TAX RETURN MISTAKES
AND ERROR PREVENTION
FOR 2020

March 12, 2020
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- one CPE for CPAs credit

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Bruce Brumberg, Editor-in-Chief and Co-Founder, myStockOptions.com

- Award-winning online resource center, has received a patent and has been featured in publications ranging from the San Francisco Chronicle to Money magazine.

- Human Resource Executive magazine featured myStockOptions.com as one of the 10 Best HR Products.

- Past President of the Boston NASPP chapter

- On the NASPP Advisory Board, and contributor to the Stock Plan Advisor.

- Producer of the “Think Twice” insider trading prevention videos (www.insidertradingvideos.com).

- Write popular blog for Forbes.com

- Bruce graduated from the University of Michigan and University of Virginia School of Law.
Tax Season 2020: What You Need To Know About New Reporting Rules

by The myStockOptions Editorial Team

Ready or not, tax-return reporting has changed yet again for the 2020 tax season. Prepare yourself with this article. Our editorial team presents the key points you need to know for your federal tax return if you had income in 2019 from stock compensation, such as stock options, restricted stock units, or an employee stock purchase plan (ESPP), or if you sold shares of company stock. Then use the resources in our Tax Center, which show you how to report this income on your tax return.

12 Tax-Return Mistakes To Avoid With Stock Options And ESPPs

Puzzled by your Form W-2, 1099-B, 3921, or 3922? Need to report sales of stock on Form 8949 and Schedule D? Tax returns involving income from stock options or ESPPs can be confusing. Recent changes in IRS reporting rules haven’t helped. This article explains errors and nasty surprises to avoid.

Restricted Stock & RSUs: 10 Mistakes To Avoid On Your Tax Return

Tax returns involving income from restricted stock and restricted stock units (RSUs) can be confusing. The potential for mistakes has been increased by recent
Tax Center

As featured in PLANSponsor, Accounting Today, and CPA Practice Advisor, the myStockOptions Tax Center explains the tax withholding, reporting, and filing for stock options, restricted stock/RSUs, performance shares, ESPPs, and SARS.

- Test your knowledge with our NEW! Tax Cuts & Jobs Act quiz and interactive answer key!
- Test your knowledge with our NEW! Tax Returns quiz and interactive answer key!
- Test your knowledge with our Taxes quiz and interactive answer key!
- Want to know more? Listen to our podcast on tax return tips and mistakes!
- Check out our podcast and video on the tax forms and reporting rules.

Selected Articles

TAX CHANGES UPDATES!

Tax Season 2020: What You Need To Know About New Reporting Rules

The myStockOptions Editorial Team

Ready or not, tax-return reporting has changed yet again for the 2020 tax season. Prepare yourself with this article. Our editorial team presents the key points you need to know for your federal tax return if you had income in 2019 from stock compensation, such as stock options, restricted stock units, or an employee stock purchase plan (ESPP), or if you sold

Special resources for tax season
Roadmap for presentation

- What’s new for the 2020 tax-return season (reporting for 2019 income)
- Review of rules for cost-basis reporting
- Common questions and errors
- Communication and education for employees, executives, and clients
Main points about the Tax Cuts & Jobs Act Related to Stock Compensation

1. Flat rate used for stock compensation income withholding (supplemental wage income) is now 22%.

2. For amounts over $1 million per year: 37%

What this means:

- The 24% tax bracket starts with yearly income over $168,400 for joint filers and over $84,200 for singles. Most employees with stock compensation are in a higher tax bracket.

- Need to know the tax bracket for total income and assess need to put money aside or pay estimated taxes.
### Key bracket thresholds for federal income tax

Tax thresholds for 2019 ordinary income, capital gains, and dividends:

<table>
<thead>
<tr>
<th>TAX RATE/IMPACT</th>
<th>INCOME THRESHOLD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income taxed at 37%</td>
<td>$510,301 single&lt;br&gt;$612,351 joint&lt;br&gt;(taxable income)</td>
</tr>
<tr>
<td>Other upper income tax rates: 22%, 24%, 32%, 35%</td>
<td>For singles, taxable income starting at:&lt;br&gt;$39,476, $84,201, $160,726, $204,101&lt;br&gt;For married joint filers, taxable income starting at:&lt;br&gt;$78,951, $168,401, $321,451, $408,201</td>
</tr>
<tr>
<td>Capital gains (long-term) and dividends (qualified) taxed at 20%</td>
<td>$434,550 single&lt;br&gt;$488,850 joint&lt;br&gt;(taxable income)</td>
</tr>
<tr>
<td>3.8% Medicare surtax on investment income; additional 0.9% Medicare tax on compensation income</td>
<td>$200,000 single&lt;br&gt;$250,000 joint&lt;br&gt;(modified adjusted gross income)</td>
</tr>
</tbody>
</table>
Underpayment of taxes

Pay though withholding and estimated taxes amount equal to:

1. 90% of the current year's tax liability

2. 100% of last year's tax liability (110% if your adjusted gross income exceeded $150,000/$75,000 married filing separate return).

2019 Tax Season: Tax penalty changed when too little paid during year

- For 2018 taxes, the IRS lowered the 90% requirement to 80%.

- Removed the requirement that estimated tax payments be sent in four equal installments.

- August 2019: IRS announced it was automatically waiving the estimated tax penalty for the more than 400,000 eligible taxpayers who had already filed their 2018 federal income tax returns but did not claim the waiver at the lower threshold.

