Freddi Eberhart & Associates Inc.
CERTIFIED PUBLIC ACCOUNTANTS

# Newsletter

JULY 2025

*Freddi Eberhart & Associates Inc. would like to thank you for selecting our firm for your tax and accounting needs. We appreciate the confidence you have shown in us, and we remain ready to assist you at any time. Also, thank you for recommending us to your family, friends, and associates. We truly appreciate your referrals.*

## This Month:

**Upcoming dates:**

**July 4**

- Independence Day

**July 27**

- Parents' Day

Our tax rules have always been a bit of a maze – complex, cryptic, and full of fine print. And yet, certain topics keeping popping up over and over again. In this month's newsletter, we provide answers to some of the most common tax questions.

Also read about how custodial accounts can be a great way to teach kids about saving and investing if you understand the trade-offs.

Please pass this information on to anyone that may find it useful and call if you have any questions or concerns.

## Common Tax Questions

### *What everyone is wondering*

Here are several of the most common tax questions and their answers. But like most things, there can be exceptions, so if in doubt always ask for help.

- **What happens to a loan if it's forgiven?** The IRS generally considers the canceled amount as taxable income, unless an exception applies. This means you may have to report the forgiven debt on your tax return and pay income taxes on it. Lenders typically issue a Form 1099-C for canceled debts, which you must include on your tax return.

- **Does my child need to report cash earned from a lemonade stand?** Yes, the cash your child earned for helping a neighbor is taxable. The IRS doesn't care if it came from mowing lawns, babysitting, or lemonade stands, earned income is earned income. Your child may not end up owing any income taxes, though, thanks to the single taxpayer standard deduction of $15,000 in 2025. But they'll still be on the hook for Social Security and Medicare taxes.

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# Common Tax Questions (Cont'd)

- **Are my rewards earned on a credit card taxable?** Taxation of any extras you earn with a credit card – including miles, discounts, even cash back – are not taxable if you had to pay to get them. Other rewards that you receive, for example a reward for signing up for a card or for referring a new cardholder, are considered taxable income per the IRS.

- **Does my employer contribution count towards the 401(k) limit?** Your employer's matching contributions do not count toward your maximum contribution limit, which for this year is $23,500. If you're 50 or older, you can sock away an additional $7,500 (for a total of $31,000) this year.

- **What happens to loans from my retirement account if I change jobs?** When you switch jobs, you must pay back any loans borrowed from your employer-sponsored retirement account within a short amount of time. If the loan isn't paid back, the outstanding balance is considered a distribution that is subject to income taxes and an early withdrawal penalty.

- **Do I really need to report gifts given to people?** Yes, but only if you give more than $19,000 ($38,000 if married) in 2025 to any one person. It must be reported to the IRS on a gift tax return. That's because the IRS keeps track of gifts you're allowed to make over the course of your lifetime, which in 2025 is $13,990,000 ($27,980,000 if married). Only after reaching this lifetime dollar amount will you need to actually make a gift tax payment.

- **Do I have to report a loss?** You may think the IRS isn't interested in losses you incur, such as when you sell a stock at a loss or if your business loses money. The reality is that you should always report losses on your tax return because you can use them to offset income under certain conditions. In addition, most losses can be carried forward to future years to offset income.

# Custodial Accounts for Kids: Understanding the Trade-offs of This Great Teaching Tool

Many parents rely on piggy banks and birthday cash to teach kids about money. But more are now turning to custodial accounts – a hands-on way for children to learn about saving and investing. While these accounts offer great learning opportunities, they also come with several trade-offs worth planning for.

### What you gain by using custodial accounts

Custodial accounts are managed by a parent or grandparent until a child turns 18 or 21 (depending on the state). There are two primary types of accounts:

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# Custodial Accounts for Kids: Understanding the Trade-offs of This Great Teaching Tool (Cont'd)

- UGMA (Uniform Gifts to Minors Act) - only basic assets are allowed, such as cash, stocks, bonds, mutual funds and ETFs

- UTMA (Uniform Transfers to Minors Act) - also allows other types of assets, such as real estate, art, and intellectual property

In addition to providing children a way to learn the basics of saving and investing, here are several other advantages of using custodial accounts:

- **Simple and accessible.** Easy to set up at most banks and brokerages.

- **Potential tax benefits.** A portion of your kids unearned income is taxed at the child's lower tax rate.

- **No contribution limits.** Custodial accounts don't cap how much you or your child can contribute to the account.

- **Flexibility.** The account's money can be used for anything that benefits your child, not just education.

While custodial accounts can be great for teaching kids about money, they do come with several trade-offs you'll need to consider.

