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Top Ten Tax Tips in a Time of Tax Uncertainty

Tips for Businesses and Individuals

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HOUSEKEEPING

Attendees may submit questions at any time using the Q&A function. Panelists may address questions at the end of the formal presentation if time permits.

Additionally, all attendees will be emailed a link to a recording of the webinar, a pdf of the presentation, and a listing of speaker biographies and contact information.

Today's presentation is not:

- Legal advice
- The final word on today's topics – updates will be continuously provided via herbein.com

Before taking any action, you should review this material with internal and/or external advisors.

CPE HOUSEKEEPING (1 HOUR)

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To be eligible for Continuing Professional Education (CPE) for certified public accountants, participants:

- Must be logged in for the entirety of the program.
- Answer at least 3 questions during the hour.

Unfortunately, we are unable to grant CPE in cases where technical difficulties prevent the participants to meet the requirements listed above. A certificate will be sent to all who meet the CPE requirements.

POLL QUESTION #1

How optimistic are you regarding your tax situation in 2021 compared to 2020?

- Feeling good!
- Feeling neutral
- Feeling negative!
- Not sure

Section One

Individual Tax Tips

Stacy A. Weller, CPA

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Historically ***low*** tax rates

Marginal Tax Rates	Married Filing Jointly	Single
10%	$0 - $19,750	$0 - $9,875
12%	$19,751 - $80,250	$9,876 - $40,125
22%	$80,251 - $171,050	$40,126 - $85,525
24%	$171,051 - $326,600	$85,526 - $163,300
32%	$326,601 - $414,700	$163,301 - $207,350
35%	$414,701 - $622,050	$207,351 - $518,400
37% *	Over $622,050	Over $518,400

* The top rate is effectively 40.8% for those individuals subject to the 3.8% Medicare surtax on net investment income

Top Tips for Individuals

- Charitable Donations: Various approaches to save taxes
- Health Savings Accounts
- Tax Efficient Loss Harvesting
- Roth IRA Conversions
- Estate Exemption and Lifetime Gifting Limits

Qualified Charitable Distributions (QCDs):

- QCD is a direct transfer of IRA funds to a qualifying charity.
- Most efficient way to make charitable donations.
- Reduce taxable IRA balances at zero tax cost for individuals over age 70 ½ before year end.
- Charity receives full distribution. Taxpayer does not have to claim any taxable income for the distribution.
- Note: Even though the Secure Act raised the required minimum distribution age from 70 ½ to 72, QCDs are still available at age 70 ½.

Health Savings Accounts (HSA)

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- Triple Tax Benefit
    - Tax deduction for contribution into HSA
    - Deferral of gain on the growth in the account
    - Money comes out tax free if used for qualified medical expenses

- Annual Contribution Limits
    - Single $3,550, Family $7,100
    - Catch up contribution amount $1,000 if 55 or older
    - For 2021 – Single $3,600, Family $7,200

Important: To be eligible, you must be enrolled in a High-Deductible Health Plan (HDHP)

For calendar year 2021, the amounts for HDHPs are:

	Minimum Deductible (The amount you can pay for health care items and services before your plan starts to pay)	Maximum out-of-pocket costs (The most you'd have to pay if you need more health care items and services)
Individual HDHP	$1,400	$7,000
Family HDHP	$2,800	$14,000

Health Savings Accounts (HSA)

Additional considerations:

- HSA balance rolls over from year to year so you can build up the account:
    - Many view as an additional retirement asset
    - Optimal savings mechanism for retirement
- Once you turn 65 you can use the money any way you want, if you don't use it for qualified medical expenses it is just taxed as ordinary income at your current tax rate – no penalties.
- Once you are participating in Medicare, you are no longer eligible to participate in an HSA because Medicare is not considered a HDHP.
    - Can use the HSA funds to pay your Medicare premiums
- If you are eligible and set up the HSA in December, you can fund for the entire year!

Charitable Donations

Simple strategy: Bunching of charity to itemize every other year and take advantage of increased standard deduction every other year.

- Standard deduction - Single $12,400/Married Filing Jointly $24,800

2020 – above the line $300 deduction for charity (if you do not itemize)

2020 – No Adjusted Gross Income (AGI) limitation on cash charity

Tax Efficient Loss Harvesting

Total $3,000 capital loss can be realized against other sources of income annually. Excess losses carry forward.

	Short-Term Gain	Long-Term Gain
Short-Term Loss	Neutral	Ineffective
Long-Term Loss	Effective	Neutral

*If you believe tax rates are going up – perhaps now is the time to trigger capital gains in 2020 rather than in 2021 or later

Poll Question #2

Roth IRAs are a popular retirement vehicle – which statement describes your experience with a Roth IRA?

