your actual basis. Document qualified expenditures each year.

Here's the whole story: If you've owned and used your home as your principal residence for at least two of the previous five years, you can elect to exclude from federal income tax up to $250,000 of home sale profit if you're a single filer; $500,000 for joint filers. There are no limits on the number of times you can claim the exclusion.

The gain for purposes of the exclusion is the difference between the net selling price and your adjusted basis in the home. For example, your basis may have been reduced to reflect rollovers from prior home sales. On the other hand, certain home improvements can increase your basis to cut down your taxable gain or to ensure that your gain is fully sheltered by your allowable exclusion.

Example: You and your spouse bought your first home for $100,000 and sold it for $400,000. Then you bought your current home for $450,000. Under the rules in effect at that time, you avoided any current tax by rolling over the home sale proceeds into your current home.

During the past few years, you've made significant improvements, including an in-ground pool, deck and finished basement. The total cost of the improvements was $125,000. Now you're looking to sell the home for $750,000.

At first glance, you might think you would owe no tax on the home sale. *Reason:* Your $300,000 profit ($750,000 less $450,000) is covered by the $500,000 home sale exclusion for joint filers. But your actual basis after the sale of your first home is $150,000 (purchase price of $450,000 less deferred gain $300,000). Even after you claim the home sale exclusion, you'd have a taxable gain of $100,000 ($750,000 minus $150,000 basis minus $500,000 home sale exclusion).

This is where detailed tax records can come to the rescue. If you can document the $125,000 of home improvements, you can increase your basis to $275,000 ($150,000 plus $125,000). So your taxable gain comes to $475,000 ($750,000 less $275,000)—less than the $500,000 threshold. Thus, your entire gain is tax free!

Besides tracking current expenses, comb over past credit card statements and checkbooks for proof of home improvements. You may be surprised at some of the costs that can help boost your basis.

Tip: Maintain a logbook, ledger or other record of expenses you're adding to your basis. Keep the information stored in a safe place. Make backup copies of electronic files.

Tax checklist of home improvements

Such improvements, which increase your home's value or prolong its useful life, can be added to the home's tax basis:

- Finishing a basement or attic.
- New plumbing, heating or air conditioning system.
- Adding a fireplace or new room.
- Outside improvements such as a patio, deck or swimming pool.
- Installing aluminum or vinyl siding or storm windows and doors.
- New landscaping.

Note that the cost of repairs—such as expenses for painting, fixing gutters, re-plastering walls and replacing broken windows—are not added to your basis. However, if you lump in repairs with home improvements, you can argue that the entire cost is for a general renovation that increases your tax basis.

Tip: Schedule repairs when you're doing improvements. This gives your basis an extra nudge.

Add more to your basis

Add these expenses to your basis to reduce your potential taxable gain:

- Attorney's fees.
- Closing costs and settlement fees.
- Title search and insurance.
- Broker commissions.
- Survey and appraisal fees.
- Recording fees for deed and mortgage.

Tip: These expenses will be reflected in your HUD closing statement.

Business

4 ways to save on cybersecurity costs

What's the biggest threat to your small business in 2021? You can choose from several possibilities, but the specter of cyberattacks should be high on your list.

Strategy: Install cybersecurity measures to protect your business. Generally, these costs can be deducted under applicable federal income tax rules.

Here are four common examples of write-offs that may be available to your small business.

1. Software packages. Your deduction for anti-virus software, malware or ransomware depends on the type of software you purchase.

For starters, you can claim a 100% first-year bonus depreciation for off-the-shelf software. In other words, you can write off the full cost in the year the software is placed in service. Alternatively, you can choose to deduct the cost ratably over three years. In addition, you can deduct monthly costs for cloud-based solutions.

If you go the extra yard and have software specifically developed or customized for your business, it is also eligible for first-year bonus depreciation in 2021.

2. Firewalls. Firewall software is designed to deter hackers from invading your company's computer system. Essentially, you're entitled to the same tax breaks as you are with other software.

3. Ransoms. Suppose you're forced to pay a ransom to cybercriminals so you can unlock your computer system. The jury is still out on whether this expense can be deducted as an "ordinary and necessary" expense or as a theft loss, or if you're entitled to any deduction at all.

Reason: The IRS may argue that the ransom isn't deductible because it's an illegal payment similar to bribes and kickbacks.

4. IT compensation. Do you have an IT department or a handful of employees responsible for cybersecurity measures? The compensation you pay them is deductible like wages paid to other employees. If you use outside services or independent contractors, those costs are also deductible as ordinary and necessary business expenses.

Note: Your small business may incur other related costs. Absent any IRS restrictions, these expenses should generally be deductible.

Tip: The IRS may issue more guidance in the near future.

Lessons from the Tax Court: Keys to vacation home loss

Say this about deducting losses from vacation home rentals: It ain't easy. A new case points out two important tax hurdles to overcome.

