What your business needs to know for 2021 taxes

With Carlos Dias

(407) 801-2244
carlos@diaswealth.com
https://calendly.com/carlosdiasjr

Connect with Carlos

https://www.linkedin.com/in/carlosdiasjr/

https://www.facebook.com/CarlosADiasJr/

https://twitter.com/carlosadiasjr

https://www.instagram.com/carlosadiasjr/

Key takeaways:

- Tax changes to expect from the Biden administration
- What to consider for the 2021 fiscal year
- Deductions your business might be missing
- Maximizing your deductions with Divvy

Biden's Tax Plan

Overview of Biden's Tax Plan

- According to Tax Policy Center, President Biden's tax plan would generate about $4.3 trillion in tax revenue over a 10-year period.

- In 2022, expected tax cut for middle-income households is about $680 larger and about $6,000 smaller on households with incomes over $788,000.

Tax Policy Center "TaxVox: Campaigns, Proposals, and Reforms Deductions"
(https://www.taxpolicycenter.org/taxvox/tpc-revises-its-revenue-estimate-bidens-tax-plan-downward-21-trillion-over-10-years)

Overview of Biden’s Tax Plan

- Currently, the majority of Biden’s proposals are preliminary and require congressional action as well as budget approval.

- Most will not likely be implemented (or diluted).

- American Rescue Plan Act changed Child and Dependent Care Tax Credit and Child Tax Credit amounts.

Overview of Biden's Tax Plan

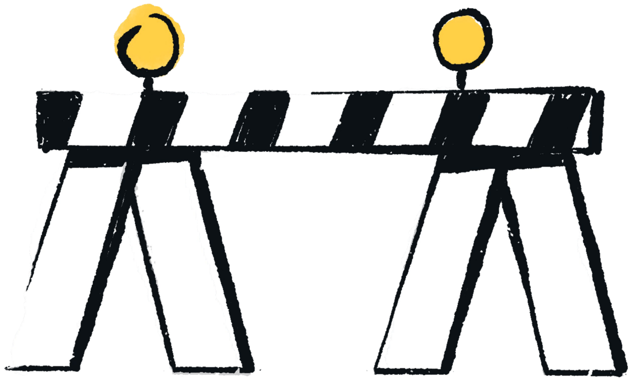
- Needs clarification on the term "anyone" if it means individuals, married couples, or both.

- According to the Penn Wharton Budget Model, 2% of all families would see their taxes increase under the Biden tax plan, with almost all of them in the top 5% by income.

Penn Wharton Budget Model (https://budgetmodel.wharton.upenn.edu/issues/2020/9/14/biden-2020-analysis)

Possible Changes to Trump Tax Cuts

- Possible changes include:
    - Increase top individual federal income tax rate
    - Increase top corporate federal income tax rate
    - Eliminate the pass-through deduction
    - Cap tax deductions
    - Increase in child tax credits
    - Caregiver and long-term care tax credits
    - Keep surtax on net investment income



JoeBiden.com "A Tale Of Two Tax Policies: Trump Rewards Wealth, Biden Rewards Work" (https://joebiden.com/two-tax-policies/)

Possible Changes to Trump Tax Cuts

- Increase long-term capital gains and qualified dividends
- Eliminate of 1031 exchanges
- Eliminate step-up in basis for inherited assets
- Eliminate carried interest

- Biden’s primary goal is not to increase taxes or limit deductions for taxpayers with an individual annual income of less than $400,000.

JoeBiden.com "A Tale Of Two Tax Policies: Trump Rewards Wealth, Biden Rewards Work" (https://joebiden.com/two-tax-policies/)

Increase Individual Tax Rate

- Biden’s tax plan would increase the top ordinary individual federal income tax rate to 39.6% (currently at 37%).

- If ordinary income tax rates don’t change any sooner, they will automatically revert back to pre-Tax Cuts and Jobs Act after December 31, 2025.

Increase Corporate Tax Rate

- Tax Cuts and Jobs Act reduced the federal corporate tax rate from 35% to 21%.

