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# HARPER | PEARSON

## Tax Newsletter

**Know Tax Angles to Investments**
**Consider all tax repercussions**

If you are a savvy investor, you may have a diversified portfolio that includes various types of assets ranging from stocks and bonds to Certificates of Deposit (CDs) and bank accounts. What are the tax implications? The rules are complex, but following is a basic overview.

**Stocks:** Sales of securities like stocks result in capital gains and losses that can offset each other. Generally, short-term gains are taxed at ordinary income rates topping out at 37%, while long-term gains for stocks owned longer than one year are taxed at a maximum 15% rate (20% for high-income investors). Excess capital losses offset up to $3,000 of ordinary income before being carried over to the next year.

Stock dividends are currently taxable even if they are reinvested. Qualified dividends (most ordinary dividends) are taxed at the favorable long-term capital gain rates.

**Mutual funds:** Mutual funds, which generally provide greater diversification than stocks, are essentially taxed in the same manner. Typically, a mutual fund pays out taxable capital gains and dividends during the year. These distributions are subject to current tax even if the amounts are reinvested. Taxable gains or losses may be realized from sales of mutual fund shares.

**Exchange-traded funds:** Unlike mutual funds, few capital gains are generally realized through ownership of exchange-traded funds (ETFs). Thus, they are considered more tax-efficient, although some annual dividends are still paid out and subject to tax. Qualified dividends are taxed at long-term capital gain rates. Otherwise, ordinary income rates apply. Sales of ETFs may result in short- or long-term capital gains.

**Bonds:** Interest earned by bonds is generally taxable annually even if the bond has not matured. There are several types of bonds, including—

- Corporate bonds: They typically offer a higher rate of return than other bonds at a greater risk. The interest is taxable as ordinary income.

- Municipal bonds: The interest on bonds issued by certain government entities is exempt from federal income tax.

- U.S. Treasury bonds: These bonds are backed by the full faith and credit of the U.S. government. Generally, interest accrues and is taxed when amounts are withdrawn or the bonds mature.

**Real estate:** The basic capital gain and loss rules apply to sales of investment real estate. However, homeowners may realize a tax-exempt gain of up to $250,000 ($500,000 for joint filers) on the sale of a qualified principal residence. In addition, investors can exchange like-kind properties without any current tax if certain conditions are met. Other special rules may come into play for rental real estate activities.

**Cryptocurrency**: Although the law is still evolving, the IRS treats cryptocurrency as property comparable to securities for federal income tax purposes. Thus, if you sold Bitcoin or some other cryptocurrency in 2024, your return will reflect a short-term or long-term capital gain or loss, depending on the holding period.

**Precious metals:** Sales of precious metals like gold and silver result in gains or losses. Unlike most capital assets, however, any long-term gains are taxed at the 28% rate for "collectibles," as opposed to the usual 15% or 20% rate. Similar rules apply to other collectibles like antiques, stamps, coins and sports memorabilia.

**CDs and banks accounts:** You may have acquired CDs from banks or credit unions and keep various accounts at these financial institutions. Annual interest earned by checking and savings accounts is currently taxable. Similarly, CD interest is taxable in the year it accrues. Thus, if you buy a five-year CD, the tax is spread over five years unless you cash it in early.

This is only an outline of several basic tax rules relating to investments. Coordinate your investment strategies with your professional tax advisor.

**IRS Pinpoints Dirty Dozen Tax Scams**
**Watch out for these common schemes**

Shortly before the 2024 tax return deadline of April 15, the IRS listed its annual "Dirty "Dozen" list of tax scams. Taxpayers are advised to steer clear of these sophisticated schemes and cons. Following is an overview.

**1. Email phishing scams:** Taxpayers and tax professionals should be alert to fake communications from entities posing as legitimate organizations in the tax and financial community, including the IRS, state tax agencies and tax software companies. These messages arrive in the form of unsolicited texts or emails. There are two main types:

- Phishing is an email meant to look like it originated at the IRS. It may offer a phony refund or threaten to send you to prison.

- Shmishing is a type of text that states a problem—such as "Your account has been hacked"—and offers a bogus solution.

Reminder: Don't click on phishing or shmishing emails.

2. **Bad social media advice:** Social media platforms routinely circulate inaccurate or misleading tax information, including on TikTok where people often share wildly inaccurate tax advice. Some involve urging people to misuse common tax documents like Form W-2.