- The IRS is not expected to do the same for 2019 taxes, although the federal tax deadline is likely to get extended beyond April 15, 2020 if suffered adverse effects from the spreading virus (March 12, 2020 at 11:30 AM EST).
Main points about Tax Cuts & Jobs Act related to stock compensation

AMT or how it applies to ISOs is not repealed. New key numbers in the AMT calculation (adjusted annually for inflation):

- The AMT income exemption amount rises to $70,300 (from $54,300) for single filers and to $109,400 (from $84,500) for married joint filers.

- Under the TCJA, the AMT income exemption starts to phase out begins at $500,000 for individuals (up from $120,700 in 2017) and $1,000,000 (up from $160,900) for married filers. BIG CHANGE!

What this means: These changes, plus SALT limit make it much less likely to trigger AMT from ISO exercise and hold.
**AMT: Important for ISOs**

**Alternative minimum tax (AMT):** The income exemption amounts, the phaseout ranges, and the threshold for the higher 28% rate are now all indexed for inflation. The table below, prepared by myStockOptions.com, shows the 2019 figures.

<table>
<thead>
<tr>
<th>Filer status</th>
<th>AMT income exemption amount</th>
<th>AMT income exemption phaseout starts</th>
<th>AMT income exemption phaseout ends (myStockOptions.com)</th>
<th>Threshold where AMT rate rises from 26% to 28%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single</td>
<td>$71,700</td>
<td>$510,300</td>
<td>$797,100</td>
<td>$194,800 (married filing separately: $97,400)</td>
</tr>
<tr>
<td>Joint</td>
<td>$111,700</td>
<td>$1,020,600</td>
<td>$1,467,400</td>
<td>$194,800</td>
</tr>
</tbody>
</table>
Polling Question #1

How has the Form 1040 tax return changed for this tax season?

a) The number of lines on main form greatly reduced

b) New schedules have been added

c) Schedule D capital gains totals reported on Form 1040 directly

d) No longer itemize deductions
Polling Question #1

How has the Form 1040 tax return changed for this tax season?

a) The number of lines on main form greatly reduced

b) New schedules have been added

c) Schedule D capital gains totals reported on Form 1040 directly

d) No longer itemize deductions
Form 1040 changes, new schedules

- Form 1040 tax return, condensed in 2018, has been revised again for the 2019 tax year.

- The numbered schedules (supplementary forms) of Form 1040 have been reduced to three (Schedules 1, 2, 3).


- On the 2019 Form 1040, total capital gain or loss on Schedule D is once again entered directly on IRS Form 1040, not on Schedule 1 as it was last year.

- The AMT calculation total on Form 6251 is entered on a different line of Schedule 2

See myStockOptions article: Tax Season 2020: What You Need To Know About The New Reporting Rules
SECURE Act & Kiddie Tax

- Kiddie Tax: Informal name of a tax-code provision that applies to a child’s unearned income (e.g. interest, capital gains, dividends).

- Tax applies to children under 19 (for full-time students, under 24).

- In 2019 (and 2020) the first $1,100 of a dependent child's unearned income is tax-free (offset by the child's standard deduction), the second $1,100 of unearned income is taxed at the child's tax rate, and any amount over $2,200 is taxed at rate changed by SECURE Act.

- At year-end 2019, Congress repealed a provision in the TCJA that had made the rate over $2,200 the tax rates for estates and trusts. This move restored the rate to the parents' top marginal tax rate.

- For 2019 income, and retroactively to 2018 income, taxpayers can choose which rate system to apply
Coverage of IRS Form 1040 changes in my blog at Forbes.com.

Editors’ Pick!
No changes in other forms for tax-return reporting this year

- Similar to last year: Form W-2, Form 1099-B, Form 8949, Schedule D
- Big change in 2020 W-4 and next year in 1099-MISC with new 1099-NEC
- Same restrictions in what brokers can report for the cost basis on Form 1099-B
- **Good news:** The core reporting rules for cost basis Form 8949 and Schedule D have not changed
Ten tax-return issues and errors

1. Not reporting stock sales on Form 8949/Schedule D
2. Not reporting tax basis correctly on Form 8949
3. Double-counting income from W-2
4. Forgetting about AMT calculation or AMT credits
5. Sell-to-cover exercises
6. Share withholding for restricted stock/RSUs
7. Dividends with restricted stock
8. Not reporting ordinary income with ESPP sales
9. Netting of income & no longer Schedule 1 for stock sales
10. Extensions
myStockOptions Knowledge Center for plan participants

Licensed by companies and stock plan providers.
Polling Question #2

If employees sold stock during the calendar year, which tax forms do they file with their IRS Form 1040 to report the sale?

a)  Form 1099-B and Schedule A

b)  Form 8949 and Schedule D

c)  Form 6251, Schedule C, Schedule 1

d)  Form 1099-MISC and Schedule D
Polling Question #2

If employees sold stock during the calendar year, which tax forms do they file with their IRS Form 1040 to report the sale?

a) Form 1099-B and Schedule A

b) Form 8949 and Schedule D

c) Form 6251, Schedule C, Schedule 1

d) Form 1099-MISC and Schedule D
1. Not reporting stock sales on Form 8949 and Schedule D

- **Event:** Sell all stock at exercise (i.e. a cashless exercise), restricted stock/RSU vesting, or ESPP purchase.

- **Employee may think:** No “gains” beyond what’s on W-2 for ordinary income. May not realize there are **two reportable events**.

- **Result of incorrect thinking:** employee does not report sale on Form 8949/Schedule D.

- IRS gets 1099-B from broker. IRS computers note no Form 8949/Schedule D reporting for it.