- Biden’s tax plan would increase the federal corporate tax rate (e.g. C-Corporations) to 28% (currently at 21%).

- Even with a federal corporate tax increase, this would still be a net 7% win for C-Corporations.

State Corporate Tax Rate

State	State Corporate Tax Rate
Alabama	6.5%
Alaska	9.4%
Arizona	4.9%
Arkansas	6.5%
California	8.84%
Colorado	4.63%
Connecticut	7.5%
District of Columbia	8.25%
Delaware	8.7%
Florida	4.458%
Georgia	5.75%
Hawaii	6.4%

State	State Corporate Tax Rate
Idaho	6.925%%
Illinois	9.5%
Indiana	5.5%
Iowa	12%
Kansas	7%
Kentucky	5%
Louisiana	8%
Maine	8.93%
Maryland	8.25%
Massachusetts	8%
Michigan	6%
Minnesota	9.8%

State Corporate Tax Rate

State	State Corporate Tax Rate
Mississippi	5%
Missouri	4%
Montana	6.75%
Nebraska	7.81%
New Hampshire	8.84%a7.7%
New Jersey	10.05%
New Mexico	5.9%
New York	6.5%
North Carolina	2.5%
North Dakota	4.31%
Oklahoma	6%
Oregon	7.6%

State	State Corporate Tax Rate
Pennsylvania	9.99%
Rhode Island	7%
South Carolina	5%
Tennessee	6.5%
Utah	4.95%
Vermont	8.5%
Virginia	6%
West Virginia	6.5%
Wisconsin	7.9%

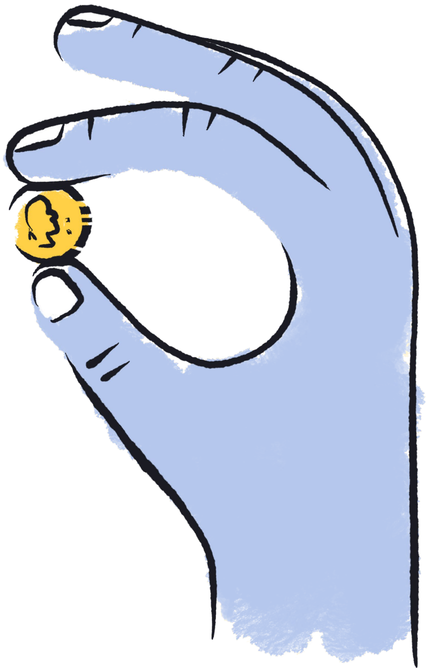
* Nevada, Ohio, South Dakota, Texas, Washington, and Wyoming have no state corporate taxes.

Eliminate Pass-Through Deduction

- In 2021, QBI deduction threshold for individuals is $164,900 ($329,800 for married couples).

- Specified Service Trade or Business (e.g. doctors, attorneys, professional athletes, and financial advisors) have phase out amounts.

- Non-Specified Service Trade or Business still receives QBI deduction.



Eliminate Pass-Through Deduction

- Biden’s tax plan would eliminate the Qualified Business Income (or “QBI”) pass-through deduction for business owners (e.g. LLCs, S-Corporations, Partnerships, and Sole Proprietors) with individual annual income above $400,000.

- Those with individual annual income above $400,000 would basically be treated as if they were Specified Service Trade or Business.

Cap Tax Deductions

- Biden’s tax plan would cap all itemized deductions to 28% (currently no limitations).

- Those currently in the 37% tax bracket will be the most impacted.

- Itemized deductions will automatically revert back to lower pre-Tax Cuts and Jobs Act after December 31, 2025.

Cap Tax Deductions

- Those in the 32% or higher tax bracket will be negatively affected.
- Pease Limitation previously suspended under the Tax Cuts and Jobs Act would be reinstated.
- State and Local Tax (or “SALT”) cap of $10,000 with the Tax Cuts and Jobs Act would be repealed.