- Have one, very satisfied
- Have one, neutral
- Have one, not very satisfied
- Considering conversion of a current plan
- Considering a new Roth IRA
- Not sure

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What is a Roth IRA Conversion?

- An amount is taken from a traditional IRA or 401(k) account.
- The taxpayer pays income tax on the distribution.
- The amount is moved into a Roth IRA.
- Monies grow tax free in Roth IRA.
- Can be beneficial for taxpayers with very large taxable retirement account benefits, who expect their future tax bills to grow by the time they retire.

ROTH IRA CONVERSIONS

The Benefits of Converting Now

- Roth IRAs grow tax-free forever
- No lifetime Required Minimum Distributions (RMDs)
- Once converted, today's low rates are locked in
- Current and future taxes are lower due to
  - Lower tax-deferred balances, resulting in
  - Lower RMDs
- For purposes of the NIIT, Roth IRA distributions are not included in NII or MAGI

Roth IRA Conversions

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- To count as a 2020 Roth conversion, the funds must leave the IRA or company plan by December 31, 2020.
- Reasons to consider a Roth IRA conversion:
    - Lower tax brackets now than in retirement years
    - Historically low tax rates
    - Tactical considerations
        - Current year ordinary losses, included Passive Activity Losses (PALS) after a disposition
        - Net Operating Loss (NOL) carryovers from prior years
        - Alternative Minimum Tax (AMT)
        - Credit carryovers
- Roth IRA conversions are permanent; be sure there are enough funds to pay the taxes before doing the conversion.

ROTH IRA CONVERSIONS

The CARES Act waived Required Minimum Distributions (RMDs) for 2020.

- Generally, RMDs cannot be converted to a Roth IRA.
- Due to waiver of RMDs for 2020, this is a one-time opportunity.
- Once RMDs begin, taxable income will be higher, making a conversion more expensive.

HOW DOES THE ELECTION IMPACT ESTATE PLANNING?

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Estate Exclusion and Lifetime Gifting Exemption:

- Tax year 2020 exemption is : $11,580,000 per person
- Tax year 2021 exemption is : $11,700,000 per person

With no legislative action set to sunset in 2025, 2026 will revert to $5 million indexed for inflation.

Step-up in basis to fair market value at date of death.

LIFETIME GIFTING

Three tiers of tax-exempt gifting:

- Annual exclusion gifts (Up to $15,000 per recipient/per year)
- Gifts for direct payments for tuition and medical expenses (unlimited)
- Lifetime gift/estate exemption for 2020 ($11,580,000 per person / $23,160,000 per married couple
    - Sunsets December 2025, or sooner
    - Gifts made now lock in today's gifting limits, as opposed to inheritances received after death

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Why now?

If gift tax exclusion amounts change, one may find oneself in a position that they cannot gift away fast enough later to avoid an estate tax.

There needs to be a sense of urgency to take steps not to make gifting decisions as quickly as possible, perhaps even before year end.

Various wealth transfer strategies - Extremely low interest rates.

COVID-19 has possibly negatively affected business valuations:

> Lower values allow business owners to transfer a greater portion of their business assets and reduce taxable estate.

Poll Question #3

Of the individual strategies discussed, which are you most likely to implement?

- Charitable Donations – Various approaches to save taxes
- Health Savings Accounts
- Tax Efficient Loss Harvesting
- Roth IRA Conversions
- Estate Exemption and Lifetime Gifting Limits
- Not sure

Section Two

Business Tax Provisions

Michael J. Hermes, CPA

Bonus Depreciation

- Applies to most new and used property
  - Must be tangible personal property
- Must be purchased and placed in service in 2020
- Deduction not prorated based on the date the asset was placed in service
- Bonus depreciation and vehicle limitations
  - Heavy vehicles—rated at more than 6,000 pounds gross vehicle weight—are exempt from the luxury-auto limitation

ADDITIONAL INFO

We will post the following as soon as it is available on our website:

2019 Year End Tax Planning Guide

2019 Automobile Letter

2019 S Corporation Letter

2020 Payroll Rate Sheet

2019-2020 Payroll Letter

Qualified Improvement Property

- The CARES Act fixed a technical problem with QIP and bonus depreciation
- Taxpayers can fully deduct qualified improvements dating back to January 1, 2018
- What happens if you've already filed 2018 and 2019 returns?
    - May file Form 3115 – Change in Accounting Method
        - Accelerate deduction to be taken in 2020
    - May amend tax returns for each year

Section 179 Expense

- Maximum dollar limitation for 2020 = $1,040,000
- Phaseout amount = $2,590,000.
  - Limits will be adjusted for inflation in 2021.
- TCJA expanded the definition of section 179 property to include qualified improvements to nonresidential real property
  - Certain improvements to a building’s interior
  - Roofs
  - HVACs
  - Fire protection systems
  - Alarm systems
  - Security systems.