When you rent out a vacation home, you can generally deduct certain expenses—such as mortgage interest, property taxes, repairs, utilities and insurance—against the rental income. Furthermore, you can potentially claim a tax loss for the year if deductible expenses exceed rental income.

Tax hurdle #1: To qualify for a deductible loss, your personal use of the vacation home can't exceed the greater of (a) 14 days or (b) 10% of the time the home is rented out.

Tax hurdle #2: Usually, the "passive activity loss" (PAL) rules limit losses from rental activities to the amount of income from other passive activities. But a loss from a short-term vacation home rental activity (meaning one with an average rental period of seven days or less) is treated as nonpassive if the taxpayer "materially participates" in the vacation home rental activity.

Material participation is defined as involvement in the activity on a "regular, continuous and substantial" basis. IRS regulations set forth seven specific tests to meet the material participation standard (e.g., spending more than 500 hours a year on the activity). Passing any one of the tests will suffice.

New decision: A taxpayer owned a vacation home in a California resort area several hours from his home. He rented out the home for 146 nonconsecutive days in 2014 and 152 nonconsecutive days in 2015. So, the average rental period was less than seven days. So far, so good.

The taxpayer paid a property management company to manage the day-to-day operations, including advertising, collecting deposit fees and rent, maintaining and cleaning the property between stays, landscaping, assisting him in hiring repair subcontractors and responding to tenant complaints. He retained control over certain administrative matters like setting rental rates and approving expenses over $100.

Also, the taxpayer performed maintenance on the vacation home about six to nine times each year. His wife helped with the upkeep in 2015. The couple used the vacation home personally only one week a year.

Believing that he had met the material participation standard, the taxpayer deducted the vacation home rental losses for the 2014 and 2015 tax years.

Tax outcome: The taxpayer didn't keep contemporaneous records demonstrating material participation for PAL purposes. According to the Tax Court, the records that he eventually reconstructed were suspect, plus he included driving time between his home and the vacation home. Therefore, the loss was disallowed under the passive loss rules. (*Lucero, TC Memo 2020-136, 9/29/20*)

Business

Consider these tax-deductible commuting expenses

If you're self-employed and have resumed work-related driving, you may be entitled to deduct some vehicle expenses.

Strategy: Squeeze every last deductible dime out of your business travel. Keep detailed records to back up your claims. For example:

- **Short stops.** It may be convenient for you to visit a client on the way into work or on the way home. As a result, you can deduct the cost attributable to the travel between your regular place of business and the client's business location.
- **Separate offices.** If your business has several different offices, you might drive between two or more business locations during the day. As with other business travel, you can deduct the costs between the different business locations.
- **Long-distance commuting.** Suppose you spend a couple of weeks visiting a client's office outside your local geographic area. You never go to your regular workplace. In this case, you can deduct the cost of your daily commute, even though it's long-distance travel.
- **Temporary assignments.** It may be necessary to work at a distant business site for a few months. Instead of commuting daily, you stay near the work site and come home on weekends. Assuming that the job lasts no more than a year, it qualifies as a temporary assignment. Therefore, you can deduct lodging and meal expenses (within certain limits) plus the cost of the weekend trips.
- **Night school.** If you're taking courses at a local college to improve your job skills, you may go straight to school after work. The cost of travel between work and the school is deductible.

Tip: These trips increase the vehicle depreciation deduction you can claim for business-related driving, subject to certain limits.

Tax returns

Avoid common filing blunders

It happens every year: Taxpayers in a hurry to complete their returns make mistakes or omit certain items. Then the IRS catches up to the error of their ways and imposes additional tax, penalties or interest—or all three.

Strategy: Don't commit the types of blunders that have often plagued taxpayers who have rushed in the past. Take the time to do things right the first time.

What sort of mistakes are we talking about? The list of possible foul-ups is a long one, but these four mistakes often show up on returns.

1. You don't report all your income. If your company issues you a W-2, you just report the wages on your return, but things are more complicated for self-employeds or those with sideline businesses. Typically, you're inundated with 1099s from a wide variety of sources, and it's easy to miss or forget one.

Tip: If you e-filed last year, the software program may ask you about missing income.

2. You enter the wrong name or Social Security number. Getting names and numbers wrong is one of the most common mistakes year in and year out. The IRS verifies names and Social Security numbers when it processes returns. If the numbers don't match up, the return is flagged and could be rejected. Likewise, use your legal name and not a nickname or shorthand version.

Tip: It is helpful if you can import this information from last year's return.

3. You enter the wrong numbers for financial accounts. This can cause problems if you're listing investment income from a brokerage or interest from a bank. In the worst-case scenario, you could be penalized if a payment is late because one or two routing numbers are off.

Tip: Double-check your entries before you submit the return.

