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Year-End Tax Planning, Review of Recent Tax Legislation and Where are we Going?

Estate Planning Council

NAEPC

National Association of Estate Planners & Councils (NAEPC)

- Value Partners (flagship *Trusts & Estates* $149 subscription) - Discounts available, no additional work by board to supply members other than promoting them
- Webinars at value pricing – Dec 8th Webinar - **Estate Planning for Modern Families: Planning for Diversity and Flexibility**
- Reduced pricing to attend annual conference, obtain CE, build national network of professionals
- Annual (Virtual) Conference – November 2, 2021

  *** 2022 in Fort Lauderdale, FL
- *NAEPC Journal of Estate & Tax Planning* – ability for council members to opt in
- Monthly Leimberg Newsletter on national website
- AEP Designation - https://www.naepc.org/designations/estate-planners

Coronavirus Aid Relief and Economic Security (CARES) Act

- Enacted March 27, 2020
- $2.2 Trillion Stimulus Package
- Recovery Rebate
- PPP Loan
- Business Tax Relief
- Individual Tax Relief

Consolidated Appropriations Act of 2021

- Enacted December 27, 2020
- $900 Billion Stimulus Package
- Recovery Rebate
- PPP Loan – 2nd Draw and Clarity of 1st Round
- Business Tax Relief
- Individual Tax Relief

America Rescue Plan Act of 2021

- Enacted March 11, 2021
- $1.9 Billion Stimulus Package
- Recovery Rebate -$1400 most adults and their children
- Aid for Schools, state and local governments
- Extension and modification of payroll tax credits
- Individual Tax Relief – increase in credits
- Child tax credits- increased from $2k to $3k (T/Ps received monthly checks in July, to receive estimated 50% benefit)
- Tax Treatment of COVID-19 Relief

SECURE Act

- Increase retirement age to 72 from 70.5 on RMDs
- Elimination of the Stretch IRAs
- For non-spousal inherited IRAs – must be distributed within 10 years, exceptions do apply, if beneficiary is a minor child
- Credits for setting up new retirement plans
- Dates for adopting new retirement plans in place can be completed after the end of the year, before the return is filed

SECURE Act 2.0 – Securing a Strong Retirement Act

- Proposed bill is an extension of the SECURE ACT
- Automatic enrollment in retirement plans
- Indexing IRA catch-up limit
- Higher catch-up limits to apply ages 62 - 64
- Increase in age for RMDs
- Individuals with domestic abuse – penalty waived
- SIMPLE and SEP Roth IRAs

Infrastructure Investment and Jobs Act

- President Biden signed the bill November 15th
- No significant tax provisions
- Termination of Employee Retention Credit – back to October 1st.
- Information reporting for digital assets – such as cryptocurrency
- Provisions covering disaster relief, capital contributions to public utilities, excise taxes, and pension interest rates.

The American Families Plan Tax Compliance Agenda

- Biden Proposal to overhaul tax administration – with nearly $80 Billion in funding
- Tax gap of $600 Billion in 2019
- Taxpayers fail to file in a timely manner
- Underreport income or overclaim deductions
- Underpay taxes despite filing a timely return
- Increase resources, reporting of financial information, overhaul technology and increased penalties for tax preparers with intentional negligence

Paycheck Protection Program (PPP) Overview

- To help cover the costs of payroll, rent and utilities
- Allows for 100% forgiveness
- Loan is administered through the U.S. Small Business Administration (SBA) but processed directly through your lender
- Approximately 11 Million loans processed, almost $525 Billion in funding.
- **Deductibility of expenses:** Finally, clarity regarding this issue. The latest bill will made it clear that **businesses will be allowed to deduct the costs covered by those loans.**

Paycheck Protection Program (PPP) Round 2

- Available to first-time qualified borrowers (who did not receive a loan the first time around)
- Businesses that previously received a PPP loan for up to $2 million, provided they have 1) 300 or fewer employees, 2) have used or will use the full amount of their first PPP loan and 3) can show a 25% gross revenue decline in any 2020 quarter compared with the same quarter in 2019.