1. Not reporting stock sales on Form 8949 and Schedule D

- Company and broker meet certain conditions: employee may not receive a Form 1099-B.
- Employee must still file Form 8949/Schedule D to report sale.
- **Employee may even have small gains or losses** for any commissions and fees for the stock sale.
1. Not reporting stock sales on Form 8949 and Schedule D

**Example:** Exercised options and sold 2,000 shares on August 14.

<table>
<thead>
<tr>
<th><strong>Exercise price</strong></th>
<th>$10 per share ($20,000 total)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Stock price at exercise/sale:</strong> $35</td>
<td>$70,000 proceeds, minus $500 commission ($69,500 net on Form 1099-B)</td>
</tr>
<tr>
<td><strong>What appears on Form W-2</strong></td>
<td>$50,000 income on exercise spread [($35-$10) x 2,000]</td>
</tr>
<tr>
<td><strong>Tax basis</strong></td>
<td>$70,000 ($20,000 + $50,000). But what is on 1099-B? $20,000 or $70,000?</td>
</tr>
<tr>
<td><strong>Schedule D (Part 1)</strong></td>
<td>Included as a $500 short-term capital loss</td>
</tr>
</tbody>
</table>

If sale is not reported, IRS gets 1099-B with the $70,000 proceeds and sends employee letter looking for taxes on that full amount!
**NQSO: Cashless Exercise**

**Form 8949**

Sales and Other Dispositions of Capital Assets

Department of the Treasury
Internal Revenue Service

**Information about Form 8949 and its separate instructions is at www.irs.gov/form8949.**

**File with your Schedule D to list your transactions for lines 15, 16, 18, 19, 20, 21, 22, 23, 24, and 25 of Schedule D.**

**Name(s) shown on return: [Blank]  Social security number or taxpayer identification number [Blank]**

Before you check Box A, B, or C below, see whether you received any Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

**Part I Short-Term. Transactions involving capital assets you held 1 year or less are short term. For long-term transactions, see page 2.**

**Note:** You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1c; you aren’t required to report these transactions on Form 8949 (see instructions).

You must check Box A, B, or C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

<table>
<thead>
<tr>
<th>On Form 1099-B *</th>
<th>Basis in Box 1c of 1099-B is correct</th>
<th>Basis in Box 1e of 1099-B is too low or blank</th>
<th>Basis in Box 1f of 1099-B is too low or blank</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS (see Note above)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>Short-term transactions reported on Form(s) 1099-B showing basis wasn’t reported to the IRS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C</td>
<td>Short-term transactions not reported to you on Form 1099-B</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Adjustment, if any, to gain or loss**

If you enter an amount in column (g), enter a code in column (k) and see the separate instructions.

**Company ticker symbol and number of shares sold**

[Box 1a on Form 1099-B]

**Exercise date**

[Box 1b on 1099-B]

**Date stock sold**

[Box 1c on 1099-B]

**Gross proceeds from stock sale**

[Box 1d on 1099-B]

**If commissions and fees were not subtracted from proceeds, see footnote.**

**Column (a): Basis in Box 1e of 1099-B**

**Column (b): Code B**

**Column (c): Limited amount (e.g., W-2 compensation not included). Put in parentheses to indicate a negative number (as this amount reduces gain or increases loss). For NQSOs, this is the exercise spread.***

**Column (d): Basis in Box 1f of 1099-B**

**Column (e): Code B**

**Column (f): Leave blank**

**Column (g): Leave blank**

**Column (h): Leave blank**

**Column (i): Enter "A.***

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*myStockOptions.com*

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Computershare
Annotated diagrams of Form 8949 and Schedule D on myStockOptions.com and in Knowledge Center
2. Not Reporting Cost Basis Correctly:

Cost basis (also called the tax basis) is the total cost of acquiring security:

\[
\text{Price paid to acquire shares} + \text{compensation recognized for acquiring them (reported on W-2)}
\]

When you sell a security, you **need to know the cost basis** to determine:

whether you have a capital gain or a capital loss for tax purposes.

\[
\text{NET PROCEEDS} - \text{COST BASIS} = \text{CAPITAL GAIN OR LOSS}
\]

Cost basis too low: you **overpay** taxes.
**Cost Basis Reporting:** IRS Form 1099-B core boxes (brokers use substitute statement with columns)

---

<table>
<thead>
<tr>
<th>Description</th>
<th>Form 1099-B Core Boxes</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1a Description of property:</strong></td>
<td>Example: 100 sh. XYZ Co.</td>
</tr>
<tr>
<td><strong>1b Date acquired</strong></td>
<td>$</td>
</tr>
<tr>
<td><strong>1c Date sold or disposed</strong></td>
<td>$</td>
</tr>
<tr>
<td><strong>1d Proceeds</strong></td>
<td>$</td>
</tr>
<tr>
<td><strong>1e Cost or other basis</strong></td>
<td>$</td>
</tr>
</tbody>
</table>

---

**Notes:**
- Brokers use substitute statement with columns.
- Form 1099-B is used for broker barter exchange transactions.
- Important fields include the description of property, date acquired, date sold, proceeds, and basis.

---

**Source:** Computershare

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*Page 30*
Cost-basis reporting for IRS tax returns

- Compensation income is not included in the basis reported on Form 1099-B for grants made starting 1/2014

- **Compensation income not recognized**: The cost-basis value is incomplete in just about every scenario

- **Need to know**: How will the broker report the cost basis of shares acquired between 2011 (when expanded 1099-B started) and the end of 2013?