4. You don't e-file your return. You can avoid some potential errors—such as sending your return to the wrong location—if you file electronically instead of submitting a paper return. This is the fastest, most accurate and most secure method of filing. Plus, the IRS typically processes e-filed returns within 48 hours, so you'll receive any refund sooner.

Tip: E-filers are notified as soon as the return is processed.

Step forward to receive charitable deductions for good deeds

You can't deduct the cost of the time and effort you spend on behalf of charity. But that doesn't mean your good deeds will go for tax naught.

This tax break is available to regular volunteers and others who help out sporadically.

Strategy: Track your out-of-pocket costs. Even though you can't deduct the value of your endeavors, itemizers can write off actual expenses associated with charitable activities.

Furthermore, you don't have to be a board member or one of the charity's biggest donators. This tax break is available to regular volunteers and others who help out sporadically.

What sort of expenses are we talking about? Here's a partial list.

- **Transportation:** If you use your car for charity, deduct the related costs attributable to gas and oil, repairs, insurance, etc. *Alternative:* You might opt for the flat-rate deduction of 14 cents per mile (plus related parking fees and tolls). Similarly, you can deduct plane, train or bus costs for traveling to charitable events.
- **Telephone charges:** You may deduct the full cost of long-distance telephone calls, faxes and cellphone charges made on behalf of a charity. If you install a landline in your home that you use solely for charitable purposes, the entire cost is deductible.
- **Home entertainment:** If you host a fundraiser or board meeting, you can deduct the entire cost of the catering expenses as a charitable deduction. *Note:* The 50% limit on entertainment and meal expenses doesn't apply here.
- **Fundraising dinners:** Normally, you can deduct the portion of the cost that exceeds the fair market value of a fundraising dinner. For example, let's say you and your spouse attend a dinner that costs $100 a head. If the meal is valued at $35 a head, you can deduct $130 ($200 cost – $70 value). *Note:* For amounts exceeding $75, obtain written documentation from the charitable organization.
- **Uniforms:** A deduction is allowed for the cost of uniforms used while performing charitable services as long as the clothing isn't suitable for everyday wear. *Classic example:* You can write off the cost of Boy Scout or Girl Scout uniforms.
- **Foreign exchange students:** If you host a foreign exchange student in your home, you can deduct up to $50 per month for each month the child attends high school. To qualify, the student must live in your home under a written agreement with a qualified charity. Also, the exchange student can't be a relative.
- **Charitable conventions:** You may be able to deduct the cost of attending a convention on behalf of a charity—such as meals and lodging—if you're an official delegate to the convention. But the convention must be the primary purpose of the trip. The deductible amount includes meals and lodging while you attend the convention. *Caveat:* The cost of any side trips to tourist attractions isn't deductible.

Tip: Individually, these deductions may be small, but collectively they add up. Keep the records you'll need at tax return time.

Contribute IRA funds to charity

Certain older taxpayers may be able to benefit from a unique tax break.

Strategy: Transfer funds directly from an IRA to an IRS-approved charity. Although the charitable contribution isn't deductible, the distribution from the IRA isn't taxable. And the payout qualifies as a required minimum distribution (RMD).

This strategy is only available to taxpayers over age 70½. Congress threatened to remove this tax break as part of the Tax Cuts and Jobs Act (TCJA). But, ultimately, the new law didn't touch it.

Tip: If you have both a traditional IRA and a Roth IRA, it generally makes sense to use the traditional IRA first for qualified charitable distributions.

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Investments

Redeem U.S. Savings Bonds for college

Maybe you bought U.S. Savings Bonds when your child was born. Now your offspring will be attending college.

Strategy: Check into a special federal income tax exclusion. If you're the owner of the bonds, you may be able to avoid tax on proceeds used to pay for college. However, this tax break is restricted and phased out for taxpayers based on their modified adjusted gross income (MAGI).

Here's the whole story: Generally, interest on Series EE Bonds is taxable when the bonds are cashed in or mature, whichever comes first. Alternatively, you can elect to pay tax on the accrued interest annually, but you must do this for all your bonds. For this reason, most people allow the bonds to continue to accrue interest.

Significantly, the interest on U.S. Savings Bonds may be exempt from federal income tax if the funds are used to pay for qualified higher education expenses, but this exclusion applies only if the following conditions are met:

- The bond is a Series EE or I Bond issued after 1989.
- You cash in the bond in the tax year for which you're claiming the exclusion.
- You pay qualified higher education expenses in the same tax year for yourself, your spouse or a dependent.
- You don't file your Form 1040 for that year as a married person filing separately.
- The bond owner was age 24 or older before the bond was issued.
- The college-bound child isn't listed as co-owner of the bond.

Thus, bonds issued in the name of a child don't qualify. This might knock you right out of the box.