Employee Retention Credit

- Employers are eligible for the credit if they operate a trade or business during calendar year 2020 and experience either:

1. the full or partial suspension of the operation of their trade or business during any calendar quarter because of governmental orders limiting commerce, travel, or group meetings due to COVID-19, or
2. a significant decline in gross receipts.

- A significant decline in gross receipts begins:

  on the first day of the first calendar quarter of 2020 for which an employer's gross receipts are less than **<u>50%</u>** of its gross receipts for the same calendar quarter in 2019.

- The significant decline in gross receipts ends:

  on the first day of the first calendar quarter following the calendar quarter in which gross receipts are more than of 80% of its gross receipts for the same calendar quarter in 2019.

The maximum amount of qualified wages taken into account with respect to each employee is $10,000, $5,000 credit an employee, a year.

- For 2021 – this is increased to $7,000 in wages a quarter – extended thru the end of the year

Recovery Rebates for Individuals – Sec. 2201 – Economic Income Payments

- $1,200 advance credit per person;
- $500 per qualifying child
- $75,000 AGI ($150,000 MFJ, $112,500 HOH)
- Reduced by $5 for each $100 that a taxpayer’s income exceeds the phaseout threshold.
- Taxpayer can still qualify for 2020 tax year.
- Changes depending on dependent children
- Review MFS for benefit of the credit in 2020

Recovery Rebates for Individuals – Sec. 2201 – Economic Income Payments
Round 2

- $600 advance credit per person; including qualifying child
- $75,000 AGI ($150,000 MFJ, $112,500 HOH)
- Reduced by $5 for each $100 that a taxpayer's income exceeds the phaseout threshold.
- Taxpayer can still qualify for 2020 tax year.
- Changes depending on dependent children
- Review MFS for benefit of the credit in 2020

Special Rules For Use of Retirement Funds – Sec. 2202

- $100,000 “coronavirus-related distribution” exemption from § 72(t)
- A qualified person:
  - diagnosed with COVID-19,
  - whose spouse is diagnosed with COVID-19,
  - who experiences adverse financial consequences as a result being quarantined, furloughed, or laid off or having work hours reduced, being unable to work due to lack of child care, closing or reducing hours of a business owned or operated or other factors determined by the Secretary

Eligible retirement plans include individual retirement accounts or annuities (IRAs), qualified employer-sponsored retirement plans, 403(a) annuity plans, 403(b) tax-sheltered annuity plans, and 457(b) plans.

Special Rules For Use of Retirement Funds – Sec. 2202

Additional Guidance – Notice 2020-50

- The individual, and the individual's spouse or a member of the individual's household being quarantined, being furloughed or laid off, or having work hours reduced due to COVID-19, being unable to work due to lack of childcare due to COVID-19, having a reduction in pay (or self-employment income) due to COVID-19, or having a job offer rescinded or start date for a job delayed due to COVID-19; or
- closing or reducing hours of a business owned or operated by the individual and individual's spouse or a member of the individual's household due to COVID-19.
- The following amounts are not coronavirus-related distributions:
  - corrective distributions of elective deferrals and employee contributions that are returned to the employee,
  - excess elective deferrals under §402(g),
  - excess contributions under §401(k),
  - and excess aggregate contributions under §401(m);
  - loans that are treated as deemed distributions pursuant to §72(p);
  - dividends paid on applicable employer securities under §404(k);
  - the costs of current life insurance protection;
  - prohibited allocations that are treated as deemed distributions pursuant to §409(p);
  - distributions that are permissible withdrawals from an eligible automatic contribution within §414(w);
  - and distributions of premiums for accident or health insurance under §1.402(a)-1(e)(1)(i).

