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Resolute Connections

With so many of us now working from home, or at least trying to work, we thought the following article might answer the question - *Who Qualifies for the Home Office Deduction?*

Street protests are being held around the world, but one area in which protests are taking place for a different reason is Hong Kong. This situation has been getting little notice in the US media. *Why China's Takeover of Hong Kong Matters to Us* makes the case that we should not ignore what is happening in that area of the globe.

Lower Rates, Little Impact explains what the Federal Reserve Board interest rates cut actually means to you and me. And *Estate Planning Made Easier* discusses a little know estate planning technique that may be helpful for some of us down the road.

Please be safe and we wish you continued health. If you have any questions about anything we have covered in the articles, or a specific situation please feel free to give us a call, or visit our website, www.ResoluteFinancial.com.

Who Qualifies for the Home Office Deduction?

Many people are doing their jobs from home on a sustained basis for the first time in their careers. They have had to set up a home office. Does that mean they can claim a home office deduction, even though they still have a workstation, cubicle or office at their place of work?

The bad news is that the Tax Cut & Jobs Act of 2017 severely curbed what had been a valuable home office deduction for staff people who had to do some of their work at home. Previously, people could deduct unreimbursed job expenses that exceeded two percent of their adjusted gross income on their income tax return. Since 2018, employees working at home can no longer deduct their out-of-pocket expenses. Only gig workers and self-employed free-lancers could still claim the deduction for qualifying costs—the rental or mortgage cost of the part of their home that was used as a home office, plus maintenance, insurance, utilities, a proportionate share of property taxes and security system fees.

The bottom line is that you need to have self-employment income to benefit from the home office deduction. If you find yourself temporarily furloughed and start taking on assignments on the side, then you can claim the education if your home is your principal place of business, and if you have set aside a "separately identifiable space" in the home (not, say, the kitchen table). During this pandemic, every penny—and tax savings—counts.

Why China's Takeover of Hong Kong Matters to Us

While most of us are distracted by the street protests around the U.S., something similar has been going on in Hong Kong for years, and there are signs that the protesters in the semi-autonomous city are losing in their efforts to stop the communist Chinese regime from taking over. Most recently, Beijing's highest representative body in Hong Kong, called the Liaison Office, insisted that it was not subject to Article 22 of the city's constitution, which guarantees an independent government for the city and the region. Instead, the Liaison Office asserted that, contrary to the plain text of the city's constitution, it had "supervisory powers" to administer Hong Kong and its political affairs.

This move could have significant implications for the U.S. economy, because it endangers Hong Kong's 'special status' under U.S. law. If Hong Kong is no longer an autonomous political and economic entity, then the U.S. could well decide to treat it as simply a part of the Chinese economy—and that would mean an end to Hong

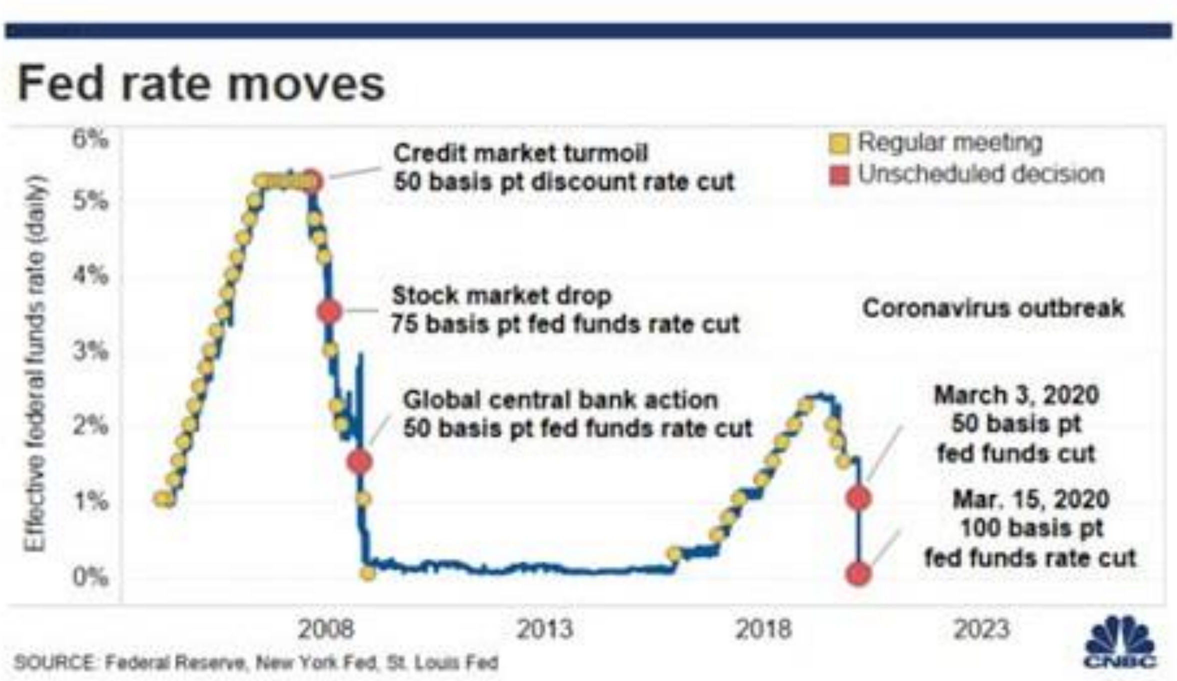
Kong's low preferential tariff rate, reverting it to the trade war tariffs that the U.S. has imposed on China as a whole.