Business Interest Expense Limitation

- Net business interest expense is limited to 50% of adjusted gross taxable income for 2020
    - Reverts to 30% of adjusted gross taxable income for 2021.
- Small taxpayer exception
    - $26 Million in average aggregate gross receipts for 2020
- Real estate and farming trades or businesses
    - May revoke election to utilize ADS to avoid Section 163(j) limitation
- May utilize 2019 adjusted taxable income to calculate interest expense deduction limitation

POLL QUESTION #4

Which best describes your company's current retirement plan?

- Satisfied with current plan
- Dissatisfied with current plan
- Considering the implementation of a plan
- Not sure

Qualified Business Income Deduction

- Deduction equal to 20% of qualified business income
  - Subject to wage and qualified property cost limitations.
- Specified service trades or businesses should consider the following to reduce taxable income below the limitation threshold:
  - Pension plan contributions
  - Bonuses
  - Accelerate expenses
  - Recognizing losses
  - Defer recognizing gains
- Non-specified service trade or business – consider additional wages and capital purchases to raise limitations.

Minimum Tax Credit Refunds

- TCJA repealed the corporate AMT
- Corporations were able claim all their unused AMT credits in the tax years beginning in 2018, 2019, 2020 and 2021
- CARES Act accelerates this timeline,
    - Allowing corporations to claim all remaining credits in either 2018 or 2019

NOL CARRYBACKS

- The CARES Act allowed for businesses and individuals to carry back NOLs
- NOLs arising in tax years beginning in 2018, 2019, and 2020 can be carried back five years
    - Quickest way to obtain a refund is generally by filing a tentative refund claim
    - Must be filed by December 31, 2020 for the 2019 calendar year
    - Tax return must be filed before a tentative refund claim can be filed

Ensure Adequate Stock and Debt Basis in S Corporations and Partnerships

- Make sure you have adequate basis to accelerate deductions or increase losses
  - Stock basis
  - Debt basis
- Good to start calculating before year-end to avoid basis issues during filing season

Automatic Change in Accounting Methods

- Can be made by the due date of the tax return, including extensions
- Some common changes in accounting methods include:
  - Change from accrual to cash method of accounting
  - Changing the treatment of prepaid expenses
  - Changing the treatment of advanced payments received
  - Reviewing the class lives used for depreciation
    - Chance to correct depreciable lives of fixed assets possibly resulting in larger deductions due to shortened tax lives
  - Electing out of or reviewing the application of the uniform capitalization rules on inventory (263A)
    - May be over-capitalizing expenses
    - Current circumstances may have material change to calculation

Disaster Loss Refunds

- Businesses may claim certain losses attributable to a disaster on a prior year tax return
- President Trump's COVID-19 disaster declaration designated all 50 states, the District of Columbia and five territories as disaster areas
  - Many U.S. business are generally in the covered disaster area
  - May be eligible for refunds from certain types of losses
- Potential to claim a COVID-19 related disaster loss occurring in 2020 on a 2019 amended return for a quicker refund
- This provision may affect specific losses arising certain circumstances, including the loss of inventory or supplies, or the closure of offices, stores or plants
  - To qualify, the loss must be attributable to or caused by COVID-19 and satisfy several other requirements

Expiring Tax Provisions

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- Several tax provisions are set to expire at the end of 2020
- The Work Opportunity Tax Credit – for businesses that are rehiring
    - As businesses start getting back to "normal," they will start to hire more employees
    - If they hire from a targeted group, they may get this tax credit
- One targeted group is the long-term unemployment recipient – those unemployed for not less than 27 consecutive weeks at the time of hiring
    - Other targeted groups also qualify

Review Retirement Plans

- Business owners who do not have a retirement already set up should consider implementing a plan
- For self-employed individuals, a Keogh plan must be set up before the end of the year
- Self-employed individuals may establish a simplified employee pension (SEP) plan up to the extended due date of their income tax return
- Self-employed individuals may make contributions to either plan up to the filing date of a timely filed income tax return

Policy Predictions and Planning:

- Tax rates expected to rise, regardless of party in power
    - Could give rise to tax planning that runs contrary to conventional tax planning
- Some basic strategies and concepts to consider in the face of predicted rising tax rates:
    - Accelerating income and delaying expenses
        - Terminate installment sales/change to full inclusion method of accounting
    - Elective capitalization – prepaids (like insurance)
    - Elect out of bonus depreciation, forgo Section 179 depreciation
    - Defer bonuses until after 3/15
    - Close M&A transactions prior to 12/31
    - Distribute E&P – Pay tax on dividends at current cap gains rates
    - Exit C-Corp structure
- Compensation and benefits planning
    - Can provide tax-free reimbursement to aid employees to more effectively work remotely.
    - Potential for equity incentive plans – lower valuations and low rates

SECTION Three

PPP Tax Issues

David E. Peritz

POLL QUESTION #5

This is not a trick question!