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions

- Distributions must take place in 2020
- 10% Excise tax on early distributions is waived
- Income from the distribution recognized ratably over a three year period (2020, 2021 and 2022)
- Elect out of 3 year period, include all in 2020
- Amount distributed can be repaid over a three year period
- 20% withholding requirement is not applicable

Special Rules For Use of Retirement Funds – Consolidated Appropriations Act of 2021

Qualified Disaster Distributions

- Similar to the CARES Act; Up to $100,000 distribution
- 10% Excise tax on early distributions is waived
- Income from the distribution recognized ratably over a three year period
- Elect out of 3 year period, include all in distribution year
- Amount distributed can be repaid over a three year period
- 20% withholding requirement is not applicable

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- New Form 8915 – E – will be filed with the individual's income tax return
- Any repayment by the filing of the tax return is not reported as income for distribution year

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- *Example 1*. Taxpayer B receives a $45,000 distribution from a §403(b) plan on November 1, 2020. Taxpayer B is a qualified individual and treats the distribution as a coronavirus-related distribution. Taxpayer B receives no other coronavirus-related distribution from any eligible retirement plan. Taxpayer B recontributes $45,000 to an IRA on March 31, 2021. Taxpayer B reports the recontribution on Form 8915-E and files the 2020 federal income tax return on April 10, 2021. For Taxpayer B, no portion of the coronavirus-related distribution is includible as income for the 2020 tax year.

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- *Example* 2. The facts are the same as in *Example 1* of this section 4.D, except that Taxpayer B timely requests an extension of time to file the 2020 federal income tax return and makes a recontribution on August 2, 2021, before filing the 2020 federal income tax return. Taxpayer B files the 2020 federal income tax return on August 10, 2021. As in *Example 1*, no portion of the coronavirus-related distribution is includible in income for the 2020 tax year because Taxpayer B made the recontribution before the timely filing of the 2020 federal income tax return.

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- *Example 3*. Taxpayer C receives a $15,000 distribution from a governmental §457(b) plan on March 30, 2020. Taxpayer C is a qualified individual and treats the distribution as a coronavirus-related distribution. Taxpayer C elects out of the 3-year ratable income inclusion on Form 8915-E and includes the entire $15,000 in gross income for the 2020 taxable year. On December 31, 2022, Taxpayer C recontributes $15,000 to the §457(b) plan. Taxpayer C will need to file an amended federal income tax return for the 2020 tax year to report the amount of the recontribution and reduce the gross income by $15,000 with respect to the coronavirus-related distribution included on the 2020 original federal income tax return.

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- *Example 4*. Taxpayer D receives $75,000 from a section 401(k) plan on December 1, 2020. Taxpayer D is a qualified individual and treats the $75,000 distribution as a coronavirus-related distribution. Taxpayer D uses the 3-year ratable income inclusion method for the distribution. Taxpayer D makes one recontribution of $25,000 to the section 401(k) plan on April 10, 2022. Taxpayer D files the 2021 federal income tax return on April 15, 2022. Without the recontribution, Taxpayer D should include $25,000 in income with respect to the coronavirus-related distribution on each of D's 2020, 2021, and 2022 federal income tax returns. However, as a result of the recontribution to the section 401(k) plan, Taxpayer D should include $25,000 in income with respect to the coronavirus-related distribution on the 2020 federal income tax return, $0 in income with respect to the coronavirus-related distribution on the 2021 federal income tax return, and $25,000 in income with respect to the coronavirus-related distribution on the 2022 federal income tax return.

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- *Example 5*. The facts are the same as in *Example 4*, except that Taxpayer D recontributes $25,000 to the section 401(k) plan on August 10, 2022. Taxpayer D files the 2021 federal income tax return on April 15, 2022, and does not request an extension of time to file that federal income tax return. As a result of the recontribution to the section 401(k) plan, Taxpayer D should include $25,000 in income with respect to the coronavirus-related distribution on the 2020 federal income tax return, $25,000 in income with respect to the coronavirus-related distribution on the 2021 federal income tax return, and $0 in income with respect to the coronavirus-related distribution on the 2022 federal income tax return.

