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HSA Inflation Adjusted Amounts

Cross References

- IRC §223
- Rev. Proc. 2019-25
- Rev. Proc. 2018-30
- Rev. Proc. 2017-37

The IRS announced inflation adjusted amounts for health savings accounts (HSAs) for 2020. These amounts are reflected in the chart below in comparison to previous years.

HSA Limitations

Annual contribution is limited to:	2020	2019	2018
Self-only coverage, under age 55	$3,550	$3,500	$3,450
Self-only coverage, age 55 or older	$4,550	$4,500	$4,450
Family coverage, under age 55	$7,100	$7,000	$6,900
*Family coverage, age 55 or older	$8,100	$8,000	$7,900
HSA Limitations continued			
Minimum annual deductibles:			
Self-only coverage	$1,400	$1,350	$1,350
Family coverage	$2,800	$2,700	$2,700
Maximum annual deductible and out-of-pocket expense limits:			
Self-only coverage	$6,900	$6,750	$6,650
Family coverage	$13,800	$13,500	$13,300

continued in next column

* Assumes only one spouse has an HSA. See IRS Pub. 969 if both spouses have separate HSAs.

Use 2018 Tax Return to Get 2019 Withholding Correct

Cross References

- IR-2019-80, April 26, 2019

Millions of taxpayers filed a 2018 tax return in the last few weeks, making now a prime time for everyone to consider whether their tax situation came out as they expected. If it didn't, they can use their recently finished 2018 return and the IRS Withholding Calculator to do a Paycheck Checkup and adjust their withholding.

Checking and then adjusting their tax withholding can help make sure they don't owe more tax than they are expecting. Usually they can also avoid a surprise tax bill and possibly a penalty when they file next year. At the same time, with the average refund more than $2,700, some taxpayers may choose to reduce their withholding to have a larger paycheck and smaller refund.

Now is an ideal time to check withholding, since having a completed tax return is helpful when using the Withholding Calculator on www.irs.gov. Since taxpayers

need to estimate deductions, credits and other amounts for 2019, having similar information from the 2018 return can make using the Withholding Calculator easier. Use the following web address to access the IRS Withholding Calculator: https://www.irs.gov/individuals/irs-withholding-calculator

Who Should Do a Paycheck Checkup?

Though doing a Paycheck Checkup is a good idea every year, for many people, it's even more important this year. This includes anyone who:

- Adjusted their withholding in 2018—especially those who did so in the middle or later part of the year.
- Owed additional tax when they filed their 2018 tax return.
- Had a refund that was larger or smaller than expected.
- Had life changes such as marriage, childbirth, adoption, buying a home or when income changes.

In addition, most people are affected by changes made in the Tax Cuts and Jobs Act (TCJA), the tax reform legislation enacted in December 2017. These changes included lowered tax rates, increased standard deductions, suspension of personal exemptions, the increased Child Tax Credit and limited or discontinued deductions. As a result, the IRS continues to encourage people to check their withholding, even if they did a Paycheck Checkup in 2018.

This includes taxpayers who:

- Have children and claim credits, such as the Child Tax Credit.
- Have older dependents, including children age 17 or older.
- Itemized deductions in the past.
- Are a two-income family.
- Have two or more jobs at the same time.
- Only work part of the year.
- Have high income or a complex tax return.

Those with more complex situations may need to use Publication 505, *Tax Withholding and Estimated Tax,* instead of the Withholding Calculator. This includes employees who owe self-employment tax, the alternative minimum tax or tax on unearned income from dependents. It can also help those who receive non-wage income, such as dividends, capital gains, rents and royalties. The publication includes worksheets and examples to guide taxpayers through these special situations.

Sooner is Better for a Paycheck Checkup

The IRS urges everyone to do a Paycheck Checkup as early in the year as possible so that if a tax withholding adjustment is needed, there is more time for withholding to happen evenly during the rest of the year. Waiting means there are fewer pay periods to withhold the necessary federal tax.

Changing Withholding

Employees can use the results from the Withholding Calculator to see if they need to complete a new Form W-4, *Employee's Withholding Allowance Certificate,* and submit it to their employer. In some instances, the calculator may recommend that the employee have an additional flat-dollar amount withheld each pay period. Taxpayers don't need to send this form to the IRS after giving it to their employer.

Those who don't pay taxes through withholding, or pay too little tax that way, may still use the Withholding Calculator to determine if they need to pay estimated tax to the IRS quarterly during the year. Those who are self-employed generally pay estimated taxes.

Draft Version of Form W-4 for 2020

Cross References

- IR-2019-98, May 31, 2019
- https://www.irs.gov/pub/irs-dft/fw4--dft.pdf

The IRS has issued a draft version of the 2020 Form W-4, *Employee's Withholding Allowance Certificate,* to be used to determine withholding for employees. A PDF of the draft version can be downloaded by using the www.irs.gov link above.

The revised form implements changes made following the 2017 Tax Cuts and Jobs Act (TCJA), which made major revisions affecting taxpayer withholding. The redesigned Form W-4 no longer uses the concept of withholding allowances, which was previously tied to the amount of the personal exemption. Due to changes in the law, personal exemptions are currently not a central feature of the tax code.