Do you expect PPP loan forgiveness will trigger a taxable event for your company?

- Yes
- No
- Not sure

Tax Treatment of PPP Loans

- Forgiveness does NOT trigger cancellation of indebtedness income for tax purposes
- CARES Act Section 1106(i):
  - TAXABILITY – For purposes of the Internal Revenue Code of 1986, any amount which (but for the subsection) would be includible in gross income of the eligible recipient by reason of forgiveness described in subsection (b) shall be excluded from gross income
  - If recorded for book purposes, reverse for tax purposes
- While the CARES Act excludes the loan forgiveness from gross income, it does not specifically address whether the expenses used to achieve the loan forgiveness would continue to be deductible.

Tax Treatment

Underlying expenses that create the forgiveness

- Expenses made during a prescribed period for:
  - Payroll
  - Employee benefits related to healthcare
  - Mortgage interest
  - Rent
  - Utilities
  - Interest on any other existing debt obligations

These expenses are incurred before receiving actual forgiveness of the PPP loan.

IRS Notice 2020-32

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- On April 30, 2020, the IRS issued Notice 2020-32 to provide guidance regarding the deductibility for federal income tax purposes of certain otherwise deductible expenses incurred in a taxpayer's trade or business that the taxpayer uses to support loan forgiveness.
- The notice states that no deduction is allowed under the Internal Revenue Code for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a PPP loan.
- The notice cites Sec. 265 as the specific disallowance provision.

IRS issues Revenue Ruling 2020-27

- On Nov. 18, 2020, the IRS issued Rev. Rul. 2020-27, clarifying the tax year for which the deduction would be disallowed.
- Rev. Rul. 2020-27 holds that a taxpayer computing taxable income on the basis of a calendar year may not deduct eligible expenses in its 2020 tax year if, at the end of the tax year, the taxpayer has a reasonable expectation of reimbursement in the form of loan forgiveness on the basis of eligible expenses paid or incurred during the covered period.

Revenue Procedure 2020-51

- Rev. Proc. 2020-51, providing a safe harbor for taxpayers who did not claim deductions for expenses intended to be used for loan forgiveness but whose loan is not forgiven.

- Rev. Proc. 2020-51 provides a safe harbor for taxpayers who paid these expenses, not claiming a deduction for such amounts, and in a subsequent year is informed that forgiveness of all or part of the loan is denied or decides not to apply for forgiveness. The safe harbor allows the borrower to deduct these expenses on an original or amended tax return for 2020 or a subsequent tax year and requires a specific statement to be attached to the income tax return on which the expenses are deducted.

Will Congress act to allow a deduction for PPP expenses?

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- In May 2020, Senate Bill 3612 was introduced to reverse the IRS's conclusion reflected in Notice 2020-32.
- Many expected that the Payroll Protection Program Flexibility Act of 2020 which became law on June 5, 2020, would adopt the provisions contained in Senate Bill 3612. Unfortunately, that did not happen.
- There were advocacy letters written in 2020 by the AICPA as follows:
  - May 28 letter to Representative Lizzie Fletcher
  - July 20 letter to Nancy Pelosi and Mitch McConnell (Recommendations for Phase Four Federal Legislation)
  - August 4 letter to Nancy Pelosi and Mitch McConnell
- There is also bipartisan support for the position concluding that it was not Congressional intent to disallow the expenses. However, IRS Notice 2020-32 is still the only authoritative guidance available as of the date of this memo.

Status of COVID Relief bill?

Bipartisan COVID relief plan includes more PPP, plus tax deductions for small businesses???

Key Points to the COVID Relief Bill:

- Lawmakers on both sides of the aisle proposed a $908 billion emergency COVID relief package. Of this, $300 billion would be earmarked for the Small Business Administration, the agency overseeing the Paycheck Protection Program.
- Small businesses with up to 300 employees and that have sustained a 30% revenue loss in any quarter of 2020 would be eligible for a second round of PPP funding.
- Business expenses paid for with PPP funding would be tax deductible, according to a summary of the proposal.

POLL QUESTION #6

Do you have any questions that would require a follow-up consultation with either or our speakers?

- Yes – Individual Issues
- Yes – Business Issues
- Yes – PPP Forgiveness Issues
- Not at this time

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Q&A