**3. IRS Individual Online Account help:** Crooks can pose as a "helpful" third party and offer to help create a taxpayer's Individual Online Account. But they are only trying to steal your personal information.

**4. Fake charities:** This problem often occurs whenever a crisis or natural disaster strikes. Scammers try to benefit from the public's generosity.

**5. False Fuel Tax Credit claims:** Taxpayers may be misled into believing they were eligible for the Fuel Tax Credit. But the credit is limited to off-highway business and farming use and is not available to most taxpayers.

**6. Credits for Sick Leave and Family Leave:** This specialized credit is available for self-employed individuals for 2020 and 2021 during the pandemic. But it cannot be claimed for later tax years, as some promotors pitch.

**7. Bogus self-employment tax credit:** Social media continues to circulate false info about a nonexistent "Self-Employment Tax Credit." Promoters market it as a way for self-employed people and gig workers to get big payments relating to the COVID-19 pandemic.

**8. Improper household employment taxes:** Taxpayers "invent" fictional household employees to claim a refund based on false sick and family medical leave wages they never paid.

**9. Overstated withholding scam:** This new scheme circulating on social media encourages people to fill out Form W-2 and 1099s with false income and withholding information. Then they request large refunds on their tax returns.

**10. Misleading Offers in Compromise:** The Offers in Compromise (OIC) program is an important program that helps people settle their federal tax debts when they are unable to pay in full. But "mills" can aggressively promote Offers in Compromise to people who clearly do not meet the qualifications, frequently costing taxpayers thousands of dollars.

**11. Ghost tax return preparers:** Most tax preparers provide outstanding and professional service. However, people should be careful of shady tax professionals and watch for common warning signs, including charging a fee based on the size of the refund. Another major red flag is when the tax preparer is unwilling to sign the return.

**12. New client scams and spear phishing:** Cybercriminals impersonate new, potential clients to trick tax professionals and other businesses into responding to their emails. Once the tax pro responds, the scammer sends a malicious attachment or URL that can compromise the preparer's computer systems.

Clearly, no one is immune to attempts by scammers. Remain vigilant.

**New Travels Rules Are for REAL**
**Identification required for travelers**

It is time for Americans to get REAL. Really!

The **REAL ID Act**, signed into law way back in 2005, sets standards for verifying identification of individuals, including requirements for drivers' licenses. The initial law was modified in 2018. If the updated standards are not met, an individual traveler will not be allowed to board commercial aircraft, beginning *May 7, 2025*.

In other words, if you do not have valid REAL ID in your possession, you generally cannot board a plane to your desired destination. Travelers will be stopped before they procced through the security section. This could lead to longer lines and flight delays, not to mention disgruntled passengers.

All states, as well as the District of Columbia and five U.S. territories, are compliant with REAL ID rules. If you have not yet obtained REAL ID, visit your state's driver's licensing agency website to find out exactly what documentation is required. At a minimum, you must provide evidence of the following five items:

**1**. Full legal name

**2.** Date of birth

**3.** Social Security Number (SSN)

**4.** Two proofs of address of principal residence

**5.** Lawful status

States may impose additional requirements, so check with your state's driver's licensing agency website for guidance.

REAL ID-compliant cards have a special marking on the upper top portion of the card such as a star or a star within a circle. If the card does not have one of these markings, it is not REAL ID-compliant and cannot be accepted as proof of identity for purposes of boarding commercial aircraft.

But a REAL ID card is not the only acceptable form of identification. Technically, you still may be able to board a plane for a domestic flight if you produce one of the following:

- Real ID-compliant state driver's license or other state photo identity card;
- U.S. passport or passport card;
- DHS-trusted traveler card (Global Entry, NEXUS, SENTRI, FAST);
- U.S. Department of Defense ID, including those issued to dependents;
- Permanent U.S. resident card;
- U.S. border crossing card;
- State-issued enhanced driver's license;
- Federally recognized, tribal-issued photo ID;
- HSPD-12 PIV card;
- Foreign government-issued passport;
- Canadian provincial driver's license or Indian and Northern Affairs Canada card;
- Transportation worker identification credentials;
- U.S. Citizenship and Immigration Services Employment Authorization Card (I-766);
- U.S. Merchant Mariner Credentials; or
- Veteran Health Identification Card.