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Distributions – Tax Treatment

- *Example 6. Example*. Taxpayer E receives a distribution of $90,000 from his or her IRA on November 15, 2020. Taxpayer E is a qualified individual and treats the distribution as a coronavirus-related distribution. Taxpayer E ratably includes the $90,000 distribution in income over a 3-year period. Without any recontribution, Taxpayer E will include $30,000 in income with respect to the coronavirus-related distribution on each of the 2020, 2021, and 2022 federal income tax returns. Taxpayer E includes $30,000 in income with respect to the coronavirus-related distribution on the 2020 federal income tax return. Taxpayer E then recontributes $40,000 to an IRA on November 10, 2021 (and makes no other recontribution in the 3-year period). Taxpayer E is permitted to do either of the following:
- Option 1. Taxpayer E includes $0 in income with respect to the coronavirus-related distribution on the 2021 federal income tax return. Taxpayer E carries forward the excess recontribution of $10,000 to 2022 and includes $20,000 in income with respect to the coronavirus-related distribution on E's 2022 federal income tax return.
- Option 2. Taxpayer E includes $0 in income with respect to the coronavirus-related distribution on the 2021 tax return and $30,000 in income on the 2022 federal income tax return. Taxpayer E also files an amended federal income tax return for 2020 to reduce the amount included in income as a result of the coronavirus-related distribution to $20,000 (that is, the $30,000 original amount includible in income for 2020 minus the remaining $10,000 recontribution that is not offset on either the 2021 or 2022 federal tax return).

Special Rules For Use of Retirement Funds – Sec. 2202

Retirement Plan Loans

- Limit increased from $50,000 to $100,000
- Limit increased to 100% of the present value from 50%
- Outstanding loan repayment delayed due between enactment of the CARES Act and before December 31, 2020 and year-end delayed one year
- Provisions extended under the new law

Temporary Waiver of Required Minimum Distributions (RMDs) – Sec. 2203

- RMDs ARE required in 2021
- RMDs are not required in 2020
- RMDs account owners over 70 ½ and 72 (SECURE Act)
- Includes inherited IRAs
- Taxpayers subject to the 5-year rule (non-designated beneficiaries) can "skip" 2020, adds a year
- Repayment of ALL RMDs by August 31, 2020; can't reverse withholding
- Defined benefit plans (such as pensions) are excluded

Modifications for NOLs – Sec. 2303

Any NOL arising in a tax year after December 31, 2017 and before January 1, 2021, may be carried back 5 years unless the carryback period is waived

Tax Year	CARES Act	Previous Law - TCJA eliminated carryback
2016 2017	3-year carryback Indefinite carryforward No 80% cap	3-year carryback 20-year carryforward
2018 2019 2020	5-year carryback Indefinite carryforward No 80% cap	No carryback allowed Indefinite carryforward of current losses Capped at 80% of taxable income
2021	No carryback 20-year carryforward for NOLs before 1/1/18 PLUS the lessor of 1) All NOLs after 12/31/17, OR 2) 80% of taxable income	No carryback allowed Indefinite carryforward of current losses Capped at 80% of taxable income

Change in Business Meals Deduction Consolidated Appropriations Act of 2021

- One of the smallest provisions is also one of the most divisive: the return of the 100% deduction of the so-called three-martini lunch — that is, an increased tax break for business lunches, which are currently at 50%. This applies to restaurant and takeout meals paid for in 2021 and 2022, and is not retroactive

Current Environment…Where are we now?

- Record government debt risks
- Highest deficit in decades

How to mitigate this?

