Chemel Kornick & Mooney, LLC
Certified Public Accountants

2020 Tax Update

Part 1
Miscellaneous Tax Updates

South Dakota v Wayfair

- Related to Sales Tax, but has far-reaching implications for State Income Tax
- Quill & PL 86-272 – How state nexus has been historically determined
  - Quill – physical presence test
  - PL 86-272 – relates only to the sale of tangible personal property

South Dakota v Wayfair

- SD passed a law creating "economic nexus"
  - If you have $100,000 of sales in SD or 100 transactions, you had nexus with SD and were required to collect Sales Tax.
  - Commerce has been changing rapidly since the Quill decision in 1992
    - Justice Neil Gorsuch, in the majority opinion in Wayfair: "The Court could not have envisioned a world where the world's largest retailer would be a remote seller."

South Dakota v Wayfair

- The far-reaching implication is this: if you are selling products or intangibles remotely, you potentially have Sales Tax and Income Tax exposure in many more states
  - Regardless of physical presence
  - If you have a customer, you have potential exposure
  - Data collection and analysis is a challenge

South Dakota v Wayfair

- While this is a Sales Tax ruling, all but 2 states have established economic presence standards for Income Tax Nexus
  - Generally $200,000 sales or 200 transactions
  - Each state varies slightly
  - Only 2 states do not have the rules on their books – FL & MO, and even they have the rules proposed

South Dakota v Wayfair

- What you need to know
  - Wayfair included a provision for no retroactive collection. The effective date for each state is generally not before 2017.
  - It is worth a discussion with your clients or with your CPA regarding how to get into compliance.
    - States will send nexus questionnaires to companies when they suspect economic nexus.
    - It is at this point that you would begin to file when you exceed the thresholds.
  - Compliance burden is potentially extreme. Justice John Roberts even made this point in his Minority Opinion

TRUMP

GILTI Update

- GILTI is the annual inclusion of foreign subsidiary income in the taxable income of a U.S. corporation.
- Established under TCJA
- Unintended consequences related to loss corporations
- Possible exception out of inclusion
  - Included in final regs just released
  - If your foreign local tax rate is high enough, you can be excepted from U.S. inclusion of GILTI
  - Very complex – if you think this applies, talk to your CPA.

CARES Act

- CARES Act – Various Provisions
  - Qualified Improvement Property – technical correction
    - QIP was streamlined under TCJA, but an error led to QIP being treated as 39 year property.
    - With technical correction, you can claim 15 year life and 100% bonus on QIP
    - IRS allowing amended returns to claim 100% bonus
  - Net Operating Losses
    - TCJA – limited to 80% of taxable income each year, no carrybacks, unlimited carryforward
    - CARES – removes 80% limitation; allows 5 year carryback
      - For NOL's generated in tax years beginning after 12/31/17 and before 1/1/21

CARES Act

- CARES Act – Various Provisions
  - Additional $300 Charitable Contribution Deduction
    - Above the line deduction even if you do not itemize
    - One deduction per return – marriage penalty
    - Possibility to become permanent and expanded in future stimulus package
  - Updates to Form 1040 for 2020
    - Cryptocurrency questions now on page 1
    - Many lines added to expand previously consolidated lines
    - Page 2, Line 30 for reconciliation of stimulus payments received during 2020

CARES Act

- Paycheck Protection Program (PPP) Loan Forgiveness
  - Window for applying for loans has passed – let's focus on ensuring that the loans are forgiven
  - Paycheck Protection Program Flexibility Act (PPPFA) signed into law on June 5, 2020
    - Payroll costs now only 60%, down from 75%
    - Loans after June 5 now have 24 weeks to spend the money
      - Loans prior to June 5 can stick to 8 weeks if so desire
    - Deadline to rehire workers is now December 31, 2020