- **Trend is standardization**: Not adding W-2 income to basis for option exercises, RSA/RSU vesting or ESPP purchases during this period

- Brokers provide supplemental information on basis and tax guides to help with tax-return reporting
2. Not reporting tax basis correctly

Cost-basis reporting is now more complex, confusing, and vulnerable to errors in over reporting the gain

Error by type of grant that leads to OVERPAYING TAXES:

- **Mistake with NQSOs, SARs, or ISO (DD)**: Using exercise price only
- **Mistake with ESPP**: Using purchase price only
- **Mistake with Restricted stock/RSUs and Performance shares**: Using purchase price of (usually $0).

<table>
<thead>
<tr>
<th>Grant type</th>
<th>Mistake with reporting basis</th>
</tr>
</thead>
<tbody>
<tr>
<td>NQSOs, SARs, ISOs (DD)</td>
<td>Exercise price only</td>
</tr>
<tr>
<td>ESPP</td>
<td>Purchase price only</td>
</tr>
<tr>
<td>Restricted Stock/RSUs</td>
<td>$0 as no purchase price</td>
</tr>
</tbody>
</table>
Risk of overpaying taxes

There are **only three disposition scenarios** in which the cost basis will not be understated:

1. qualifying dispositions of ISOs (all capital gain)
2. disqualifying dispositions of ISOs, with shares sold at a loss (all capital loss)
3. qualifying dispositions of ESPPs, with shares sold at a loss (all capital loss)

In other scenarios, the cost basis will be understated or omitted (i.e. the box will be blank). Unless participants and tax professionals are aware of this, taxpayers risk:

- overreport capital gains
- pay more taxes than they owe!
Amount of **ordinary income** recognized: reported on Form W-2 and part of basis

<table>
<thead>
<tr>
<th>Grant type</th>
<th>Income reported on W-2</th>
</tr>
</thead>
<tbody>
<tr>
<td>NQSOs</td>
<td>Spread at exercise</td>
</tr>
<tr>
<td>Restricted stock, RSUs, performance shares</td>
<td>Value at vesting and share delivery</td>
</tr>
<tr>
<td>Section 423 (qualified) ESPP</td>
<td>Depends on holding period</td>
</tr>
<tr>
<td>ISO in disqualifying disposition</td>
<td>Depends on the sales price relative to the market price at exercise</td>
</tr>
</tbody>
</table>
Cost-basis confusion: three situations

1. Stock purchases before 2011: **No cost basis reported to IRS.**

2. Securities not purchased with cash (restricted stock or RSUs): **No cost basis reported to IRS.**

3. Compensation part of cost basis for stock compensation: **Cannot be part of basis reported to IRS for stock acquired or granted starting 1/2014.**
What to do on Form 8949 if…

<table>
<thead>
<tr>
<th>The cost basis on Form 1099-B is too low</th>
<th>The cost-basis box on Form 1099-B is blank</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Basis from 1099-B in column (e)</td>
<td>1. Put correct basis in column (e)</td>
</tr>
<tr>
<td>2. Adjustment in column (g)</td>
<td>2. Check Box (B) or (E) near top</td>
</tr>
<tr>
<td>3. Code B in column (f)</td>
<td>3. No adjustments or codes in other columns needed</td>
</tr>
<tr>
<td>4. Check Box (A) or (D) near top</td>
<td></td>
</tr>
</tbody>
</table>
### Cost-basis example: restricted stock units

<table>
<thead>
<tr>
<th></th>
<th>Per share</th>
<th>Total (1000 shares)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Vesting date price</strong></td>
<td>$10</td>
<td>$10,000</td>
</tr>
<tr>
<td><strong>Compensation income reported on Form W-2</strong></td>
<td>$10</td>
<td>$10,000</td>
</tr>
<tr>
<td><strong>Purchase price</strong></td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td><strong>Cost basis</strong></td>
<td>$10</td>
<td>$10,000 (but $0 on the 1099-B)</td>
</tr>
<tr>
<td><strong>Sale price</strong></td>
<td>$15</td>
<td>$15,000</td>
</tr>
</tbody>
</table>
| **Taxable gain and capital gains tax** | $15 - $10 = $5 | $15,000 - $10,000 = $5000  
$5000 x 15% = $750  |
| **Capital Gain: Overpaying using wrong cost basis** | $15-$0 = $15 | $15,000 - $0= $15,000  
$15000 x 15% = $2250 |
Polling Question #3

What is the column on Form 8949 for cost basis?

a) 3
b) (e)
c) (g)
d) CB
Polling Question #3

What is the column on Form 8949 for cost basis?

a) 3

b) (e)

c) (g)

d) CB
### Form 8949: Sales and Other Dispositions of Capital Assets

#### Part I: Short-Term Transactions

**Note:** You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the total directly on Schedule D, line 1a; you are not required to report these transactions on Form 8949 (see instructions).

