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FOR TAX YEAR 2021

Tax Matters

Insights to help navigate the implications of the current tax environment on your finances

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At time of publishing, significant legislation is under consideration in Washington that would impact the taxes paid by many Americans. Our Tax Policy & Research team is closely monitoring the outcome of the legislative process and all strategies discussed in this guide are subject to change. As always, we encourage you to consult with your strategic advisors in advance of taking any action. It is important to note that for some of these provisions, changes in their effective dates could make any year-end actions futile.

Relevant Tax Provisions

In 2018, the Tax Cuts and Jobs Act (TCJA) established a new paradigm for tax planning and preparation. Many taxpayers have been surprised by the disparity of their refund/amount owed from previous years.

Let's review a few key relevant provisions that all taxpayers should be aware of:

Income tax brackets and rates. The top bracket tax rate holds steady from 2020 at 37%, but the upper income limits for each bracket have increased slightly, indexed for inflation.

The standard deduction for single taxpayers is $12,550 for 2021 (up from $6,350 prior to the TCJA), and for married filing jointly, it is $25,100 this year. As a result, many who had itemized prior to the TCJA now take the standard deduction. An additional standard deduction of $1,350 is available in 2021 for taxpayers who are at least 65 years old.

Personal exemptions remain suspended (previously $4,050 per person).

The deduction for **state/local property taxes and income or sales taxes (SALT)** is currently limited to $10,000, but there is legislation under consideration that could increase or repeal this limit. This legislation could be effective for tax year 2021.

Unless grandfathered, the limit on mortgages qualifying for the **home mortgage deduction** is now $750,000 (down from $1,000,000).

The deductibility of **home equity loan interest** has been greatly curtailed. See more on pages five and six.

Miscellaneous itemized deductions (subject to the 2% of adjusted gross income [AGI] threshold) are suspended.

The **Alternative Minimum Tax (AMT) exemption** amount was significantly increased, and the threshhold for phaseout of the exemption was dramtically increased, which reduces the number of taxpayers subject to the AMT. See more on page seven.

The **Child Tax Credit (CTC)** has been changed for 2021 only as part of the American Rescue Plan Act. The new credit limit is $3,600 per child under age six and up to $3,000 for children ages 7-18. Previously, the credit was $2,000 per child regardless of age and the age limit for a qualifying child was 17. Limits apply based on modified AGI.

Also under the American Rescue Plan Act, the **Child & Dependent Care Credit (CDCC)** applicable credit rate is now 50%-0% (previously 35%-20%). Qualifying expenses are now limited to $8,000 per qualifying individual or $16,000 for 2+ qualifying individuals (previously $3,000 and $6,000 respectively). Limits apply based on AGI.

Year-end tax planning

There are a number of tax-related proposals under consideration in Congress that may impact several of these techniques. For a detailed look at tax changes under consideration in Washington and actions taxpayers may want to consider according to the proposed effective date of those changes, check out this **Insight** from specialists in our Tax Policy & Research group. Stay close to your advisor or tax specialist to discuss how potential changes could impact your personal situation. Here are a few strategies to consider from our tax specialists:

Bunching your deductions

As the standard deduction nearly doubled in the TCJA, many taxpayers are finding that their itemized deductions may not exceed their standard deduction most years. (In 2021, the standard deduction for head of household filers is $18,800. The standard deduction is $25,100 for married taxpayers filing jointly and qualifying widow(er)s and $12,550 for all other taxpayers.) These taxpayers may benefit by “bunching” itemized deductions in alternate tax years to get the maximum benefit from those deductions. For instance, if it is possible you will exceed the standard deduction in 2021 but are uncertain in 2022, consider accelerating those deductions into the current year (subject to limitations and AMT). Conversely, if you won’t itemize in 2021, think about delaying deductions into 2022. Second, when possible, “bunch” your deductions in the year where you are in a higher tax bracket to provide a greater tax benefit. If the SALT cap is raised or lifted, itemizing each year may become possible again for some taxpayers. This will be most impactful for those who have been taking the standard deduction one year and bunching/itemizing in alternate years and those living in states with a higher income tax.

State and local taxes

If your property tax payments have already exceeded the $10,000 SALT limitation, any acceleration into the current year will have no impact on your deductions for this year. Therefore, consider postponing such payments while being mindful of underpayment penalties. We recommend consulting your advisor or tax specialist, as this strategy is dependent on the timing of the property assessment by your local tax jurisdiction. Additionally, the SALT limit is of particular interest for Democrats who are looking to raise or repeal it, potentiality for tax year 2021. It is conceivable the SALT cap could be repealed or modified and if that happens, the timing of these deductions will need to be carefully considered. Our Tax Policy & Research team will be keeping a close eye on any developments.