Today, more than 1,300 American companies have business operations in Hong King, including nearly every major U.S. financial firm. According to the State Department, roughly 85,000 U.S. citizens live and work in Hong Kong, representing American companies. If the Trump Administration revokes special status, it could lead to an exodus of those firms, and an expensive relocation to cities like Singapore. It would also anger the Chinese leadership, and lead to another round of trade wars between the world's two largest economies.

Lower Rates, Little Impact

During times of economic crisis—like today—we read that the Federal Reserve Board has "cut interest rates," or "lowered the Fed funds rate." But what does that actually mean to you and me?

The following chart tells an interesting story; it shows the Fed funds rate—the rate that the Fed charges banks when they take out virtually unlimited short-term loans from the Fed or each other—rising steadily from around 2004 to late 2008. After the brokerage industry suddenly took the global economy to the edge of bankruptcy, you see the Fed dramatically lowering its discount rates to the banking industry, down to essentially zero for the next eight years. Then there was a very cautious period when the Fed governors started raising rates, until the COVID-19 virus started tanking the markets. Now we're back to zero again.



So, the first thing to know is that the banking industry—particularly the banks affiliated with the largest brokerage firms—can borrow as much money as it wants without paying any interest. Try to get the same deal from your local bank.

This low discount rate has a number of real-world consequences. One is that the brokerage and banking firms can lend money, at a profit (basically anything above zero percent) to companies that need to borrow. Theoretically, that will boost the economy. However, both in 2008-9 and now, banks were leery about lending to businesses in an uncertain economy. They can still lose money, after all, if the borrower goes bankrupt and defaults on the loan.

For consumers, there are small impacts. One is that credit card rates are down from a high of 17.85% last July, when the Fed started cutting rates, to a three year low of 16.46% today. If you think that's a very incremental decrease compared with the magnitude of the Fed moves, well, you're right. And the economic impact is diminished further, since banks are making credit cards much harder to obtain in this uncertain environment.

Finally, mortgage rates are slightly lower today than they were a year ago; Bankrate says that the average 30-year fixed rate is down to 3.55%. Yet again, however, banks have stopped offering many of their refinancing options due to the shaky economy, making it hard for homeowners to obtain this rate.

There must be a great deal of frustration in the Federal Reserve building these days, at the ineffectiveness of their bold moves to get the economy moving again. Over and over again, their actions are blunted by the self-interested actions of the big banks and brokerage firms—and there's no sign that that is going to change any time soon.

Estate Planning Made Easier

Most people no longer have to worry too much about the federal estate tax, since (currently) $11.58 million is sheltered from federal taxes for the heirs of each person; $23.16 million for couples. Any unused amount after one spouse dies can be applied to shelter estate assets whenever the surviving spouse dies.

But what about wealthy people who will pass on more than that to their heirs? Or what if the current $11.58M exemption is lowered to 2000 era levels of $1M per person as many in DC seem to desire? Is there any way to mitigate the nasty 40% tax, or perhaps 50% if some have their way, bite on estates for any dollars passed on above those thresholds?

The current investment environment seems like the worst of all possible worlds: practically nonexistent interest rates and bear market returns. But it offers an unprecedented opportunity for high-end estate planning. To cite one opportunity, a wealthy individual who is worried about estate taxes can lend some of the money she wanted to pass on to her heirs. In order to avoid having to pay gift taxes on the transactions, the heirs must pay interest at a rate of at least the so-called Section 7520 rate, which is adjusted monthly based on current interest rates. The current rate, 0.8%, happens to stand at a record low, down from well above 2% for most of last year. The previous record low was 1% in January 2013.

That is the rate for loans that are paid back within 9-20 years; the rate for shorter (3-9 year loans) fell to 0.58% in May. The estate planning strategy is for the heirs to invest the assets and, theoretically, earn a much higher return than the amount that has to be paid back to the parents. The investment returns more than pay the interest and loan repayments, and at the end of the term, the heir's pocket whatever is left estate-tax free.

At the same time, lower valuations on stocks, due to the recent bear market decline, makes it more beneficial to sell assets (at low current prices) to trusts or other structures that would benefit future generations. The gains in those assets take place in the hands of the heirs.

Source:
Bob Veres Inside Edition Newsletter

For more information on these topics or for a free consultation, contact Resolute Financial, LLC at (978) 463-8771 ext. 1003.