You must check Box A, B, or C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have more short-term transactions than will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

<table>
<thead>
<tr>
<th>Description of property (Example: 100 sh, XYZ Co.)</th>
<th>Date acquired (Mo., day, yr.)</th>
<th>Date sold or disposed (Mo., day, yr.)</th>
<th>Proceeds (sales price)</th>
<th>Cost or other basis</th>
<th>Adjustment, if any, to gain or loss.</th>
<th>Gain or (loss) from instructions</th>
<th>Amount of adjustment</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1000 Shares XYZ</strong></td>
<td></td>
<td></td>
<td>15,000</td>
<td>0</td>
<td></td>
<td></td>
<td>15,000</td>
</tr>
<tr>
<td><strong>1000 Shares XYZ</strong></td>
<td></td>
<td></td>
<td>15,000</td>
<td>10,000</td>
<td></td>
<td></td>
<td>5,000</td>
</tr>
</tbody>
</table>

Report the actual cost basis
Review: Reporting cost basis on Form 8949 depends on 1099-B

1. Basis just right

Put number from 1099-B in column (e)
2. Basis too low

- Put number from 1099-B in column (e)
- Adjustment amount in column (g)
- Code B in column (f)
Review: Reporting cost basis on Form 8949 depends on 1099-B

3. Basis blank

Put correct basis
In column (e), including W-2 income (columns (f) and (g) left blank)
2. Not reporting tax basis correctly: commission

- 1099-B does not subtract commissions or other fees from the proceeds (see what’s checked in Box 6).

- Do not add it to your cost basis on Form 8949

- **What to do:** adjustment on Form 8949 in column (g) and add Code E in column (f).

- **Starting with 2014 stock sales, less of an issue:** IRS requires reporting sales proceeds net of transaction fees after January 1, 2013.
3. Double-counting income from W-2 in Box 12 or 14

W-2 income in Box 1 already includes stock comp income, along with salary, wages. Put amount in Box 1 as part of income on line 1 of Form 1040 for “Salary, wages…”

**Mistake:** Using the amount in Box 12 (NQSOs) or Box 14 to report income on the line for "Other income" (line 8) of Schedule 1 (no longer on Form 1040 directly).

**Alert:** If you do this, you pay tax on income twice as ordinary income. Use Line 8 of Schedule 1 only when the company mistakenly omits stock comp income from W-2, no W-2c sent, and Form 4852 not used. Can happen for sales of ESPP stock in qualifying disposition.
### EXAMPLE: W-2: ESPP reporting for tax-qualified Section 423 ESPPs

<table>
<thead>
<tr>
<th>Field</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>22222</td>
<td>Employee’s social security number</td>
</tr>
<tr>
<td>Void</td>
<td></td>
</tr>
<tr>
<td>a</td>
<td>For Official Use Only</td>
</tr>
<tr>
<td>OMB No. 1545-006</td>
<td></td>
</tr>
<tr>
<td>b</td>
<td>Employer identification number (EIN)</td>
</tr>
<tr>
<td>c</td>
<td>Employer’s name, address, and ZIP code</td>
</tr>
<tr>
<td>d</td>
<td>Control number</td>
</tr>
<tr>
<td>e</td>
<td>Employee’s first name and initial, Last name, Suff.</td>
</tr>
<tr>
<td>f</td>
<td>Employee’s address and ZIP code</td>
</tr>
<tr>
<td>g</td>
<td>State, Employee’s state ID number</td>
</tr>
<tr>
<td>h</td>
<td>State wages, tips, etc.</td>
</tr>
<tr>
<td>i</td>
<td>State income tax</td>
</tr>
<tr>
<td>j</td>
<td>Local wages, tips, etc.</td>
</tr>
<tr>
<td>k</td>
<td>Local income tax</td>
</tr>
<tr>
<td>l</td>
<td>Local tax name</td>
</tr>
<tr>
<td>m</td>
<td>ESPP income included</td>
</tr>
<tr>
<td>n</td>
<td>ESPP income included if state/local tax applies</td>
</tr>
<tr>
<td>o</td>
<td>Note: with ESPPs, no income should be added to boxes for Social Security or Medicare, and no withholding should be included in any boxes (unless the company has voluntary withholding).</td>
</tr>
<tr>
<td>p</td>
<td>Note: Your company may voluntarily report the ESPP income in this box.</td>
</tr>
</tbody>
</table>

Form W-2: Wage and Tax Statement

Conv A For Social Security Administration — Send this.
Remind employees about what they need for tax-return reporting

<table>
<thead>
<tr>
<th>IRS Forms to gather</th>
<th>Additional Information &amp; Forms</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Form W-2</strong> if shares were sold at exercise/vesting/purchase</td>
<td>Exercise/vesting/purchase income reported on <strong>Form 1040</strong> if shares were acquired in a prior year. (Helps with cost-basis calculation.)</td>
</tr>
<tr>
<td><strong>Form 1099-B</strong> from broker or transfer agent</td>
<td><strong>Supplemental information</strong> (if any) provided by the broker to help with the cost basis.</td>
</tr>
<tr>
<td><strong>Form 3921</strong> for ISO exercises; <strong>Form 3922</strong> for ESPP purchases</td>
<td>Exercise, purchase, vesting, and/or trade <strong>confirmations</strong> from the company or the stock plan provider.</td>
</tr>
</tbody>
</table>

**Alert:** Understand how the basis is reported on the substitute statement and to the IRS (**not the same**). Taxpayer’s responsibility to make adjustments on Form 8949.
4. AMT calculation and credits

- For AMT purposes, always complete **IRS Form 6251 Line 2i (no longer line 14)** when ISOs are exercised & held through calendar year of exercise (not on W-2).

  - ISO stock is dual-basis stock. Your gain or loss for the AMT system and the regular-tax system will differ when sell.

  - For the year when you sell ISO stock, avoid paying or calculating more AMT than is required for your stock sale by reporting (as a negative amount) your adjusted gain or loss on Line 2k (no longer line 17) of **IRS Form 6251**.