CARES Act

- Paycheck Protection Program (PPP) Loan Forgiveness
  - For loans not forgiven, you now have 5 years to pay back the loan
  - Loans are generally nonrecourse
  - Additional Waivers under PPPFA
    - You were unable to hire someone for the same position that you previously cut
    - You were unable to return to the same level of business you had on February 15, 2020

CARES Act

- Paycheck Protection Program (PPP) Loan Forgiveness
  - Haircuts – Reductions of Loan Forgiveness
    - FTE Haircut
      - Generally you must have the same number of Full Time Equivalent (FTE) workers by December 31, 2020 that you had in February 2020
      - 40 hours/week = 1 FTE (overtime doesn't count)
      - You can choose a safe harbor which counts each PT employee as .5 FTE, regardless of hours worked
      - Simple example – 10 FTE in February, $100k PPP
        - 9 FTE in December
        - Forgiveness reduced to $90,000

CARES Act

- Paycheck Protection Program (PPP) Loan Forgiveness
  - Haircuts – Reductions of Loan Forgiveness
    - Wage Reduction Haircut
      - Generally, you can cut up to 25% of previous payroll costs without having a haircut
      - This only applies to workers who worked during the covered period
      - No wage reduction counted for any worker who, in any given pay period, earned over $100,000 on an annualized basis, even if salary for the year is less than $100,000
      - Only for portion NOT from reduced hours

CARES Act

- Paycheck Protection Program (PPP) Loan Forgiveness
  - Amounts forgiven are NOT COD income
    - No 1099-C will be issued
    - Will be taxable – in the form of the expenses paid for with loan proceeds will be nondeductible.
      - Expenses funded by the Federal government are not deductible – this is the current argument
      - Very important to discuss with your clients when planning for 2020 income taxes

CARES Act

- Additional Stimulus?
  - Looking like nothing until after Inauguration Day
  - HEROES Act – passed by the House
    - Includes another round of PPP
    - Incudes another round of stimulus checks
    - By all indications, will be similar to what we already had earlier this year.

BIDEN

Part 2

President-Elect Biden Tax Plan

Presidential Tax Plan

- President-Elect Joe Biden
  - Payroll Tax & Individuals
    - Additional 12.4% FICA tax on earned income above $400k, evenly split between employee & employer.
      - Donut Hole between $137,700 & $400,000
    - Top tax rate reverts to pre-TCJA level of 39.6% starting at $400,000 (down from about $600,000 for 2020)
    - Qualified Income taxed at ordinary income tax rates (39.6% max) on income above $1,000,000.
    - Itemized deductions limited to 28% of value – similar to AMT pre-TCJA
    - Restores Pease Limitation
    - QBI Deduction phased out if over $400k
    - Estate tax – lifetime exemption reduced to pre-TCJA levels with elimination of step up in basis at death

Presidential Tax Plan

- President-Elect Joe Biden
  - Business Changes
    - Corporate Tax increase from 21% to 28%
    - AMT of 15% on book profits of $100 million or higher
    - Tax rate on GILTI (foreign profits) increased from 10.5% to 21%
    - Various credits related to businesses with layoffs or institutional closure, among other credits

Presidential Tax Plan

- President-Elect Joe Biden
  - Various
    - $8,000 credit for childcare
    - Eliminating real estate industry loopholes
    - Expansion of the ACA Premium Tax Credit
    - Economic Impact
      - While Joe is saying he won't raise taxes on anyone making less than $400,000, the Tax Foundation analysis shows that the bottom 20% would see a .5% decrease in after tax income while the top 1% would see a 13% decrease
      - Overall, the economy would shrink by 1.51%

WOLF

Part 3

Tax Planning for 2020 & 2021

Planning for 2020 & 2021

- What Does the Planning Environment Look Like?
  - Historically low tax rate environment
  - Even with Biden being elected, any major changes most likely would not take effect until 1/1/2022
  - TCJA only changed specific transactions at the end of 2017, with the major changes taking effect as of 1/1/2018, a full year after inauguration

Planning for 2020 & 2021

- Basics of Tax Planning – Accelerating Deductions and Deferring Income
  - Cash in hand is probably still always preferable to theoretical rate savings down the road
  - Timing of transactions is something to consider when major tax law changes take place
  - Time the transaction in 2020 to ensure current rate structure
  - 2021 probably ok as well, but impossible to know
  - Don’t let the tax tail wag the dog!