Tax loss realization

Educated investors know that general tax doctrine allows for capital losses and capital gains to be aggregated. Realizing losses can be helpful in offsetting any realized gains. Further, should capital losses exceed capital gains, an individual is entitled to offset ordinary income in a given year up to $3,000 ($1,500 for married taxpayers filing a separate return), with the remainder being carried forward. As usual, there are many planning considerations relative to holding capital assets versus selling.

Taxpayers with gains could also consider investing in a Qualified Opportunity Fund (QOF). Investment in such a fund allows taxpayers to temporarily defer any gains realized within 180 days prior to the investment, although some or all of the gains deferred must be recognized no later than December 31, 2026, at then-applicable capital gains rates. Taxpayers may exclude gains from any appreciation in value of the QOF investment, if held for at least 10 years. There are some unique loss considerations for 2021 related to the COVID-19 pandemic. Check out pages 13-14 for an explanation of disaster relief that may be applicable to your personal situation.

Your withholdings under the TCJA

- The IRS released new withholding tables beginning with tax year 2018 reflecting the new tax rates and adjusted brackets
- The new withholding tables could impact any expected refund or balance due
- A bonus or lump-sum payment will likely be withheld at a flat rate of 22%
- When supplemental wages exceed $1 million, the flat withholding rate is at the top marginal rate of 37% (or possibly 39.6% if legislative proposals are enacted)
- Withholdings could be impacted by the ability to correctly file and use the new W-4 form
- To ensure you’re withholding the right amount, contact your tax advisor

Withholding is important to:

- Avoid incurring any underpayment penalties
- Avoid being surprised with an unexpected tax bill in April

Year-end tax planning

New equipment/infrastructure

If the taxpayer has a small business that needs new equipment, they can place the equipment in service in 2021 to qualify for depreciation (including, in most cases, 100% bonus depreciation). Alternatively, if the taxpayer expects to be in a higher tax bracket in 2022, they can delay the equipment purchase in order to offset income that would otherwise be taxed at a higher rate.

If the taxpayer is considering the purchase of any solar electric, solar water heating, fuel cell, small wind energy or geothermal heat pump property for a personal residence, there are timing considerations to keep in mind. Under current Residential Energy Efficient Property (REEP) proposals, the credit for that property would increase the credit back to 30% for systems installed between January 1, 2022 and December 31, 2031, before the credit is phased down in 2032 and 2033, and eliminated in 2034. The credit for systems installed in 2021 would remain at 26%. Taxpayers may want to consider waiting until 2022 to install one of these systems to see if the credit is increased. The Nonbusiness Energy Property credit proposed would extend and increase the credit for energy efficient windows, exterior doors and insulation from the previous lifetime cap of $500 to $1,200 every year up to the end of 2031.

Accelerating Income Into 2021

President Joe Biden has proposed a number of changes to the tax code that, at the time of publishing, are still under consideration in Congress. There are many questions surrounding the final details of this proposed legislation and our Tax Policy & Research team is monitoring the situation. Taxpayers should spend time at year-end projecting their income in 2021 and 2022. This is key to understanding if strategies for accelerating or decelerating income would apply to your personal situation, depending on your potential effective tax rate under the final outcome of proposed legislative changes. As always, we encourage you to consult with your strategic advisors in advance of taking any action. Taxpayers who believe that their marginal tax rate could go up in 2022 can consider some of the following common methods for accelerating income into 2021:

- Exercising non-qualified stock options
- Making an 83(b) election upon receipt of restricted property from an employer
- To the extent possible, billing customers and clients early enough that payment can be received prior to year end
- Manipulating (to the extent possible) the timing of discharge of indebtedness income

Previous proposals to increase long-term capital gains rates were taken out of the Build Back Better bill passed by the House in late November. There is nothing guaranteeing some sort of increase won't be reintroduced as the bill advances to the Senate. If that were to occur, taxpayers might want to consider timing of sales, depending on whether the provision is based on the date of introduction of the legislation or date of enactment. Alternatively, taxpayers may want to consider accelerating capital gains using these common strategies:

- Selling appreciated investments in 2021. (Note that no wash sale rule applies for investments sold at a gain, so taxpayers can repurchase investments immediately after the sale)
- Electing out of installment sale treatment
- Avoiding like-kind exchange treatment on an otherwise qualifying exchange

Cryptocurrency

Form 1040 now includes the following question: "At any time during 2021, did you receive, sell, send, exchange, or otherwise acquire any financial interest in any virtual currency?" Taxpayers who have, among other things, sold or exchanged cryptocurrency for cash or another cryptocurrency, paid for goods or services with cryptocurrency, transferred cryptocurrency to others, or received new units of cryptocurrency in a hard fork or for performing a task or service will likely have to answer yes to this question. They may also have additional reporting obligations related to these cryptocurrency transactions on a tax return.

Roth IRA conversions

A proposal is currently under consideration to prohibit after-tax IRA or 401(k) contributions from being converted to a Roth IRA, regardless of income level. Impacted taxpayers may want to consider converting any traditional IRA holding after-tax contributions in 2021.

Home mortgages and home equity

The TCJA changed the rules on interest deductibility of debt on a person's primary residence and on one secondary home. Be aware of how these changes may impact you.

Key changes to deductibility

Debt Type	Use	Secured by	Old	New
Acquisition Indebtedness	Buy, build or substantially improve a residence	The qualified residence the loan was used to purchase, build or improve	Indebtedness incurred on or before December 15, 2017: $1 Million	Indebtedness incurred after December 15, 2017: $750,000
Home Equity Indebtedness	Any (debt consolidation, educational expenses, etc.)	Any qualified residence	Prior to January 1, 2018: $100,000	As of January 1, 2018: No longer deductible, unless used for some otherwise deductible purpose

The rules governing the deductibility of interest on home-related debt can be complex, so we suggest reviewing with a tax advisor for clarity on how these change your personal tax planning.

Qualified residence

A qualified residence is your primary residence plus one secondary home. You can elect different secondary homes each year (but generally not mid-year).

Pitfalls

- If acquisition debt is refinanced and the principal of the new loan exceeds the principal outstanding on the mortgage at time of refinance, excess principal is not deemed acquisition debt and therefore is non-deductible interest (unless excess is used for improvements or some other deductible purpose, like purchasing taxable investments)
- The rules on deductibility for construction loans can be complex relative to the construction period, cash used and timing of lien

What about existing loans?

The TCJA allows the interest on most acquisition indebtedness incurred on or before December 15, 2017 to continue to take advantage of the prior $1 million limitation ($500,000 for married taxpayers filing separately).

New loans incurred after December 15, 2017 may also qualify for the $1 million limitation, but only to the extent they are used to refinance the remaining balance of loans incurred on or before December 15, 2017.

Home mortgages and home equity

Is it deductible? Here are some examples to help clarify:

Q. I have a current mortgage of $600,000. I recently took out a $300,000 mortgage in 2021 to buy a second home. Is the interest on all the debt deductible?

A. No. Under the new rules, only the interest up to $750,000 is deductible.

Q. We file as married filing jointly, and have a $500,000 mortgage. In 2021, we took out a $75,000 HELOC to build an addition on our house. Is this deductible?

A. Yes. Your total loan balance of $575,000 is under the $750,000 limit, and all HELOC proceeds were used to substantially improve your home. All the interest is deductible.

Q. I currently have a $100,000 HELOC which I took before the TCJA was passed. Can I still deduct the interest?

A. That depends...If the proceeds were used to buy, build or substantially improve the home securing the HELOC—and combined with other similar debt is under the limit—then yes. If the proceeds were used for other personal reasons, then it no longer qualifies.

Q. I currently have a mortgage of $800,000 which I incurred on or before December 15, 2017. If I do an $850,000 cash-out refinance of that mortgage, is the interest on the full $850,000 deductible?

A. No. Only the interest on the $800,000 being refinanced is deductible. A new loan that refinances an existing loan which was used to buy, build or improve a qualified residence and was incurred on or before December 15, 2017 will also be grandfathered into the prior $1 million limitation. However, the new loan will only be grandfathered up to the remaining balance of the existing loan. Any additional amounts taken out with the new loan will be subject to the $750,000 limitation, which is only available to the extent you are not already deducting interest on $750,000 of grandfathered indebtedness.

Alternative Minimum Tax (AMT)

Far fewer taxpayers will be included in the Alternative Minimum Tax (AMT) system for tax years 2018–2025, due to changes made under the TCJA.