Increase Child Tax Credits

- For 2021, Child and Dependent Care Tax Credit for qualified expenses is $8,000 for one child up to $16,000 for multiple children (phases out after $125,000 and completely at $400,000).

- For 2021, Child Tax Credit is $3,000 for children ages 6 to 17 and $3,600 for children under age 6 (phases out at $75,000 for single individuals or $150,000 for married couples filing jointly).

Caregiver Tax Credit

- Biden’s tax plan would provide a new tax credit up to $5,000 for individuals who provide informal care.

- Modeled off legislation supported by AARP.

- Caregivers would not have to live with the individual they are assisting.

Long-Term Care Insurance Tax Benefits

- Biden’s tax plan would increase the tax benefits for older Americans who choose to buy long-term care insurance.

- Needs clarification on if only applies to long-term care insurance or includes life insurance policies or annuities with long-term care rider.

- Possibly only partnership policies.

Keep Net Investment Income Tax

If 2021 Modified Adjusted Gross Income (or “MAGI”) is:

Filing Status	Threshold Amount
Married filing jointly	$250,000
Married filing separately	$125,000
Single	$200,000
Head of household (with qualifying person)	$200,000
Qualifying widow(er) with dependent child	$250,000

IRS "Questions and Answers on the Net Investment Income Tax"
(https://www.irs.gov/newsroom/questions-and-answers-on-the-net-investment-income-tax)

Increase Capital Gains and Dividend Tax Rates

- Biden's tax plan would increase both long-term capital gains and qualified dividends to 39.6% (plus 3.8% surtax on net investment income) for individuals with an annual income above $1 million (currently 20% plus 3.8% surtax on net investment income).

- Needs clarification on whether it's based on gross, adjusted, or total income.

Eliminate 1031 Exchanges

- Biden's tax plan would eliminate 1031 exchange for individuals with an annual income above $400,000 (currently no limitations on income).

- Possibly subject to ordinary income tax rates on real estate sales if the capital gains are above the $1 million threshold.

- Needs clarification as details are still unclear.

Eliminate Step-Up in Basis on Inherited Assets

- Currently, stocks, bonds, mutual funds, real estate and other investment property receive a “step-up” in basis at the owner's death (original cost basis is adjusted to its new inherited value).

- Biden’s tax plan would eliminate step-up in basis except what is classified as Income in Respect of a Decedent (untaxed income that owner earned during their lifetime).

Eliminate Carried Interest

- Tax Cuts and Jobs Act retained long-term capital gain treatment for carried interest if held for 3 years or longer.

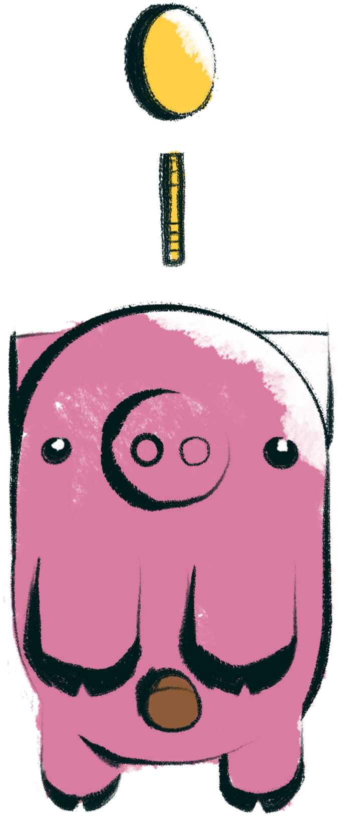
- Biden’s tax plan would eliminate carried interest for individuals with an annual income above $1 million.

- Possibly reverts to ordinary income tax rates.

Social Security and Payroll Taxes

- In 2021, the Social Security payroll tax is 6.2% on both the employee and employer on wages up to $142,800.

- Self-employed individuals pay 12.4% of their net profits.



Social Security and Payroll Taxes

- Biden's tax plan would include additional Social Security payroll tax of 6.2% on both employer and employee with earned income of $400,000 or more.