- This negative adjustment can reduce the AMT and let you recover more of your AMT credit. The negative adjustment can't be greater than the capital gain for regular-tax purposes plus $3,000.
4. AMT calculation and credits

- AMT is no longer directly reported on Form 1040 from the calculation on Form 6251.
- The AMT, if owed, from the Form 6251 calculation now goes into Line 1 of Schedule 2 (change from last year when line 45)

<table>
<thead>
<tr>
<th>Part I</th>
<th>Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Alternative minimum tax. Attach Form 6251</td>
</tr>
<tr>
<td>2</td>
<td>Excess advance premium tax credit repayment. Attach Form 8962</td>
</tr>
<tr>
<td>3</td>
<td>Add lines 1 and 2. Enter here and include on Form 1040 or 1040-SR, line 12b</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Part II</th>
<th>Other Taxes</th>
</tr>
</thead>
<tbody>
<tr>
<td>4</td>
<td>Self-employment tax. Attach Schedule SE</td>
</tr>
<tr>
<td>5</td>
<td>Unreported social security and Medicare tax from Form: a □ 4137 b □ 8919</td>
</tr>
<tr>
<td>6</td>
<td>Additional tax on IRAs, other qualified retirement plans, and other tax-favored accounts. Attach Form 5329 if required</td>
</tr>
<tr>
<td>7a</td>
<td>Household employment taxes. Attach Schedule H</td>
</tr>
<tr>
<td>7b</td>
<td>Repayment of first-time homebuyer credit from Form 5405. Attach Form 5405 if required</td>
</tr>
<tr>
<td>8</td>
<td>Taxes from: a □ Form 8959 b □ Form 8960 c □ Instructions; enter code(s)</td>
</tr>
</tbody>
</table>

- Attach Form 6251 to Schedule 2. The totals from this schedule go into Line 12b of Form 1040 (change from last year when line 11)
4. AMT and credits

Once AMT has been triggered, you must complete Form 6251 every year, along with Form 8801 for the AMT credit.

It used to take years to benefit fully from the AMT credit if you are selling at a substantial loss. Changed in 2018 tax year with TCJA provisions.

Use of AMT credit: In year when you do not trigger AMT, use credit against regular income tax up to amount of what would be your AMT. Does not require you sell the ISO stock.

Example:

- Last year ISO exercise and hold triggered $14,000 of AMT
- This year, regular tax is $35,000, while AMT is only $30,000
- $5,000 of the $14,000 credit used, and carry forward $9,000 to future
- The amount from Line 25 of Form 8801 now goes into Schedule 3 ("Non-Refundable Credits") on Line 6 (check box b). Change from Line 54.
- Totals from Schedule 3 go onto Line 13b of Form 1040. Change from Line 12.
5. Sell-to-cover exercises

- Broker sells just enough shares from exercise to pay the exercise price, tax withholding, and the broker's transaction fees.

- Employee receives the remaining shares.

- For the year of sell-to-cover, **report on your Form 8949 only the number of shares sold and their tax basis.**

- Do not report the number and tax basis of all the options exercised that are part of W-2 income.
5. Sell-to-cover example: Exercise NQSOs for 2,000 shares on August 14

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exercise price</td>
<td>$10 per share ($35 stock price)</td>
</tr>
<tr>
<td>Exercise cost</td>
<td>$20,000</td>
</tr>
<tr>
<td>Tax withholding</td>
<td>$17,500 (combined 35% tax rate on $50,000)</td>
</tr>
<tr>
<td>Brokerage commission</td>
<td>$250</td>
</tr>
<tr>
<td>Total needed</td>
<td>$37,750</td>
</tr>
<tr>
<td>What is included on Form W-2</td>
<td>$50,000 income [($35 - $10) x 2,000]</td>
</tr>
<tr>
<td>Number of shares sold</td>
<td>1,079 (keep 921)</td>
</tr>
<tr>
<td>Form 8949 reporting</td>
<td>$37,515 ($37,765 - $250 commission)</td>
</tr>
<tr>
<td>Tax basis on sold shares</td>
<td>$37,765 (Schedule D includes a $250 short-term capital loss in Part I)</td>
</tr>
</tbody>
</table>

In the future, when you sell any or all of the net shares (921 shares net): report the **tax basis of $35 per share**.
6. Share withholding for restricted stock and RSUs

- **Definitely report a sale for taxes** at vesting if you received a 1099-B that reports the proceeds. Sell-to-Cover for taxes.

- When the shares directly withheld by your company (often called “net share withholding”), the situation is different.

- Report this "sale" back to company to cover the taxes if receive a 1099-B. Most companies do not issue these to employees.

- **Rumor:** IRS has informally approved this practice of not issuing 1099-Bs for share withholding.

- **Common Mistake:** Remember to exclude these tax shares when you calculate your capital gains on Form 8949 after you sell the remainder.

See the sections Restricted Stock: Taxes and Restricted Stock: Taxes Advanced at myStockOptions.com or in the Knowledge Center
6. Share withholding with restricted stock and RSUs: Potential for confusion

<table>
<thead>
<tr>
<th>Description</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>2,000 shares of restricted stock vest on Aug. 15</td>
<td>Vesting value: $20 per share ($40,000)</td>
</tr>
<tr>
<td>Shares surrender/ net-settled to pay taxes</td>
<td>625 (1,375 appear in account)</td>
</tr>
<tr>
<td>Amount your W-2 reports for the vested restricted stock</td>
<td>$40,000 (2,000 x $20)</td>
</tr>
<tr>
<td>Remaining 1,375 share sold the next year at $25 per share (after commissions)</td>
<td>$34,375</td>
</tr>
<tr>
<td>How you calculate capital gain</td>
<td>$34,375 proceeds – $27,500 cost basis (1,375 x $20)</td>
</tr>
<tr>
<td>Capital gain reported on Form 8949</td>
<td>= $6,875</td>
</tr>
</tbody>
</table>
7. Dividends with restricted stock/RSUs

- **Dividends paid:** compensation during vesting period or at vesting. Reported on W-2.