Note that children under age 18 are not required to provide identification when traveling with a companion within the U.S. The companion, however, will need acceptable identification.

Finally, be mindful that a REAL ID is not a replacement for a passport. You still need a passport to travel internationally even if you have REAL ID card. (But a passport may be an acceptable alternative to REAL ID for domestic travel.)

**Caution:** These are the current rules applicable to U.S. travel. Stay alert to any future changes.

**Tax Keys to Home Office Deductions**
**Be wary of special recapture rule**

If you are like many members of the gig economy or self-employed individuals pursuing a personal passion, you may qualify for generous home office deductions on your 2024 tax return. But the question is: should you claim the maximum deduction? Despite your knee-jerk reaction, it may not be a slam-dunk.

**Background:** You are eligible to claim home office deductions only if you use part of the home regularly and exclusively as (1) your principal place of business or (2) a place where you meet or deal with customers, clients, or patients in the normal course of trade or business. For example, you may have set up a bedroom as the sole location of your self-employed consulting or freelance writing business.

Similarly, if you have no single fixed place of business and provide services at a multitude of different locations, you may still write off home office deductions if you handle administrative matters at home. This often applies to self-employed individuals such as interior designers, lawn care providers and other local businesses.

However, you cannot deduct any home office expenses if the work area is used more than incidentally for other purposes. For example, you do not qualify if you stick a work desk in a finished basement where your kids play with their toys. On the other hand, if a specific part of the basement is allocated exclusively to business use, you still may qualify for deductions.

If you deduct actual expenses, the list includes expenses directly related to your home office plus a portion of the home's overall expenses based on the percentage of business use of the home. Therefore, if you use 10% of your home for an office, you may deduct 100% of the cost of painting the office plus 10% of your mortgage interest, property taxes, utilities, repairs, home security, etc. (If you itemize deductions, you may otherwise qualify for mortgage interest and property tax deductions.) Finally, you may also claim a depreciation allowance for the home office, computed under IRS tables.

Alternatively, you may use a "simplified" deduction method equal to $5 per square foot of the area used as a business office, up to a maximum of $1,500, in lieu of deducting actual expenses. All home office expenses, including depreciation, are "built into" the simplified deduction.

Although the actual expense method usually produces a bigger overall deduction—sometime much bigger—there is one major hitch.

**Special rule:** If you subsequently sell the home, you must "recapture" any depreciation attributable to the home office after May 6, 1997, at the *25% tax rate*. This can result in an unpleasant tax surprise on the tax return for the year of the home sale.

The best approach is to examine your current situation. If you have just set up a home office and expect to move soon, you might bypass the home office deduction. Or you may opt for a smaller deduction through the simplified method that does not require depreciation recapture.

**Final point:** Fortunately, you do not have to go it alone. Your professional tax advisor can provide the necessary guidance.

**Tax Respite for CD Penalty**

Suppose you closed out a bank Certificate of Deposit (CD) before maturity. Not only do you owe income tax on the accrued interest, but you probably were also hit with an early withdrawal penalty.

**Saving grace:** The penalty for an early CD withdrawal can be deducted on your personal 2024 return. So, at least you salvage some tax benefit. What's more, the deduction is available whether you itemize or take the standard deduction.

This deduction can easily fall through the cracks, so check your records.

**Facts and Figures**
**Timely points of particular interest**

**For Late Filers**—If you are still scrambling to collect all the information needed to file your 2024 tax return, do not panic. The IRS allows you to obtain an automatic six-month extension—no questions asked—just by filing the proper form. This gives you until October 15, 2025, to complete your 2024 return. **Reminder:** An extension to file is *not* an extension to pay tax. You still must make a good faith estimate payment by April 15. Be careful to avoid an estimated tax liability for the year.

**Beneficial Ownership Rule**—On March 26, 2025, the **Financial Crimes Enforcement Network (FinCEN)** issued an interim final rule effectively eliminating the new requirement for U.S. companies and individuals to report "beneficial ownership information" (BOI) under the Corporate Transparency Act (CTA). The final rule clarifies and revises certain definitions included in the CTA. Bottom line: All entities created in the U.S. and their beneficial owners are exempt from the requirement to report BOI to FinCEN.