Who falls into the AMT system?

Taxpayer	AMT Exemption Amount (2021)	Exemption Phase-out (2021)
Single	$73,600	$523,600
Married, filing jointly	$114,600	$1,047,200

The AMT is generally triggered when income exceeds the relevant exemption amount. This means taxpayers must calculate their tax liability under both the regular income tax system and the AMT system and then pay the higher of the two. For specific questions on calculations and tax liability, connect with your advisor or tax specialist.

Changes under the TCJA

Under the TCJA, the AMT exemption amount and phase-out thresholds for tax years 2018–2025 have been increased significantly. They will also be adjusted annually for inflation for tax years after 2018. The increased AMT exemption amount and phase-out thresholds are currently scheduled to sunset after 2025.

AMT payable

AMT is only payable to the extent the tentative minimum tax calculated under AMT rules exceeds the tax calculated under the regular tax rules. For example, if the regular tax is $40,000 and the tentative minimum tax is $45,000, the taxpayer pays the $40,000 of regular tax and $5,000 of AMT, for a total of $45,000.

Suspended deductions

Because these deductions have been suspended under the TCJA for tax years 2018-2025 for regular tax purposes, there is no difference between regular tax and AMT for:

- Regular tax personal exemptions (however, a separate AMT exemption applies)
- Interest on a home equity line that is not used to purchase, build or substantially improve the home
- Miscellaneous itemized deductions

Tax rate

- For 2021, the AMT tax rate is 26% of the AMT tax base up to $199,900 ($99,950 for married taxpayers filing separately) and 28% of the AMT tax base in excess of $199,900
- Capital gains rates of 0%, 15%, or 20% apply for AMT to the extent they apply for regular tax
- Qualified dividends are taxed at the same rate that applies to net capital gain

Credits

- The AMT Foreign Tax Credit is available to offset the AMT
- Individual taxpayers can offset their entire regular tax liability and AMT liability by their nonrefundable personal tax credits

Capital gains and qualified dividends

AMT may be an issue for taxpayers who have large capital gains and qualified dividends relative to other income—both are taxed at a 20% rate for AMT and regular tax purposes. When rates that apply for regular tax versus AMT are the same for a significant portion of income, the taxpayer may find they are in AMT, even with relatively few AMT add-backs. This is especially true for taxpayers in states with high tax rates.

State tax refund

Generally, a state income tax refund is taxable if itemized deductions were taken in the prior year. However, if the taxpayer was in the AMT that year, it's possible the taxpayer didn't benefit from the deductions (since state taxes are nondeductible under the AMT system). This could make some or all of the refund untaxable.

The AMT Credit

The AMT tax credit is available to reduce a taxpayer's regular tax liability in future years only if they are placed in the AMT by a timing difference. Timing differences occur when an item is taxable, or deductible, for both AMT purposes and regular tax purposes but AMT rules require that the income be recognized sooner—or the deduction be delayed longer—than is required for regular tax purposes.

The purpose of the credit is to avoid double taxation of an income item. The AMT credit can only be used in future years when the regular tax liability exceeds the AMT tax liability. Any portion of the credit that is not allowed in a given year may be carried forward indefinitely. The exercise of ISOs is a common example of a timing difference that triggers the AMT and, in turn, generates an AMT credit.

An informed approach to maximizing the tax benefit of your charitable contributions

Bunching

For taxpayers who have the ability to control the timing of charitable donations, bunching can help maximize the tax benefit by spreading contributions over alternating years. By delaying a year's worth of charitable giving from one year to the next, and giving double in the second year, the total amount of giving stays the same and the tax benefit over multiple years could be increased. Individuals will want to make sure that they are still under the percentage-of-AGI contribution limits for the particular year for the applicable charitable contribution category (i.e., 60%/30%/20%). The CARES act included some extender provisions, including (1) extending the above the line deduction of $300 for charitable contributions (now allowing $600 for a married couple filing jointly — for 2021 only, unless extended), and (2) increasing the higher limit on charitable cash contributions to provide COVID relief to 100% of an individual's AGI for 2021. In previous years, the limit was 60% under the TCJA. Qualified contributions are cash contributions made to a qualifying charitable organization(s). The taxpayer must elect the 100% limit on their 1040. Cash contributions made either to supporting organizations or to establish or maintain a donor-advised fund do not qualify, nor do cash contributions to private foundations and most cash contributions to charitable remainder trusts.