- Tax increases?   Spending Cuts?
- Corporate tax rate – possible increase from 21% (28% - Biden Proposal)
- Capital Gains – proposal to increase to ordinary rates on capital gains over $1 million
- Most TCJA individual provisions expire 12/31/25
- Estate Tax change TCJA - scheduled to expire 12/31/25

Latest Tax Policy – Build Back Better plan by the House Ways & Means Committee

	CURRENT PROPOSAL	ORIGINAL PROPOSAL	COMMENT
INCOME TAX RATES	No Change to current law	Increase tax rates from 37% to 39.6%	Included in all proposals, rates restored to pre-TCJA
LONG TERM CAPITAL GAINS & QUALIFIED DIVIDEND RATES	No Change to current law	Increase rate from 20% to 25% for higher income taxpayers	Higher capital gain rates included in all proposals, including use of ordinary rates
NET INVESTMENT INCOME TAX	Expand the 3.8%, will apply to income from trade / business New Surcharge – 5% on MAGI > \$10M, 3% > \$25M	Expand the 3.8% surtax, will apply to income from trade / business	Additional surtax for higher income taxpayers Surcharge applies to trusts >\$200k; >\$500k
QUALIFIED BUSINESS INCOME DEDUCTION	No Change to current law	Limit IRC Sect 199A – max deduction of \$500k / \$400k (Single)	May impact entity choice – flow thru vs C Corp

Latest Tax Policy – Build Back Better plan by the House Ways & Means Committee

	CURRENT PROPOSAL	ORIGINAL PROPOSAL	COMMENT
Carried Interest Tax Benefit	No Change to current law	Increase holding period for preferential tax treatment from 3 to 5 yrs	Changed from 1 yr to 3yrs - TCJA
Retirement Account Changes	Limits size of IRAs to \$10M, accelerate RMDs on these accounts	Limits size of IRAs to \$10M, requires extra RMDs for larger IRAs; elimination of back door Roth IRAs	New provisions, surprising possible new laws
Corp tax rate	Impose 15% min tax for corp, profits > \$1B (2023); foreign changes	Increase from flat 21% to 26.5% (add tiered levels)	Included increase in many proposals
Estate, Gift and Generations Skipping Taxes	No Change to current law No repeal of stepped-up basis/ capital gain; No special restrictions on GRATs	Reduce exemption to \$5M pre-TCJA amounts (indexed for inflation); sunset on Jan 1, 2026	Additional rules relating to grantor trusts and eliminating discounting

Latest Tax Policy – Build Back Better Plan

House Rules Committee Print 117-18 – released Nov 3 and amended Nov 4

- Raise the cap on state and local tax (SALT) deduction from $10,000 to $80,000; extend the cap through 2030; the cap would also apply to the 2021 tax year
- Create a 1% excise tax on the value of stock repurchases
- Extend the American Rescue Plan Act - Child Tax Credit expansion through 2022, make the CTC fully refundable on a permanent basis
- Extend the American Rescue Plan Act temporary expansion of the Earned Income Tax Credit eligibility and amount through 2022

Estate Tax

- Increased exemption only though 2025
- Biden term 2020 to 2024
- Rate might decrease below 2012 amounts
- Planning to use the large exemption ***now*** – ***while you can***

Estate and Gift Tax
"Use it or Lose it"

- Final Regs – NO clawback – if the exemption is used and the exemption decreases
- OLD exemption - $5,790,000 – this amount is used first
- 2018 Exemption increase - $5,790,000 – LOST if not used before the law changes

$2.3 M Benefit

Estate Tax Planning

- Suppressed assets values if business is down in 2020-21 due to the impact of Covid
- Valuation discounts
- Donating Capital Gain Property
- Loss Harvesting
- Planning for No Step-Up in Basis
- Low interest rates – for purposes of
  - family loans, note sales, GRATs

- Best planning done as a TEAM!