"The new draft Form W-4 reflects important feedback from the payroll community and others in the tax community," said IRS Commissioner Chuck Rettig. "The primary goals of the new design are to provide simplicity, accuracy and privacy for employees while minimizing burden for employers and payroll processors."

The IRS and Treasury collected extensive feedback over the past year while working closely with the payroll and tax community to develop a redesign that best serves taxpayers.

The IRS expects to release a near-final draft of the 2020 Form W-4 in mid-to-late July to give employers and payroll processors the tools they need to update systems before the final version of the form is released in November. To make additional improvements to this initial draft for 2020, the IRS is now accepting comments for 30 days. To facilitate review of this form, IRS is also releasing FAQs about the new design. Follow this link:

https://www.irs.gov/newsroom/faqs-on-the-early-release-of-the-2020-form-w-4

The IRS anticipates the related instructions for employers will be released in the next few weeks for comment as well.

The IRS reminds taxpayers that this draft Form W-4 is not for current use, but is a draft of the form to be used starting in 2020. Employees who have submitted a Form W-4 in any year before 2020 will not be required to submit a new form merely because of the redesign. Employers can continue to compute withholding based on the information from the employee's most recently submitted Form W-4.

For 2019, taxpayers should continue using the current Form W-4. The IRS also continues to encourage people to do a paycheck checkup as soon as possible to see if they are withholding the right amount of tax from their paychecks, particularly if they had too much or too little tax withheld when they filed their 2018 taxes earlier this year. People with major life changes, such as a marriage or a new child, should also check their withholding.

Taxation of State Income Tax Refunds

Cross References

- Rev. Rul. 2019-11

If a taxpayer receives a federal tax benefit from deducting state and local taxes, and in the following year the taxpayer receives a refund of all or a portion of those state taxes, a portion of the refund may be subject to federal income tax in the year the refund is received.

The issue is further complicated with the new $10,000 limit under the Tax Cuts and Jobs Act (TCJA). For tax years starting in 2018, the itemized deduction for taxes paid is limited to $10,000 ($5,000 MFS) for the aggregate of:

1) State and local property taxes not paid or accrued in carrying on a trade or business, or an activity related to the production of income (rental real estate activities), and
2) State and local income, war profits, and excess profits taxes (or sales taxes in lieu of income taxes, etc.) paid or accrued in the tax year.

It is this $10,000 limit under TCJA and the various situations that may apply that is the subject of a recent IRS revenue ruling. If a taxpayer pays only the proper amount of state and local tax in the prior year, then itemized deductions for that year may either be lower, or the taxpayer may have opted for the standard deduction. The taxpayer must determine in each situation the amount of itemized deductions (or standard deduction) that the taxpayer would have deducted in the prior year had the taxpayer paid only the proper amount of state tax. The taxpayer must then compare this amount to the total itemized deductions actually taken, or the standard deduction that could have been taken, and include the difference as income on the current year return if the taxpayer received a tax benefit in the prior tax year from that itemized deduction.

Assume that in the following examples, all of the taxpayers are single and itemize deductions on their federal income tax returns for 2018 in lieu of using the standard deduction of $12,000. The taxpayers did not pay or accrue the taxes in carrying on a trade or business or an activity for the production of income. Also assume that the taxpayers were not subject to AMT and were not entitled to any credit against income tax. Each taxpayer uses the cash method of accounting for reporting income and deducting expenses.

Example #1: *Amy paid local real property taxes of $4,000 and state income taxes of $5,000 in 2018. Amy's state and local tax deduction was not limited by IRC section 164(b)(6) because it was below $10,000. Including other allowable itemized deductions, Amy claimed a total of $14,000 in itemized deductions on her 2018 federal income tax return. In 2019, Amy received a $1,500 state income tax refund due to her overpayment of state income taxes in 2018. Had she paid only the proper amount of state income tax in 2018, her state and local tax deduction would have been reduced from $9,000 to $7,500. As a result, Amy's itemized deductions would have been reduced from $14,000 to $12,500, a difference of $1,500. Amy received a tax benefit from the overpayment of $1,500 in state income tax in 2018. Thus, Amy is required to include the entire $1,500 state income tax refund in her gross income for 2019.*

Example #2: *Brenda paid local real property taxes of $5,000 and state income taxes of $7,000 in 2018. IRC section 164(b)(6) limited her state and local tax deduction on her 2018 federal income tax return to $10,000. Brenda could not deduct $2,000 of the $12,000 state and local taxes paid. Including other allowable itemized deductions, Brenda claimed a total of $15,000 in itemized deductions on her 2018 federal income tax return. In 2019, Brenda received a $750 state income tax refund due to her overpayment of state income taxes in 2018. Had she paid only the proper amount of state income tax in 2018, her state and local tax deduction would have remained the same ($10,000) and Brenda's itemized deductions would have remained the same ($15,000). Brenda received no tax benefit from the overpayment of $750 in state income tax in 2018. Thus, she is not required to include the $750 state income tax refund in gross income for 2019.*