Key point: This special tax exclusion phases out at relatively moderate income levels. For 2021, phase-out occurs between $83,200 and $98,200 of MAGI for single filers and between $124,800 and $154,800 for married joint filers.

If your child owns the bonds, it may make sense to have him or her redeem them while the child is in a low tax bracket.

Tip: Reduce the child's tax hit by spreading out redemptions over several years.

Business

3 tax tips for gig economy

According to recent data from the Federal Reserve, nearly one out of every three Americans is involved in the gig economy (aka the "sharing economy").

Strategy: Idenfify the tax consequences. Gig economy workers have tax obligations and opportunities similar to those of other self-employed individuals. Notably, you must pay taxes on your earnings, but you could be entitled to some offsetting deductions. Here are 3 tips to avoid problems and maximize available tax benefits.

1. Report large cash transactions. Any business taxpayer, including a participant in the gig economy, who receives more than $10,000 in cash in a single transaction (or in a series of related transactions) is required to file Form 8300, *Report of Cash Payments Over $10,000 Received in a Trade or Business*, within 15 days after receiving payment.

2. Avoid estimated tax penalty. If you're participating in the gig economy, you will have to make quarterly installment payments of "estimated tax" or adjust your withholding from another job, or both. Use Form 1040-ES, *Estimated Tax for Individuals*, to help figure out these payments. Generally, to avoid an estimated tax penalty, you must pay at least 90% of your current year tax liability or 100% of the prior year's liability (110% if your AGI for the prior year exceeded $150,000).

3. Keep good records. Recordkeeping is essential for tracking taxable income and deductible expenses. This also helps you substantiate claimed deductions if the IRS ever challenges them. Your recordkeeping system should include a summary of all business transactions. Generally, it is best to record transactions on a daily basis.

Want to know more? The IRS has created the "Sharing Economy Resource Center" at **www.irs.gov/businesses/small-businesses-self-employed/sharing-economy-tax-center**. It is designed to provide assistance to taxpayers participating in the gig economy.

Tip: You can also view a YouTube video at **www.youtube.com/watch?v=J1S7nxN6mxE**.

Mail Call

MEAL AND ENTERTAINMENT EXPENSES

Q I received an invitation for a free meal at an investment seminar. Is this taxable, if I go? *B.R., Tinton Falls, N.J.*

A No. The event is governed by the general tax rules for meal expenses. Therefore, as the recipient of the meal, you don't owe any income tax on this benefit. But it's not completely "free." Undoubtedly, you'll have to listen to a sales pitch from a financial planner, plus you may have to endure follow-up contacts.

Tip: If you pay to attend an investment seminar or convention, you can't deduct the cost, either.

HOME OFFICE DEDUCTIONS: STAND ON FIRM GROUND

Q In a previous issue, you stated that you could deduct home office expenses based on the number of rooms in the home. Do you have any authority for this statement? *J.R.M., Largo, Fla.*

A Yes. Typically, home office deductions are based on the percentage of business use (square footage of the business portion of the home divided by the total square footage). But the IRS says in Publication 587, *Business Use of Your Home*, a taxpayer *can* base the percentage on the number of rooms if the rooms are about the same size. Say you use one room of an eight-room house for business. The room is 300 square feet out of a total of 3,000 square feet. In this case, the "rooms method" (12.5%) yields a bigger deduction than the square-footage method (10%).

Tip: Access Publication 587 at **www.irs.gov/pub/irs-pdf/p587.pdf**.

TAP UNIQUE TAX BREAK ON COMPANY STOCK

Q When my friend retired several years ago, she didn't roll over her company stock into an IRA. (She had bought some of the stock and her employer gave her some.) If she sells the stock, will it be taxed as capital gain? *F.G., King of Prussia, Pa.*

A Partially. Assuming your friend holds the company stock in a qualified retirement plan, she's eligible for a unique tax break: If a retirement plan distribution is paid in company stock, the retiree is taxed at ordinary income rates on the stock's original cost. Any appreciation is untaxed. When she sells it, the difference between the sales price and the original cost is taxed as capital gain.

DIVIDING THE SPOILS OF A SPOUSAL IRA

Q I retired in 2018, but my wife is still working. I'm now 68, and my wife is 62. We both have IRAs and we file a joint tax return. Can we both still contribute to our IRAs this year? *A.K., Margate, N.J.*

A Yes. Since you qualify for a "spousal IRA" and you're both over age 50, you have until April 15, 2021, to jointly contribute up to $14,000 to your IRAs for 2020 (assuming either of you earned at least that much in compensation during the year). That maximum $14,000 contribution can be divided among your IRAs in any manner in which you see fit as long as no more than $7,000 is allocated to either account. You have until your tax return due date to make the annual contribution.

Tip: To delay mandatory distributions from the IRA, allocate more of the contribution to the younger spouse.

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