The benefit arises from:

- Making charitable gifts in the year in which you're in a higher tax bracket
- Avoiding charitable gifts in a year you won't itemize

Using donor-advised funds

One problem with the bunching strategy is that it leaves charities short on funding in off years. A solution to this problem (as well as a potential for even greater tax savings) is to contribute to a donor-advised fund (DAF).

A DAF is a charitable entity that allows donors to make tax-deductible contributions to the fund in the year of the gift, but then keep the funds in the account until the donor decides to make distributions to a particular charity. The donor can realize an upfront tax deduction in the current year, while retaining the ability to spread their grant-making over several years. A potential additional benefit to keeping funds in the DAF is that they can be invested to grow tax-free, providing even more funds to transfer to charity in the future.

Funding a DAF with appreciated securities held for more than one year can yield an even greater tax benefit.

There is no recognition of capital gains upon the transfer and you get a full tax deduction at the fair market value of the security.

Qualified charitable distribution

Those 70.5 years and older are allowed up to $100,000 per year to be transferred directly from an IRA to a qualifying charity on a tax-free basis. If you file a joint return, your spouse can also have a qualified charitable distribution and exclude up to $100,000.

The IRA owner can exclude otherwise taxable IRA distributions from income. Although no corresponding charitable itemized deduction is allowed for such excluded income, this can be used to satisfy the annual required minimum distribution (RMD) from the IRA.

Substantiation

The IRS is placing increased emphasis on having the necessary documentation to substantiate charitable deductions. Any donation of cash or property valued $250 or more requires a letter of acknowledgement from the receiving charity. Larger deductions—especially property—may require additional substantiation, such as an appraisal. There's also a deadline for such substantiation. Check with your tax advisor before December 31, 2021.

Nonresident state income taxation: A puzzling situation

If you work mostly in one state, but travel to work (or work from “home”) in other states—even for one day—you may be liable for income tax to those nonresident states if you are working there as an employee. Adding further complication, each state has its own definition of what constitutes income sourced to the state.

Some terms you may need to know:

- **Resident state:** Domicile is the place that the taxpayer considers “home” even though he or she may not be there frequently. It is the place to which the taxpayer eventually intends to return. Even if a person is not domiciled in a state, that person can still be considered a resident of the state based on that state’s rules for determining residency. You only have one domicile, but you can be a resident of more than one state
- **Nonresident state:** A state in which you work or earn income, but do not reside. If you live in one state, yet you’ve earned money in another state, you may have to file a nonresident state tax return depending on the state’s minimum filing requirements
- **Reciprocity:** A reciprocal agreement between usually neighboring states where workers from another state are only required to pay state and local taxes in their resident state
- **Board income:** Self-employment income earned by serving on a corporate board
- **Nonresident state tax credit:** Generally, if you pay income tax to a nonresident state, you are entitled to a credit against resident state taxes. There are limitations—ask your tax advisor

Tip: Be mindful of having a place of abode in a nonresident state.

Telecommuting

How telecommuting from a different state could impact your taxes

Whether you're working from home out of choice—or perhaps out of necessity due to the pandemic—you may face some unanticipated tax consequences as a telecommuter. That's especially true if you live in a state that's different from where your employer is located.

We've highlighted several scenarios that might apply to you, and provided some guidance. Even if you don't live or work in the locations mentioned, it's possible your tax situation could be similar based on applicable laws. Please contact your tax advisor for more details.

You're working from your second home which is located in a different state than you reside. Do you need to report your work-from-home (WFH) compensation to that state?

Yes, you will need to report income if that state taxes non-residents on any compensation earned (including WFH income) within its borders. Keep in mind, you'll also be taxed by your home state on those WFH wages. However, you might be able to receive a tax credit from your home state to alleviate the double taxation. You may need to pay estimated taxes to the nonresident state.

You're telecommuting frequently from your second home, but you're not domiciled in that state. Could you be considered a statutory resident?

Yes, it's possible. Each state has its own statutory resident standards. You should be aware of the criteria used by the state and record the number of working and non-working days spent there. Make sure to be accurate because state auditors may monitor your activity through your cell phone or credit card records.

You typically work in Manhattan. But you live in another state and have been strictly working from home during the COVID-19 crisis. Should you make estimated payments or switch withholding to your home state?