Planning for 2020 & 2021

- Charitable Contributions – under TCJA, charitable giving has become one of the main planning areas for additional deductions
  - CARES Act increased AGI limit to 100% for 2020
  - Bunching – this has gained popularity as a strategy when TCJA raised the standard deduction
    - Vast majority of taxpayers claiming standard deduction
    - Let's assume no mortgage, $10,000 of SALT – this leaves $14,000 of charitable deductions required just to start receiving any benefit
    - Most taxpayers take the "Free $14,000" and don't give anything else

Planning for 2020 & 2021

- Charitable Contributions – under TCJA, charitable giving has become one of the main planning areas for additional deductions
  - Bunching
    - The planning concept here is to "bunch" the charitable deductions into one year, instead of multiple years
    - Example:
      - $20,000/yr annual giving for 5 years = $100,000 total over 5 years
      - Under TCJA, $6,000 deduction each year, or $30,000 total over 5 years; $30,000 total itemized deductions each year for 5 years; $150,000 total

Planning for 2020 & 2021

- Charitable Contributions – under TCJA, charitable giving has become one of the main planning areas for additional deductions
  - Bunching
    - Example – with Bunching
      - $100,000 in year 1, so $110,000 itemized deductions in year 1 and $24,000 in years 2-5; $206,000 total
      - The "Free $14,000" only applies in year 1. In years 2-5, standard deduction of $24,000 is claimed
    - Client should be charitably inclined already, and have the cash flow for this to make sense
    - Donor Advised Fund

Planning for 2020 & 2021

- Charitable Contributions – under TCJA, charitable giving has become one of the main planning areas for additional deductions
  - Gifting of Appreciated Property
    - Forego the capital gains tax while also receiving a full deduction for the FMV at the time of the gift
    - As mentioned, capital gains are an area of emphasis under Biden's plan, so this could only get better
  - Reminder: gifts in one tax year that exceed 60% of AGI will carryforward for 5 years
  - Qualified Charitable Disbursement (QCD)

Planning for 2020 & 2021

- Roth IRA Conversions
  - “Backdoor” Roth Conversions
    - Roth IRA’s have very low income limitations, so many higher income taxpayers don’t qualify for direct contributions
    - Nondeductible Traditional IRA Contribution to new Traditional IRA account
    - Convert this contribution to a Roth – pay tax on the earnings (should be close to $0)
    - Caution: this works best for taxpayers with no other Traditional IRA’s, as you are required to account for the FMV of ALL Traditional IRA’s when converting to a Roth. You cannot pick and choose IRA funds.
    - Sole Shareholder of S-corporation – SEP IRA

Planning for 2020 & 2021

- Roth IRA Conversions
  - Does it make sense to convert to a Roth in 2020?
    - Locks in lowest rates possible on entire balance at date of conversion
    - Grows tax free
    - No RMD’s in later years
    - No unexpected tax bills for beneficiaries
    - Important: only convert if you can pay the tax from non-IRA funds. This preserves as much of the benefit as possible.
    - Plan around conversion, possibly pair it with another deduction or loss that makes sense

Planning for 2020 & 2021

- What Does Good Tax Planning Look Like?
  - Proactive
  - Focused on the best result for all parties while meeting the requirements of the tax code
  - Considers all aspects of the transaction, not just the tax savings.
- Where is the Value in Good Tax Planning?
  - Minimize tax obligations
  - Peace of mind regarding future transactions
  - Someone in your corner with the IRS
  - Do you truly understand your tax situation?

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Questions?

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