Shavano LIVING

July 2021

A publication exclusively for the residents of Shavano Park

Meet the **WOMACK FAMILY**

Taxes on *Collectibles*

Many valuable coins, stamps, artwork, cars, and other collectibles are considered alternate investments by the IRS. With the pandemic reportedly sparking new interest in memorabilia and the trading of collectibles going digital--some using online tokens as payment--it's time to brush up on what that means for your taxes.

What Happens When You Sell Collectibles? The IRS treats collectibles as capital assets. As long as you hold onto a collectible for more than a year, any income you make from selling the item will be considered a capital gain on a long-term investment. While most net capital gain taxes are set at 15-20% depending on your taxable income, collectibles are different. They're taxed as an alternative investment at a maximum 28% rate.

You may also be able to acquire collectibles through a self-directed retirement account, including certain IRAs. But when doing so, you'll be taxed on the purchase instead of the sale, as the IRS deems it a distribution of cash and then a purchase of the collectible. Therefore, you must declare the cost of the collectible to the IRS and pay a tax that usually amounts to ordinary income (with 10% additional tax on early withdrawals if you're under the age of 59½). Certain metals and coins are excluded from the rule and any distributions you take after that initial tax bill will be tax-free up to the initial tax amount you paid.

What's Considered a Collectible? The IRS defines collectibles as works of art, rugs or antiques, alcoholic beverages, most metals or gems, rare stamps, and some coins. But the IRS also reserves the right to deem any tangible personal property it sees fit as a collectible. That means a restored car, baseball cards, or any number of assets that are commonly collected could be taxed at that higher alternative investment rate when sold.

What if you sell the collectible at a loss? You may also be able to take a tax loss, but you can expect the IRS to scrutinize your claim. It matters whether you, as the taxpayer, held the collectible for investment purposes versus entertainment or personal use (which wouldn't earn you a tax break). It could become as granular as considering your behavior. In the case of artwork, for instance, did you purchase and store the art until it appreciated, or did you display the art in your home?

Recent Developments | Have you heard of non-fungible tokens (NFTs)? These digital assets are typically bought and sold online with cryptocurrency. They include digital art, gifs, videos (including sports highlights), music, and tweets. They can also include digital assets that represent tangible collectibles like designer shoes.

Before you roll your eyes, you should know that NFTs are becoming highly valuable. A 2011-era cat GIF recently sold for $600,000 while a single highlight video clip of LeBron James sold for $200,000. The IRS hasn't yet offered guidance on the tax implications of NFTs, but you can assume they'll be subject to the alternative investment tax (and, of course, the even higher short-term capital gains taxes if you sell an NFT less than one year after acquiring it).

What about inherited collectibles? Generally, these assets benefit from a step-up in basis, meaning that their taxable value is reset at the time it's passed down instead of being calculated from its original price (which could have been set decades ago). But the Biden administration may change that, at least for high-value collectibles.

Certain tax vehicles can help protect your precious valuables from unnecessary taxes, but the rules can be as unique as the collectible itself. It's best to understand what you're getting into before the IRS jumps to conclusions for you.

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