

Tax consequences of unemployment insurance benefits



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American workers have suffered significant job losses as a result of the COVID-19 pandemic. Millions of these workers have filed for and received unemployment insurance benefits, including the additional payments from the federal government to supplement the standard state payments. These payments are taxable and can have a substantial impact on 2020 tax returns.

[This article from the IRS](#) details the tax consequences of these payments and the steps you can take to minimize their impact on your 2020 tax returns. Recipients of benefits have the *option* of withholding from each payment a flat 10% for federal tax and, in Kentucky, a flat 4% for state tax. Otherwise, no income taxes are withheld. Even if recipients are aware of and elect the withholding option, they may still have a balance due for the year.

We analyzed the impact in a hypothetical case of a single person, a Kentucky resident, whose compensation was an annual salary of \$80,000, but who was furloughed for six months after the first quarter of 2020. The person elected to have withholdings on the unemployment benefits at the standard rates.

For 2019, the person had tax refunds of \$1,354, but for 2020 would owe \$1,450 upon filing, a change of \$2,804. If the person did not elect to have withholdings on the unemployment benefits, \$7,610 would be the balance owed when filing 2020 tax returns, a change of \$8,964. Residents of states other than Kentucky should expect different results.

Planning should be done now to avoid what might be a very unpleasant surprise.