Tax Consequences of Losing Your Job

Article Highlights:

- Severance Pay
- Unemployment Compensation
- Health Insurance
- Employer Pension Plan
- Job Search Expenses
- Moving Expenses
- Home Sale

If you have lost your job, there are a number of tax issues that you may encounter. How you deal with these issues can profoundly impact both your taxes and your finances. The following are typical issues along with their tax treatment:

Severance Pay – Your employer may provide you with severance pay. Severance pay and payment for unused vacation time will be included in your W-2 income, and both are fully taxable.

Unemployment Compensation – If you do not find another job right away, you generally will qualify for unemployment compensation. Unemployment benefits are taxable for federal purposes and may or may not be taxable by your state of residence.

Heath Insurance – When you lose your job and you had health insurance through your employer's group health coverage plan, you will need to determine your available options for continued coverage via COBRA or a replacement policy. If you give up coverage, you may be subject to Obamacare penalties for not being insured.

- *COBRA* Coverage - The Consolidated Omnibus Budget Reconciliation Act (COBRA) requires continuation coverage to be offered to covered employees, their spouses, former spouses, and dependent children when group health coverage would otherwise be lost. COBRA continuation coverage is often more expensive than the amount that active employees are required to pay for group health coverage because the employer usually pays part of the cost of employees' coverage, whereas 102% of the total cost can be charged to individuals receiving continuation coverage (the extra 2% covers administration costs). COBRA generally applies to private-sector employers with 20 or more employees and state or local governments that offer group health coverage to their employees. In most cases COBRA coverage is limited to 18 months.
- *Obamacare* – When existing health coverage is lost, a family may enroll in Obamacare through a government health insurance Marketplace outside of the normal enrollment window. In addition, depending upon your income for the year, you may qualify for the premium tax credit for the part of the year when you don't have coverage through your employer, which will help pay for the insurance.

Employer Pension Plan – Depending upon the provisions of your employer's pension plan, you may be able to leave your retirement funds in the employer's plan or have the option of moving the funds to your IRA account. You can have the funds transferred to your IRA or take a distribution and roll it into your IRA within 60 days. However, this is where a tax trap exists; for a distribution, the employer is required to withhold 20% for federal taxes, meaning only 80% of the funds will be available to roll over and the remaining 20% will end up being taxable unless you can make up the difference with other funds.

In the event you should ever want to roll those funds into a new employer's retirement plan, those retirement distributions should not be comingled with other IRA accounts.

Should you be tempted not to roll the funds over, be aware that the distribution will generally be taxable, and if you are under the age of 59.5 there will also be a 10% early withdrawal penalty.

Job Search Expenses – Expenses incurred while looking for a new job in your ***current occupation*** are deductible, even if a new job is not obtained. Examples of eligible expenses include:

- Fees you pay to employment and outplacement agencies and for career counseling.
- Resume preparation costs, such as typing, printing and mailing.
- Travel and transportation expenses if the trip is primarily to look for a new job. Even if the travel expenses to an area aren't deductible because job search wasn't your primary reason for the trip, the expenses looking for work in the area are allowed.

Moving Expenses – If you end up moving to obtain employment, you may qualify to deduct your moving costs, which generally include shipping, moving van, truck rentals, packing, insurance and in-transit storage. To qualify, the distance from your former home to your new work site must be at least 50 miles further than the distance from your old home to your old job, and you must work in the new location for 39 of the first 52 weeks in the new location.

Home Sale – If you relocate and have to sell your home and have owned and occupied the home as your primary residence for 2 of the previous 5 years, you will be able to exclude up to $250,000 of the gain ($500,000 if you are married and both you and your spouse qualify for the exclusion). If you do not meet the 2-out-of-5-years qualifications because you have lost your job, you will be allowed a prorated gain exclusion.

As you can see, there are a number of issues that may apply when a job loss occurs. To learn more about how these issues might affect your particular situation, please give this office a call.