Recent Tax Law Changes and Tax Planning Opportunities

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CARES Act

- Coronavirus Aid, Relief, and Economic Security (CARES) Act gave most Americans a stimulus check in 2020 for $1,200 ($2,400 for couples filing jointly), plus $500 more for each child under age 17.
- The payments were phased out for joint filers with adjusted gross incomes above $150,000, head-of-household filers with AGIs above $112,500, and single filers with AGIs above $75,000.
- Treated as an advance payment on a special 2020 credit.

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CARES Act

- Qualified Improvement Property – A huge benefit and fix to the 2017 TCJA glitch
- Improvements or renovations to an existing building (interior and non-structural) are **15-year property and eligible for 100% bonus depreciation (39 year depreciation to immediate write-off)**
- Not applicable to enlargements, elevators and escalators, internal structural framework, and residential property
- Effective January 1, 2018. 100% bonus available through December 31, 2022

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SECURE Act/CARES Act

- Major changes to retirement plans
- Beginning age for Required Minimum Distributions (RMDs) increased from 70 ½ to 72. You can skip the RMD in 2020.
- Now allowed to make traditional IRA contributions after age 70 ½
- Fellowships and grad student stipends are treated as compensation for IRA purposes

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SECURE Act/CARES Act

- Withdrawal rules tightened for inherited IRAs
- Surviving spouses can still take it over their remaining life expectancies
- 10% early withdrawal (pre age 59 ½) penalty waived for up to 100K of COVID related payouts, 3-year spread & optional repayment

Itemized Deductions

- No AGI limitation for cash contributions in 2020 and 2021
- Nonitemizers can deduct up to $300 cash charitable contributions per return. The CAA extends (expands MFJ to 600) through 2021.
- Mortgage Insurance Premiums treated as qualified residence interest extended through 2021

Estate and Gift Tax Planning

- Lifetime estate and gift tax exemption 11.7 Million per individual and 23.4 Million per couple
- 40% Estate tax rate
- Biden has proposed restoring the 2009 levels of 3.5 Million, 1 Million gift, 45% estate tax rate
- 15,000 annual gift tax exclusion per done
- 529 plans can now pay for fees, books, supplies and up to 10K can be used to pay off student debt

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Various

- HSAs and FSAs can be used to buy over-the-counter medicines without the need of a doctor's prescription, as well as menstrual care products.
- 20% QBI deduction for SE and pass-through income is subject to limitations at 326,600 for MFJ and 163,300 for singles
- The cap on business losses at 500,000 MFJ or 250,000 for singles was suspended

Consolidated Appropriations Act 2021

- Extended many of the CARES Act provisions through 2021
- **Discharge of personal residence forgiveness as nontaxable income** extended until 12/31/2025
- The $300 **charitable deduction for non-itemizers** in 2020 is increased to $600 for joint filers in 2021.
- The **100% of Adjusted Gross Income limitation for cash contributions** to public charities is extended through December 31, 2021.
- **Limitations of charitable contributions by corporations** to 10% was **increased to 25%** by the Cares Act through 2020. The Act extends this through 2021. In addition, contributions of food inventory normally limited to 15% of income and increased by the Cares Act to 25% through 2020 is extended through 2021.

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Consolidated Appropriations Act

- **Medical Expenses** - The 10% floor on medical deductions set to take effect in 2021 will permanently remain at 7.5%
- **Student Loans** - The provision allowing employers to pay for employee's student loans up to $5,250 per year with such amounts being excluded from the employee's taxable income has been extended to December 31, 2025.
- **Educator Expenses** - The $250 above the line deduction for unreimbursed teacher expenses is expanded to include PPE expense (masks, disinfectant and other supplies to prevent the spread of COVID-19).
- Individuals can **rollover unused benefits** in their FSA and Dependent Care accounts from 2020 to 2021 and 2021 to 2022.

PPP Loans

- Forgiven PPP loans remain **nontaxable**.
- Congress specifically overrode the IRS position that expenses attributable to the forgiveness were not deductible. As such, **expenses utilized to qualify for forgiveness will now be deductible**.
- The Act also authorizes additional permissible nonpayroll costs to qualify for forgiveness, including costs related to personal protective equipment (PPE).
- **New round** of PPP-2 loans. May be eligible even if your already received PPP loan in the first round.

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Business Meals

100% Deduction for business meals from a restaurant

- The usual 50% limitation on business meals is suspended from January 1, 2021 until December 31, 2022 as long as the food and beverages are provided by a restaurant.

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AZ Prop 208

- Additional tax of 3.5% on income over 250K single and 500K MFJ
- Legality is being challenged in court
- Department of Revenue wants to quash the effort and begin collecting the tax

Biden Tax Proposals

Razor thin democratic majority in the Senate:

a. Don't expect tax changes right away –too many other important matters

b. Won't get everything he asks for

1. Tax the wealthy more heavily - Higher maximum tax rate

- The pre-election Biden tax plan would raise the top individual federal income rate on ordinary income and net short-term capital gains back to **39.6%**, the top rate that was in effect before the Tax Cuts and Jobs Act (TCJA) lowered it to 37% for 2018-2025.
- Biden also said he would **generally raise taxes on folks with incomes above $400,000** without supplying specifics.
- Phase out the 20% QBI deduction for upper income taxpayers

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Biden Tax Proposals

- **2. Itemized deductions**
- **Limit the tax benefit of itemized deductions to 28%** for upper-income individuals. In other words, each dollar of allowable itemized deductions could not lower your federal income tax bill by more than 28 cents, even if you are in the proposed 39.6% maximum tax bracket.
- Reinstate the pre-TCJA rule that reduces total allowable **itemized deductions** above the applicable income threshold. Allowable deductions are **reduced by 3 cents for every dollar of income above the threshold**.
- Biden would **eliminate the TCJA's $10,000 cap on itemized deductions for state and local taxes.**

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Biden Tax Proposals

3. Higher maximum rate on long-term capital gains

- Upper-income individuals would face higher capital gains taxes. Under current law, the maximum effective federal income tax rate on net long-term capital gains and qualified dividends recognized by individual taxpayers is 23.8%.

