

Tax Law Update & Year-End Tax

Planning 2021



Legislative Update

Where are we with Reconciliation Now?:

- What I was *almost* certain about...
 - 39.6% tax rate
 - Increased capital gains rate
 - Loss of increased Estate Tax Exemptions
- What I was concerned about...
 - Loss of Like-Kind/Sec. 1031 exchanges
 - Wealth planning techniques – Dynasty Trusts
 - Step-up in basis at death
- None of these are in the latest, stripped-down version of the bill...
- What is in the new version of the Build Back Better Act for individual taxpayers...
 - 5% surtax on income above \$10MM
 - 8% surtax on income above \$25MM
 - SALT deduction limit raised to \$80K
- The only consistency has been surprise...

Business Owner Update

Build Back Better Act for Business Owners...

- 3.8% Net Investment Income Tax (NIIT) will apply to S-Corporation distributions
- Qualified Small Business Stock exemption is reduced from 100% to 50%
- Limit the use of active pass-through business losses to 80% of income from future years
- But... keep an eye on AB 150 to permit a fuller deduction of state and local taxes

Income Tax Planning

Minimize Income Where Possible:

- Wait to sell assets that have capital gain
- Defer invoices if cash-method accounting

Maximize Deductions:

- Maximize contributions to qualified plans
- Sell loser investments – tax loss harvesting
- Take advantage of \$3K of capital loss against ordinary income
- Incur deductible business expenses before year-end
- Put new equipment in service that qualifies for 100% Sec. 179 deduction
- Consider “bunching” charitable deductions or use a Donor Advised Fund

Income Tax Planning

Business Specific Issues :

- Pay attention to your Net Operating Losses and speak with your tax advisor
- Maximize your 199A deduction if you qualify (20% deduction against QBI)
- Review your overall business entity structure at year-end

Pay Attention to Tax Elimination Strategies:

- Consider Qualified Opportunity Zones
- Position yourself to meet requirements for Qualified Small Business Stock exclusion

Tax-Loss Harvesting

Selling stock at a loss to offset capital gains in other positions

But Remember:

- You cannot repurchase the same security within 30 days (unless its Bitcoin?)
- But you can (i) buy something similar (not too similar), or (ii) wait 31 days
- Don't let the tax tail wag the investment dog—maintain your investment strategy
- Business owners should look to sell assets that are held at a loss

Account with Special Tax Treatment

Benefits of qualified accounts [401(k) and IRAs]:

- Reduces taxable income in the current year
- Tax on growth is deferred until funds are withdrawn
- But... all distributions are taxed as ordinary income

Qualified Accounts for Business Owners:

- Consider a Solo 401(k) or a SEP IRA
- With significant income, consider a Defined-Benefit Pension Plan or Cash Balance Plan... but there are administrative requirements and actuarial calculations involved Contact an administrator

Qualified Account Considerations:



Roth IRA Conversion:

- Converting an IRA to a Roth IRA is a taxable event and will cause the converted amount to be included in your taxable income.
 - All growth is then tax-free
 - Distributions are entirely tax-free

Charitable Distributions:

- Qualified Charitable Distributions can be made from your IRA
 - Must be 70 and 1/2 years old
 - Creates a guaranteed indirect deduction regardless of AGI amounts or whether the taxpayer itemizes
 - Satisfies your RMD requirements

Charitable Gifting

Deductions for Charitable Gifts:

- Cash gifts to qualified charities – up to 100% of AGI
- Gifting appreciated stock in-kind for a “double” deduction
- Bunching charitable gifts to reach itemization level of deductions – Donor Advised Fund can be helpful here

Charitable Remainder Trust:

- Prior to a sale of business or valuable, highly appreciated asset, consider the use of a Charitable Remainder Trust
- The trust sells the asset and pays no income tax
- You make investment decisions with the sale proceeds
- You receive an annuity for a term of years or the rest of your life (this payment is taxable to you, but that tax is deferred over the life of the annuity)
- Charity receives the remaining assets after the term of the annuity

Family Gifting

Tax-free gifting:

- Each taxpayer can make a \$15K tax-free gift (\$30K for married couple) to as many beneficiaries as they choose.
- This annual gift tax exemption is lost if not used within the calendar year.
- These gifts can be made outright or in trust (with a small complexity).
- Also note that any payment for education or health care paid directly to the institution does not count against this annual exclusion.

Gifting strategies:

- Gift annually into a trust to buy life insurance and family receives proceeds tax free.
- 529 education savings plans which can grow tax-free if used for qualified educational expenses.
- Make in-kind gifts to beneficiaries in a lower tax bracket.

Using the **Increased** Lifetime Exemption

Current lifetime gifting exemption

- For high-net-worth individuals, there is an opportunity to make substantial gifts during your lifetime
- Federal exemption amount in 2021
 - \$11.7 million per person
 - \$23.4 million married couple
- Under current law, the exemption amount will sunset in 2026
 - \$5 million per person (indexed for inflation)


Legislation may impact exemption availability

- Laws could change bringing these increased exemptions down prior to 2026
- Grantor Trust rules may be impacted as well impacting many of the strategies commonly used to take advantage of the gift and estate tax exemption.

Estate Plan Review

Review your estate plan at year-end:

- Collect documents and ensure all necessary documents are in place
 - Will
 - Trust
 - Powers of attorney for health or financial matters
 - Beneficiary designations and TOD account titling
- Ensure that the dispositive/distribution provisions of your documents accomplish your goals
- Review the individuals you have nominated to serve various roles
 - Look at your executor and trustee nominations as well as Powers of Attorney and health care surrogates
- Review beneficiary designations and Transfer-on-Death (TOD) account titling
 - Review beneficiary designations for retirement accounts and life insurance policies
 - Review TOD account titling for bank accounts and securities
 - These designations can be every bit as impactful as the Will and Revocable Trust



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