In regards to estimated payments, all your income will be taxed by your resident state. Keep in mind, New York State (NYS) has a "convenience of the employer" rule which gives it the authority to tax the wages of nonresident employees, like yourself, for work-related services they perform at their home office. However, you may be able to receive a credit from your home state for the WFH taxes paid to NYS, which may negate the need to make estimated payments to your resident state. Either way, you should continue to have your employer withhold to NYS, unless you plan on contesting the applicability of the state's convenience of the employer rule to your situation.

You primarily work in NYS, but don't live there. You've been telecommuting from your home in a different state during the pandemic. Will NYS still tax you for those days?

It's likely NYS will tax you based on the state's convenience of the employer rule which permits NYS to tax all your work-related income when you work from home. This even applies to income such as bonuses or equity compensation generated in 2021 but received in 2022.

You work and live in one state. However, you have a second home in another and occasionally telecommute from there (but not enough to be considered a statutory resident). Should you be concerned about any tax implications from the second state?

Yes. You'll typically face the normal home-state taxation on all your income. But, the second state may also tax you on any WFH days spent within its borders. While some resident states provide you with a tax credit to avoid this double-taxation scenario, not all do.

You live in Connecticut and usually work in Manhattan. During the health crisis, you've been working from home. Are there any tax implications to consider?

Yes. Connecticut will continue to tax all your work income as normal. Additionally, NYS will tax any telecommuting days performed in Connecticut. However, you should be able to receive a credit from Connecticut for the WFH taxes paid to NYS.

Nonresident state income taxation: A puzzling situation (continued)

With these scenarios in mind, some considerations that need to be weighed as you plan your taxes include:

- **Allocating income to a nonresident state.** Each state has its own rules for how sourced income should be allocated to the nonresident state. In many instances, it will depend on the type of income being allocated. A common approach is by using a days in/days out allocation over the calendar year
- **Keep a calendar.** It is crucial that detailed calendars be kept, substantiating where the work is being performed for nonresident allocation purposes and for possible relief from double taxation
- **Long-term awards, equity grants.** When allocating income to a nonresident state, it's natural to assume that one starts with W-2 wages. However, for the portion of W-2 earnings that were effectively earned over more than one year (e.g., three-year restricted stock vesting or stock option exercises during a 10 year grant), prior year work days count into the nonresident state calculation
- **Nonresident retirement income excluded.** Although the general rule is that a nonresident state can tax income that was earned for working in that state, there is a federal law that prohibits a nonresident state from taxing certain retirement income
- **Severance payments.** In most instances, severance payments are taxable to a nonresident state if the individual ever worked in that state. However, each state has its own rules
- **Nonresident state withholding.** Each state imposes its own withholding rules on an employer. These rules may be different from your resident state. It is always important to check the specific rules for each state
- **Place of abode.** If an individual maintains a place of abode in the nonresident state, they could be considered a statutory resident, depending on state law

Domicile

Changing your domicile may not be as easy as you think

The COVID-19 pandemic has dramatically impacted life in urban areas, leading many to seek shelter in states other than their normal residence. Some are reconsidering their long-term living arrangements, including the state where they maintain their domicile. Income taxes could be a major factor in this decision.

Your domicile is defined as the place where you have your true, fixed, permanent home—and the place to which, whenever absent, you intend to return. Your domicile does not change monthly or yearly. Once domiciled in a state, your domicile continues there until a new one is established.

To establish a new domicile, you must:

- Abandon your old domicile
- Have no intent to return to the old domicile
- Establish physical presence in a new state
- Have the intent to make the new state your domicile

While your intent is subjective, it is not enough to just say that you have the intent to change your domicile. State auditors will require you to prove your intent through a combination of facts and circumstances.

This is particularly relevant for those who've maintained a domicile in New York. There is a long list of factors that states consider when determining whether you've changed your domicile, but New York, in particular, relies heavily on the following five factors:

- The location of your near and dear items (often referred to as the "teddy bear test")
- The size and features of the home you live in as compared to other homes you may own
- The location of your business ties
- Time spent in New York as compared to the new domicile state
- Family connections (the location of your immediate family)

While it is often understood that you should change your driver's license to your new state of domicile, this action alone is NOT enough to change your domicile. Spending less than 183 days (six months, plus one day) is also often not enough to change your domicile.

Many states, including New York, have a statutory resident rule. This rule defines a resident as a person who maintains a permanent place of abode and spends more than 183 days in a state during the year—but this test does not apply to someone if they are already domiciled in the state. For example, if you are domiciled in New York, you will still be a New York resident even if you spend less than 183 days in New York in 2021.