## Trade-off #1 : The Kiddie Tax

Custodial accounts can trigger something called the kiddie tax. Here's how it works.

In 2025, the first $1,350 of your child's unearned income is tax-free. The next $1,350 is taxed at your child's tax rate (usually no more than 12%). Any unearned income above $2,700 ($1,350+ $1,350) is taxed at the parents' rate, which can be as high as 37%!

***What to do instead:*** *If your child has earned income, a Roth IRA for minors offers tax-free growth and avoids the kiddie tax entirely.*

## Trade-off #2: Impact on Financial Aid

Custodial accounts are counted as a child's asset on the Free Application for Federal Student Aid (FAFSA). Student assets are assessed at a much higher rate (20%) than parent assets (5.64%). This means that $10,000 in a custodial account can reduce financial aid eligibility by $2,000 or more.

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# Custodial Accounts for Kids: Understanding the Trade-offs of This Great Teaching Tool (Cont'd)

***What to do instead:*** *If you're saving for college, consider a 529 plan. The account owner retains control, the funds grow tax-free, and qualified withdrawals are tax-free as well. Plus, 529 plans are treated more favorably in financial aid calculations.*

### Trade-off #3: Loss of Control

Once the child comes of age, they can spend the money however they want. If your goal was to fund education but your 18-year-old wants to buy a motorcycle instead, you're out of luck.

***What to do instead:*** *Spread your child's earned income around multiple types of accounts. Put some in a 529 plan or other education account. Contribute another amount to a traditional or Roth IRA in the child's name. And make a deposit into a custodial account that your child can (eventually) do whatever they want with.*

### Bottom Line

Custodial accounts still have their place, especially for general-purpose savings or teaching financial responsibility. But it's important to understand the trade-offs and long-term implications.

# From Chaos to Covered: Your Family's Financial Emergency Blueprint

Building and reviewing an emergency plan can help your family know what to do in a crisis – especially if the next one is financial. Here's how to create your own family financial emergency plan, stress-test your budget, and build a great financial foundation.

**Step 1: Assess your current financial situation.** Start by gathering the following information:

- Income sources. Document all incoming money, including salaries, wages, side gigs, and passive income.
- Fixed expenses. These are expense you pay at consistent intervals, such as your rent or mortgage, utilities, insurance, or internet access.
- Variable expense. This includes items like groceries, gas, and entertainment.
- Discretionary spending. These are the nice-to-have but not necessary expenses such as shopping, hobbies, and certain subscriptions.

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## From Chaos to Covered: Your Family's Financial Emergency Blueprint (Cont'd)

**Step 2: Simulate a job loss or income cut.** Next, simulate a scenario where one or both income earners lose their jobs or face a significant pay cut. Ask the following questions:

- How long can you continue meeting essential expenses?
- What would be your first financial response? (cutting discretionary spending or using savings)
- What resources are available? (emergency fund, severance, unemployment benefits)

Now rebuild your budget assuming this new, lower income level. Prioritize essential categories such as housing, food, utilities, & healthcare. This exercise help you pinpoint which expenses can be eliminated or reduced.

**Step 3: Build an emergency fund.** Financial experts recommend saving 3 to 6 months' worth of living expenses. If this amount feels out of reach, aim for one month of essential expenses and build from there.

**Step 4: Identify candidates for cutbacks.** Pinpoint which expenses you could immediately pause or cancel in a crisis. Then develop a cutback plan in writing. This becomes your go-to response plan, allowing you to act quickly with no emotion or debate.

**Step 5: Create an income recovery strategy.** Increasing your income can speed up recovery. Brainstorm income replacement options in advance such as side hustles or freelance work; gig economy jobs like ride sharing, delivery, or tutoring; selling unused items online; accessing short-term assistance programs; tapping into a professional or industry network for job leads.

**Step 6: Practice communication and assign roles.** While creating your financial emergency plan, bring your family together and assign roles:

- Who handles bills and payments?
- Who checks into benefits and aid?
- How will you explain the situation to children in age-appropriate ways?

**Step 7: Review and repeat.** Your financial emergency plan isn't a one-time task. Schedule reviews every 6 to 12 months or after any major life event like a new job, having a baby, or moving.

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## From Chaos to Covered: Your Family's Financial Emergency Blueprint (Cont'd)

Creating a family financial emergency plan doesn't guarantee immunity from hardship. But it does provide clarity, direction, and peace of mind. It also ensures that when the unexpected happens, you're not starting from scratch.

As always, should you have any questions or concerns regarding your tax situation please feel free to call.

*This newsletter provides business, financial, and tax information to clients and friends of our firm. This general information should not be acted upon without first determining its application to your specific situation. For further details on any article, please contact us.*

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