- **Exception:** Employee makes a Section 83(b) election (not available for RSUs). Eligible for the lower 15%/20% rate for qualified dividends. Reported on 1099-DIV.

- **Once the shares vest:** dividends are no longer compensation and instead become dividend income.

- Form 1040 line for dividend income: changed to 3a or 3b.
7. Dividends: Complications

- Pre-vesting dividends included on W-2 + Double-reported on Form 1099-DIV.

- Can occur if the company's transfer agent routinely issues dividend payments and 1099-DIV as it does to shareholders.

- The IRS recommends: list these dividends on Schedule B (“Interest and Ordinary Dividends”) of Form 1040. Subtract them from the total with a note that you have already included them in wages.

- See IRS Publication 550, “Investment Income and Expenses (Chapter 1),” for more details on reporting restricted stock dividends.
8. ESPP sales: Not reporting ordinary income

- Tax-qualified Section 423 ESPP: the purchase itself does not trigger tax-return reporting. The sale does.

- **At sale:** need to include the discount from the year of purchase as income

Review of Tax Rules for QD:

- With qualifying disposition: *Ordinary income in the year of sale* equal to: the lesser of either the actual gain upon sale or the purchase price discount at the beginning of the offering.

- The discount at the beginning of the offering **does not qualify** for capital gains treatment even if you hold stock for longer than one year.

- Beyond the discount, all additional gain is long-term capital gain.

*For details, examples, and videos see sections ESPPs: Taxes and ESPPs: Taxes Advanced at myStockOptions.com or in the Knowledge Center*
8. Not reporting ordinary income with ESPP sales

**Example:** 15% discount from the stock price on either first or last day of offering, whichever is lower.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Stock price on first day of offering</strong></td>
<td>$10</td>
</tr>
<tr>
<td><strong>Stock price on last day of offering (purchase date)</strong></td>
<td>$8</td>
</tr>
<tr>
<td><strong>Purchase price</strong></td>
<td>$6.80 (85% of $8)</td>
</tr>
<tr>
<td><strong>Net at sale after commission</strong></td>
<td>$18</td>
</tr>
<tr>
<td><strong>Income recognized at sale after meeting ESPP holding periods</strong></td>
<td>$1.50 per share in ordinary income (15% of $10)</td>
</tr>
<tr>
<td><strong>Cost basis</strong></td>
<td>$8.30 ($1.50 ordinary income + $6.80 purchase price)</td>
</tr>
<tr>
<td><strong>Long-term capital gain</strong></td>
<td>$9.70 per share ($18 minus cost basis of $8.30)</td>
</tr>
<tr>
<td><strong>What should be reported on Form W-2</strong></td>
<td>$1.50 multiplied by the number of shares purchased (if this is not reported, still report that amount on your tax return, using the line “Other income”). Using Form 3922: Box 3 minus Box 8.</td>
</tr>
</tbody>
</table>

If your sale gain is less than $1.50 per share (i.e. stock price of $8.30 per share or lower), just ordinary income for the amount of the actual gain. Sales below a stock price of $6.80 per share are all capital losses.
ESPP: Purchase/sell after holding short-term

Form 8949

Sales and Other Dispositions of Capital Assets

Before you check Box A, B, or C below, see whether you received a Form(s) 1099-B or substitute statement(s) from your broker. A substitute statement will have the same information as Form 1099-B. Either will show whether your basis (usually your cost) was reported to the IRS by your broker and may even tell you which box to check.

Part I

Short-Term. Transactions involving capital assets you held 1 year or less are short-term. For long-term transactions, see page 2.

Note: You may aggregate all short-term transactions reported on Form(s) 1099-B showing basis was reported to the IRS and for which no adjustments or codes are required. Enter the totals directly on Schedule D, line 1a; you aren’t required to report these transactions on Form 8949 (see instructions).

You must check Box A, B, or C below. Check only one box. If more than one box applies for your short-term transactions, complete a separate Form 8949, page 1, for each applicable box. If you have any short-term transactions that will fit on this page for one or more of the boxes, complete as many forms with the same box checked as you need.

1. Description of property
(Example: 100 shares of XYZ Co.)

2. Date acquired

3. Date sold or disposed of

4. Proceeds, before all sales
adjustments and tax

5. Cost or other basis

6. Net gain or loss

7. Code(s) from Form 8949 instructions

8. Adjustments, if any, to gain or loss

9. Gain or basis. Subtract column 8 from column 6 and combine the result with column 7.

**

Basis in Box 1a of Form 1099-B is correct

Column (e): Basis in Box 1a of 1099-B

Column (f): I leave blank

Column (g): I leave blank

Basis in Box 1a of Form 1099-B is too low or blank

If Box A is checked:

Column (e): Basis in Box 1a of 1099-B

Column (f): Code B

Column (g): Enter "5.0."

If Box B is checked:

Column (e): Correct basis of the sold shares (purchase price + income on W-2 for the spread at purchase).***

If the basis is blank or 0:

Column (f): I leave blank

Column (g): I leave blank

If the basis is incorrect:

Column (f): Code B

Column (g): Enter "5.0."

myStockOptions.com

Computershare
9. Netting of capital gain/loss

- Only same kinds of income net each other out.