Build Back Better Plan – Estate Tax Provisions

- Elimination of valuation discounts for interests in entities holding non-business assets – passive assets like marketable securities – like family limited partnerships (FLP)
- Grantor trusts includible in the Estate (grandfathering trusts before date of enactment)
- Gifts made to a pre-existing grantor trust subsequent to date of enactment, this gift would result in portion of the trust includable in grantor's taxable estate
- Sales between grantor and grantor trust treated as a realized income tax event
- Issue for ILITs – funding of premiums

Estate Tax Planning

- If taxable estate is jointly greater than $20 Million, consider using the excess exemption that will sunset, by creating a SLAT
- Establish and fund an irrevocable grantor trust now
- Complete gifts in 2021 where you can still use discounts in the member interests of FLP or similar property
- Fund grantor retained annuity trusts (GRATs), and consider setting a longer term than is customary for those GRATs (greater mortality risk, would keep assets in a transfer tax-efficient structure for longer) Usually, GRATs are created for brief terms, often two or three years

Estate Tax Planning

- Dynasty Trusts – designed to provide assets free of transfer taxes to two or more generations below the grantor
- Spousal Lifetime Access Trust (SLAT) – permits each spouse to transfer assets of the couple's estate and allows the non-transferor spouse to be a lifetime beneficiary of the trust
- Charitable intent? – Charitable Remainder Trusts
- Use of Disclaimers – effectiveness for income tax purposes is uncertain/should work for transfer tax

Estate Planning - Charitable Remainder Trusts

- Transfer of highly appreciated assets to a trust
- Annual payments (or more frequently) for life (or a term of years)
- At the time of transfer – calculation is completed for the present value of the remainder interest for a tax deduction
- At the donor's death (or end of the term), charity receives the residual assets from trust
- Charitable Remainder Annuity Trust (CRAT)
- Charitable Remainder Unitrust (CRUT)

Income Tax Planning

- Accelerate income into 2021—particularly if your income is above $5 million, as your total rate increase might be 5.6%(2.6% for ordinary bracket + 3% surtax).
- Defer deductions including charitable deductions into 2022. A deduction's economic value is higher when the taxpayer's tax rate is higher. To be sure, deferring the deduction, or accelerating discretionary income, requires paying tax sooner on income, so taxpayers would have to weigh the economics of paying more tax now at a lower rate rather than recognizing more income in a future year at higher rates. If 2021 was an outsized income year for you or you are donating appreciated assets to charity, it could still make sense to donate in 2021 even if rates increase next year.
- Watch changes in Itemized Deductions – possible items previously mentioned – SALT eliminate $10k cap and reinstate PEASE

Income Tax Planning

- Retirement planning – increase deductions in 2021, maximizing contributions – cash balance plan
- Qualified Business income deduction – review taxable income, retirement contributions can decrease your income, causing a taxpayer eligible for 199A deduction
- Review the full picture of 2021 and 2022, analyzing the tax impact with new tax laws

ROTH IRA CONVERSIONS

- SECURE – elimination of the stretch IRA
- Potentially lower business income or loss due to economic environment
- Offset in increased charitable contribution deduction (100% of AGI)
- Payment of tax – reduces estate
- Possible increase in tax rates in the future

IRA Planning

- Most likely tax rates will increase in future years, opportunity to take advantage of a Roth IRA conversion. Possible benefit to complete a Roth IRA conversion based on tax law changes.
- SECURE Act eliminates the “stretch IRA”
- New concern for clients with substantial retirement accounts
- All inherited IRAs starting January 1, 2020, you can no longer stretch your distributions
- For non-spousal inherited IRAs – must be distributed within 10 years
- Exceptions – minor child, less than 10 years younger than original owner and disabled/chronically ill
- Market volatility – beware - no longer can reverse the conversion

Charitable Donations

- Important to make <u>timely</u> deductions – not necessarily to accelerate – increased standard deduction
- Donor Advised Funds - DAF
- Contribution of appreciated assets
- Qualified Charitable Distributions from IRAs
- 2021 – allows for 100% AGI limitation for cash donations – does not include DAF
- 2021 - $300 above the line Charitable donation, $600 joint

Tax law changes should hopefully be finalized soon which will help to obtain SOME clarity.

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Please reach out if additional assistance is needed

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Thank you!