__Example #3:__ Cameron paid local real property taxes of $5,000 and state income taxes of $6,000 in 2018. IRC section 164(b)(6) limited Cameron's state and local tax deduction on her 2018 federal income tax return to $10,000. As a result, Cameron could not deduct $1,000 of the $11,000 state and local taxes paid. Including other allowable itemized deductions, Cameron claimed a total of $15,000 in itemized deductions on her 2018 federal income tax return. In 2019, Cameron received a $1,500 state income tax refund due to overpayment of state income taxes in 2018. Had she paid only the proper amount of state income tax in 2018, Cameron's state and local tax deduction would have been reduced from $10,000 to $9,500. As a result, Cameron's itemized deductions would have been reduced from $15,000 to $14,500, a difference of $500. Cameron received a tax benefit from $500 of the overpayment of state income tax in 2018. Thus, she is required to include $500 of the state income tax refund in gross income for 2019.

__Example #4:__ Deb paid local real property taxes of $4,250 and state income taxes of $6,000 in 2018. IRC section 164(b)(6) limited Deb's state and local tax deduction on her 2018 federal income tax return to $10,000. Thus, Deb could not deduct $250 of the $10,250 state and local taxes paid. Including other allowable itemized deductions, Deb claimed a total of $12,500 in itemized deductions on her 2018 federal income tax return. In 2019, she received a $1,000 state income tax refund due to the overpayment of state income taxes in 2018. Had Deb paid only the proper amount of state income tax in 2018, her state and local tax deduction would have been reduced from $10,000 to $9,250. As a result, Deb's itemized deductions would have been reduced from $12,500 to $11,750, which is less than the standard deduction of $12,000 for 2018. The difference between Deb's claimed itemized deductions ($12,500) and the standard deduction she could have taken ($12,000) is $500. Deb received a tax benefit from $500 of the overpayment of state income tax in 2018. Thus, Deb is required to include $500 of her state income tax refund in gross income for 2019.

Summary. If a taxpayer received a tax benefit from deducting state or local taxes in a prior year and the taxpayer recovers all or a portion of those taxes in the current year, the taxpayer must include in gross income the lesser of:

1) The difference between the taxpayer's total itemized deductions taken in the prior year and the amount of itemized deductions the taxpayer would have taken in the prior year had the taxpayer paid the proper amount of state and local tax, or
2) The difference between the taxpayer's itemized deductions taken in the prior year and the standard deduction amount for that prior year, if the taxpayer was not precluded from taking the standard deduction in that prior year.

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Strict Substantiation Requirements for Charitable Contributions

Cross References

- *Simpson*, T.C. Summary Opinion 2019-9, May 2, 2019

Under strict substantiation requirements for cash charitable contributions of less than $250, a taxpayer must have one of the following:

- A bank record such as a canceled check, bank statement, or credit card statement,
- A receipt with date, contribution amount, and organization name, or
- Payroll records and a pledge card, if made by payroll deduction.

For cash charitable contributions of $250 or more, a taxpayer must obtain a written acknowledgement from the charitable organization that shows the following:

- Date and amount of contribution,
- Whether any goods or services other than intangible religious benefits were provided by the organization (including a good faith estimate of the value), and
- A statement that the only benefit the taxpayer received was an intangible religious benefit (if applicable).

The taxpayers in this case deducted $2,125 for cash charitable contributions they made to their church for 2013. The taxpayers credibly testified during their tax court trial that they contributed tithes and offerings to their church by check and in cash during the year. They said they received a contribution letter each year from their church, but they did not keep a copy of the letter for 2013. The court understood their testimony to mean that they made regular contributions each of which may have been less than $250 to their church throughout the year.

A letter from their church, dated November 22, 2016, addressed to the taxpayers listed the total amounts of contributions it received from the taxpayers for 2011, 2012, and 2013. The letter explained that the church does not archive contribution letters for more than two years. For 2013 the letter lists contributions made by the taxpayers totaling $2,125 but does not indicate on what dates the contributions were made. The letter also states: "These donations were not in exchange for goods or services and are tax deductible."

The court stated the letter does not include the date(s) of the contributions as required by IRC section 170(f)(17). The court concluded that the taxpayers are not entitled

to deduct $2,125 for the cash charitable contributions they made to their church in 2013 because they failed to meet the recordkeeping requirements of the statute.

Note: The court stated the taxpayers credibly testified that they contributed tithes and offerings to their church. Since the practice of tithing is to contribute a percentage of ones earnings, it is reasonable to assume the court believed the taxpayers contributed regularly to their church. $2,125 ÷ 12 = $177. Assuming the taxpayers made cash contributions at least once per month based off of a percentage of their income, then each contribution would have been under the $250 stricter substantiation requirement. Had the taxpayers been able to produce cancelled checks, each less than $250, the letter from the church would not have been required. Thus, even if each contribution is under the $250 threshold, this court decision illustrates that proof of the date of each contribution is still required.