- Only capital gains and losses net each other out on Schedule D. **Stock compensation income is not capital gains income.**

- Matching capital losses with gains is called “tax-loss harvesting.” Up to $3,000 (joint filers) in capital losses can be netted against ordinary income. Remainder carries forward.

**Example:** You sold company stock early last year at $9,000 short-term capital loss.

- You bought and sold this year at a short-term capital gain of $5,000.

- The loss carryforward and current year’s gain net each other out on your Schedule D, leaving you $4,000 of unused losses.

- $3,000 is used to offset against ordinary income on your current tax return.

- $1,000 is carried forward.

**Wash sale issues:** purchase company stock at gain within 30 days of sale at loss.

**Easy mistake to make in volatile or down markets.**

See my Forbes.com blog: Harvest Capital Losses: Beware Wash Sales!
9. Netting of capital gain/loss: Step after Schedule D

- **What's the same:** First report sale on Form 8949 and enter the totals from 8949 on Schedule D.
- **What's new:** Form 1040 again has a line labeled "Capital gain or (loss)."
- Schedule D total is now entered on the Form 1040 (Line 6) and not on Schedule 1
10. Extensions

- IRS **Form 4868**: automatic six-month extension for the due date of your tax return (until mid-October). No explanation or signature is needed to get the automatic extension.

- Federal tax deadline is likely to get extended beyond April 15, 2020 if suffered adverse effects from the spreading virus (status as of March 12, 2020 at 11:30 AM EST). States likely to follow.

- To avoid the failure-to-file penalty on what you owe, you must file the extension no later than the original deadline of your return (for details, see [IR-2006-58](#)).

- **Payment of the actual tax is not delayed** (just the period for filing the return). Pay 100% of anticipated tax when file the extension to avoid interest and penalties.

- Extensions do not delay estimated tax payments for the current tax year.

- Complications for US expatriates: avoid double taxation by using the foreign earned income exclusion ($105,900 in 2019) or a US tax credit for taxes paid in a foreign country.
12 Tax-Return Mistakes To Avoid With Stock Options And ESPPs

Bruce Brumberg and Lynnette Khalfani

Key Points
1. Stock options and employee stock purchase plans bring their own special issues to your tax return.
2. Common mistakes to avoid include double-counting income, misreporting the cost basis of stock sales, and miscalculating taxes on ESPP income.
3. Other common errors include massing up the AMT calculation, overpaying AMT, and forgetting to use capital-loss carry-forwards.

After reading this article, test your knowledge with a fun, interactive quiz on tax returns.

By the end of January, you should have received your IRS Form W-2, as usual. It will show any ordinary income stemming from stock options or employee stock purchase plans.

If you sold shares during 2019, before mid-February your brokerage will send you IRS Form 1099-B, which brokers usually reformat into their own substitute statement. Form 1099-B reports stock sales made during the year. In addition, you will also receive IRS Form 3921 if you purchased ESPP shares in 2019 and IRS Form 3921 if you exercised ISOs in 2019.

Puzzled by what to do with your W-2, Form 1099-B, or Forms 3921 and 3922? Don’t quite know how and where to report sales of company stock? Or, if someone wants to handle your tax return (taxpayers know some of the basics on stock). The Tax Center of myStockOptions.com can help with sales on tax returns.

What’s New For Tax-Year 2019: How to avoid tax pitfalls.

For a free copy of our article on tax-return mistakes to avoid, email editors@mystockoptions.com. Available to distribute to employees or clients.
NEW! Tax Returns Quiz

Take a few minutes to test your knowledge of the tax-return reporting for equity compensation. (Mistakes here are far less costly than errors on tax returns!)

Please answer the following 12 questions. This quiz is also a course of study. The answer key links to content on the topic for follow-up reading.

1. If you sold stock last year, which of the following IRS forms will you need for your tax return, along with any other information provided by your broker or your company?
   - Form 1099-B (or your broker’s equivalent substitute statement) and Form W-2
   - Form 3921 (if you sold shares acquired from incentive stock options)
   - Form 3922 (if you sold shares acquired from an employee stock purchase plan)
   - All of the above

2. Starting in 2018, what are the top tax rates on ordinary income and capital gains?
   - 35% and 20%
   - 35% and 15%
   - 37% and 20%
   - 39.6% and 15%

3. If you sold stock during the calendar year, which tax forms do you file with your IRS Form 1040 tax return to report the sale?
   - Form 1099-B and Schedule 1
   - Form 8949 and Schedule D
   - Form 6251 and Schedule 2
   - Form 8949, Schedule D, and Schedule 1

4. What is the cost basis of stock that has been sold?
   - Price paid to acquire shares + compensation recognized for acquiring them (reported on Form W-2)
   - Price paid to acquire shares + compensation recognized for acquiring them (reported on Form 1099-B)
   - Proceeds from stock sale + compensation recognized for acquiring shares (reported on Form W-2)
   - Proceeds from stock sale + amount paid to acquire shares (reported on Form 1099-B)

See home page and Tax Center for quiz on tax-return reporting. Courses for CE credit in Learning Center.
The video appears in the Tax Center
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The 2020 event offers all new sessions and a pre-conference bootcamp, plus more networking opportunities. Expert speaker topics include:

- Case studies and examples of successful financial-planning strategies
- Special sessions on financial planning for clients at pre-IPO companies
- Tax, estate, and SEC-related planning challenges
- Strategies for concentrated stock, option exercises, divorces, and more
- Methods for attracting and advising some types of high-net-worth clients

**June 15-16:** mystockoptions.com/conference