Spending time out of your resident state, when you intend to return at a later time, does not change your domicile. This is true even if you don't know exactly when you will return. A temporary absence does not change your domicile.

Importantly, domicile audits do not occur immediately and often occur a few years after you changed your domicile. The analysis of auditors will take into account where you have been spending your time from the date you changed your domicile, up to when the audit occurs. What you do in 2021 would not be the only deciding factor.

If you are looking to change your domicile, continuing to own or rent a home in your former state can cause challenges when trying to prove your intent. Many of the difficult domicile audits that we have seen stem from individuals continuing to own or rent a home in New York after moving out.

Keep in mind, even in the case where you have legitimate intent to change your domicile and take proper steps to do so, that does not mean that you will no longer owe taxes to your former state. Certain states, including New York, have a convenience of the employer rule that taxes nonresidents on income earned or sourced to the state. For New York, this typically includes work performed from home for a company located in the state. New York will also tax any residual, sourced income you've earned in New York that is paid out at a later date. It is possible to end up in a situation where you will have to pay tax to your new domicile state and to the state where your employer resides, with no credit for the double tax.

Many of these considerations apply not just to changing domicile out of New York to another state, but rather a similar analysis applies to a domicile change to or from any state.

If you are considering changing your domicile and would like more guidance about this process, please reach out to your tax advisor.

Disaster relief

Disaster relief and the COVID-19 pandemic

On March 13, 2020, former President Trump proclaimed the COVID-19 outbreak in the United States constituted a national emergency, beginning March 1, 2020—making the entire United States a "disaster area" under the Emergency Assistance Act.

A presidentially declared disaster area with a national scope may create unique one-year loss carryback opportunities under §165(i) if a loss arising from a closed and completed transaction is attributable to the declared disaster and occurs within the disaster area. The critical issue for taxpayers attempting to claim a loss will be showing a sufficient connection between the disaster and the loss within the disaster area.

For tangible property, application under this rule is more straightforward. For intangible property, such as stocks and bonds, it will be more difficult to secure the one-year loss carryback.

In certain cases, there may be sufficient evidence to establish a loss that can meet the causation element and geographic boundary test under §165(i). All such cases will be highly dependent upon the specific facts and circumstances of the loss.

Some taxpayers may attempt to argue that sales of intangible securities at a loss are attributable to the disaster. At the present time, we do not recommend that individuals assume typical security losses upon sale will be eligible for carryback treatment under §165(i). Precedent is lacking for applying §165(i) in this context and individuals should not expect to carry back intangible investment property losses under most circumstances.

Potential changes to key personal casualty loss provisions

Earlier versions of the proposed legislation included a provision that would eliminate the TCJA limitation on personal casualty losses only allowable to the extent they were attributable to a federally declared disaster. This provision was not included in the most recent version of the bill. If reintroduced, it is possible that the change would be retroactive to tax years beginning after December 31, 2017, allowing the possibility of amending prior year returns. However, the likelihood of this provision making its way back into the bill is uncertain.

To determine if you qualify for disaster relief as a result of the COVID-19 pandemic, you should review your specific situation with your tax advisor.

Hurricane Ida

In IR-2021-175, the IRS announced that victims of Hurricane Ida have until January 3, 2022 to file various individual and business tax returns, and to make tax payments. Thus, individuals who had valid extensions for 2020 returns until October 15, 2021, now have until January to file.

The January deadline also applies to estimated payments due on September 15, 2021. Further, Individuals and businesses in a federally declared disaster area could choose to report unreimbursed disaster-related losses on their 2020 or 2021 returns. Taxpayers should include the FEMA disaster declaration number on any return claiming losses. This applies to various states, including Louisiana, Mississippi, New York, New Jersey and Pennsylvania. Please see the current list of eligible localities available on the disaster relief page on **IRS.gov.*** Also, note this only applies to Federal returns. Please consult each state's website to determine whether the state conforms to this filing relief.

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Disaster relief

Wildfires

Wildfire damage in a federally declared disaster area falls under the casualty loss deduction for federal income tax purposes. If you have personal, rental or business properties located in a federally declared disaster area, unexpected expenses or damage caused by the disaster may raise income tax questions.

Generally, damage caused by the disaster that is not reimbursed by your insurance or other sources is deductible, but you must file an insurance claim first. You cannot claim a deduction for losses while you have a reasonable expectation of receiving a reimbursement. However, not all casualty losses are deductible, so you may not be entitled to a deduction even though you had property damaged or destroyed by the disaster.