- Under the Biden plan, net long-term gains (and presumably dividends) collected by **those with incomes above $1 million would be taxed at the same 39.6% maximum rate** that is proposed for ordinary income and net short-term capital gains.

- With the 3.8% NIIT add-on, the maximum effective rate on net long-term gains would hit 43.4% (39.6% plus 3.8%). That would be **almost double** the current maximum effective rate of "only" 23.8%.

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Biden Tax Proposals

4. Higher Social Security taxes for upper-income individuals

- Current law: the 12.4% Social Security tax hits the first $137,700 of 2020 wages or net self-employment income. Employees pay 6.2% via withholding from paychecks, and employers pay the remaining 6.2%. Self-employed individuals pay the entire 12.4% out of their own pockets via the self-employment (SE) tax. For 2020, the 12.4% Social Security tax cuts out once 2020 wages or net SE income exceed the $137,700 ceiling. This FICA base is adjusted annually for inflation.

- The FICA base or ceiling for 2021 is $142,800.

- The Biden tax plan would restart the 12.4% Social Security tax on wages and net SE income above $400,000. This is the so-called *donut hole approach* to increasing the Social Security tax. Over the years, the donut hole would gradually close as the lower edge of the hole is adjusted upward for inflation while the $400,000 upper edge of the hole remains static.

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Biden Tax Proposals

5. Elimination of basis step-up for inherited assets

- Under current law, the federal income tax basis of an inherited capital-gain asset is stepped up (or down) to fair market value as of the decedent's date of death. So, if heirs sell inherited capital-gain assets, they only owe federal capital gains tax on the post-death appreciation, if any. This provision can be a huge tax-saver for greatly-appreciated inherited assets — such as personal residences that were acquired many years ago for next to nothing and are now worth millions.

- Restore the 2009 levels of 3.5 Million lifetime exemption, 1 Million gift, 45% estate tax rate

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Biden Tax Proposals

6. Elimination of real-estate tax breaks

- Eliminate the $25,000 exemption from the passive loss rules for rental real estate losses incurred by middle-income individuals

- Eliminate Section 1031 like-kind exchanges that allow deferral of capital gains taxes on swaps of appreciated real property

- Eliminate rules that allow faster depreciation write-offs for certain real property

- Eliminate qualified business income (QBI) deductions for profitable rental real estate activities

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Biden Tax Proposals

7. Increased child- and dependent-care credits

- The Biden tax plan would increase the maximum refundable child credit to $4,000 for one qualifying child or $8,000 for two or more qualifying children. Families making between $125,000 and $400,000 would receive reduced credits.

- Apparently, the same rules would apply to an enhanced credit for expenses to care for qualifying dependents.

- Biden would also establish a new credit of up to $5,000 for informal caregivers.

- Expand the child and dependent care credit to 8,000 per child (16,000 max)

- Forgive student loan debt and make it nontaxable

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Biden Tax Proposals

8. New credits for homebuyers and renters

- Create a new refundable tax credit of up to $15,000 for eligible first-time homebuyers. The credit could be collected when a home is purchased, rather than later at tax-return filing time.

- Establish a new refundable tax credit for low-income renters. The credit would be intended to hold rent and utility payments to 30% of monthly income.

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Biden Tax Proposals

9. ‘Green energy’ tax changes

- Reinstate or expand tax incentives intended to reduce carbon emissions — such as deductions for emission-reducing investments in residential and commercial buildings

- Restore credits for buying **electric vehicles** produced by manufacturers whose credits have been phased-out under current law.

- Eliminate federal income tax deductions for oil and gas drilling costs and depletion.

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Biden Tax Proposals

10. And finally…Increase Corporate Tax Rate to 28%

- One of the biggest changes in the 2017 Tax Cuts and Jobs Act (TCJA) was the installation of a flat 21% corporate federal income tax rate for 2018 and beyond. Before the TCJA, the maximum effective rate for profitable corporations was 35%. The Biden plan would increase the corporate tax rate to 28%. This change would raise an estimated $1.1 trillion or so over 10 years.

- Impose a new **15% minimum tax** on corporations with at least $100 million in annual income that pay little or no federal income tax under the “regular rules.” An affected corporation would pay the greater of: (1) the “regular” federal income tax bill or (2) **15% of reported book net income**. This new tax would raise an estimated $160 billion to $320 billion over 10 years.

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Tax Planning Tips

- Use the 0% capital gains tax rate if your taxable income is less than 40,000 for single or 78,750 for MFJ
- Take advantage of 100% bonus depreciation (for 5, 7, and 15-year and QIP property), maximize your new vehicle deductions, improve existing commercial real estate, get a cost segregation study on a new building
- Use the liberal repair and expensing provisions still in place on business and rental properties

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Tax Planning Tips

- Plan for higher taxes
- Review your estate planning & update your wills and trusts

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