Determining the amount of your casualty loss can be complex. To calculate your deductible loss, generally, the amount is the lesser of the adjusted basis (the amount you originally paid for the property, plus the cost paid for any improvements, less any depreciation) immediately before the disaster or the decrease in fair market value (FMV) due to the disaster. If a business property is completely destroyed and the FMV is less than the adjusted basis, the loss is calculated solely on the adjusted basis (less any insurance proceeds).

In order to take a casualty loss deduction with respect to personal use property, you MUST file a timely claim if the property is covered by insurance.

When damaged property is located in a federally declared disaster area, you can elect to deduct the losses in either the year of the casualty, or you may amend and deduct the loss on the return for the year immediately before the casualty.

The Tax Cuts and Jobs Act of 2017 temporarily restricts the deduction for personal casualty losses to only those attributable to a federally declared disaster. It is important to note this limitation is for personal casualty losses, and not losses connected with a business. Several of the California wildfires have been declared federal disasters. FEMA publishes a list of federally declared disasters at **www.fema.gov/disasters**,* as well as links to various resources and assistance available to individuals impacted by a disaster. Taxpayers with personal casualty losses outside of these designated disaster areas can only deduct those losses to offset personal casualty gains.

The IRS has some helpful information on recovering from disasters on its website, including how to request copies or transcripts of previously filed tax returns and other possible disaster relief programs. There's also an IRS Disaster Assistance Hotline, which can be reached at 1-866-562-5227. IRS Publication 547 (Casualties, Disasters, and Thefts) is an excellent resource to reference for more information regarding the tax deductibility of a casualty loss, as well as IRS Form 4684 (Casualties and Thefts) and its instructions.

If you have any other questions about the financial implications of a natural disaster, you can contact an advisor for help.

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Foreign Financial Assets

If you have an interest in a foreign financial asset, you may need to file a special return, in addition to your federal and state tax returns. While these forms are just informational and will not impact your taxes, there are significant potential penalties for noncompliance. If you hold any foreign financial assets, you should be aware of the various form-filing obligations that may exist.

Common assets/scenarios that can trigger informational form filings

Financial interest in or signature authority over a "foreign financial account"

- Examples of foreign financial accounts:
  - Foreign bank accounts, foreign brokerage accounts and cash value accounts from foreign insurance policies
- Filing obligation:
  - Report of Foreign Bank and Financial Accounts (FBAR)
- Penalties for failing to report:
  - Non-willful violation: $10,000 adjusted annually for inflation
  - Willful violation: $100,000 or 50% of the account balance at the time of the violation

Interest in "specified foreign financial assets" exceeding—in the aggregate—the applicable filing threshold

- Examples of specified foreign financial assets:
  - Foreign bank accounts, foreign brokerage accounts, foreign pension and other retirement accounts, and an interest in any foreign corporation, partnership, trust or estate
- Filing obligation:
  - Form 8938
- Penalties for failing to report:
  - $10,000 penalty per year of noncompliance

Investing over $100,000 in a foreign entity within a 12-month period

- Filing obligation:
  - Form 8865 (for a foreign partnership) or Form 926 (for a foreign corporation)
- Penalty for failing to report:
  - 10% of the FMV of the amount transferred—capped at $100,000, unless the failure was due to intentional disregard

Holding 10%+ interest in a foreign entity

- Filing obligation:
  - Form 8865 (for a foreign partnership) or Form 5471 (for a foreign corporation)
- Penalty for failing to report
  - Form 8865 and Form 5471: $10,000 per year of noncompliance

Receiving a gift or bequest from a nonresident alien individual or foreign estate in excess of $100,000 per calendar year

- Filing obligation:
  - Form 3520
- Penalty for failing to report:
  - 25% of the fair market value of the gift/bequest

Various interactions with a "foreign trust"

- Examples of transactions that trigger an obligation:
  - Creating a foreign trust, making transfers to or receiving distributions from a foreign trust, and being considered the owner of a foreign trust under the U.S. grantor trust income tax rules
- Filing obligation:
  - Form 3520 and/or 3520-A
- Penalties for failing to report:
  - Generally range from $10,000 to 35% of gross trust assets

If you identify the need to file delinquent international forms, the IRS provides several options for coming into compliance. In many cases, you will need to work with a qualified attorney to determine which procedure is most appropriate for your specific situation, and to guide you through the process itself.

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