- No additional Social Security tax would be added on wages between $142,800, up to $400,000.

- Needs clarification as details are still unclear.

Incentives for Retirement Savings

- In 2021, defined contribution plans such as 401(k)s offer more incentives for high-income earners to save versus middle and low-income.

- For example, individual earning $1 million per year in the 37% tax bracket would receive $370 deduction per $1,000 saved; individual earning $50,000 per year in the 22% tax bracket would receive $220 deduction per $1,000 saved.

Incentives for Retirement Savings

- Biden’s tax plan would eliminate the current “bracket step-up deduction” and replace with 26% “flat-tax credits.”

- Needs clarification and will be “revenue-neutral,” effectively decreasing deductions for those in higher tax brackets.

Incentives for Retirement Savings

Example #1

- Individual contributes $10,000 to their retirement plan
- Currently in 12% marginal tax bracket

Can deduct **$2,600** ($10,000 x 26% = $2,600) for a $10,000 contribution, effectively increasing it by another **14%** (26% - 12% = 14%).

Incentives for Retirement Savings

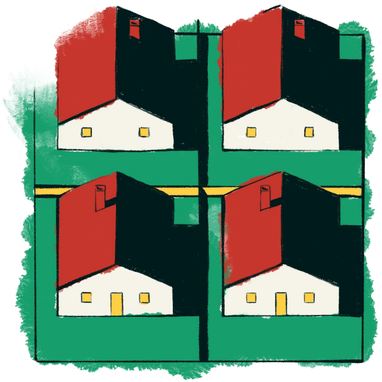
Example #2

- Individual contributes $10,000 to their retirement plan
- Currently in 37% marginal tax bracket

Can deduct **$2,600** ($10,000 x 26% = $2,600) for a $10,000 contribution, effectively decreasing it by another **11%** (37% - 26% = 11%).

Lower Estate Tax Exemptions

- In 2021, estate tax exemption is $11.7 million for individuals and $23.4 for married couples (includes portability).
- Gift tax exemption is $11.7 million per individual.
- Generation-Skipping Transfer Tax (beneficiary at least 37 ½ years younger) is $11.7 million per individual.



Lower Estate Tax Exemptions

- Estate tax exemptions will automatically revert back to lower pre-Tax Cuts and Jobs Act after December 31, 2025 (indexed for inflation).

- Estates above exemption amounts are taxed at 40%.

Federal Estate Tax Rates

2021 estate tax brackets are as follows:

Income Level	Tax Rate
$0 to $10,000	$23,800 base plus 30% on excess
$10,001 to $20,000	$38,800 base plus 32% on excess
$20,001 to $40,000	$70,800 base plus 34% on excess
$40,001 to $60,000	$8,200 base plus 24% on excess
$60,001 to $80,000	$13,000 base plus 26% on excess
$80,001 to $100,000	$18,200 base plus 28% on excess

IRS Revenue Procedure 2020-45 (https://www.irs.gov/pub/irs-drop/rp-20-45.pdf)

Federal Estate Tax Rates

2021 estate tax brackets are as follows:

Income Level	Tax Rate
$100,001 to $150,000	$23,800 base plus 30% on excess
$150,001 to $250,000	$38,800 base plus 32% on excess
$250,001 to $500,000	$70,800 base plus 34% on excess
$500,001 to $750,000	$155,800 base plus 37% on excess
$750,001 to $1 million	$248,300 base plus 39% on excess
Over $1 million	$345,800 base plus 40% on excess

IRS Revenue Procedure 2020-45 (https://www.irs.gov/pub/irs-drop/rp-20-45.pdf)

State Estate Tax Exemption Amounts

2021 estate tax brackets are as follows:

State	Exemption Amount
Connecticut	$7,100,000
District of Columbia	$4,000,000
Hawaii	$5,490,000
Illinois	$4,000,000
Maine	$5,800,000
Maryland	$5,000,000
Massachusetts	$1,000,000

State Estate Tax Exemption Amounts

2021 state estate tax exemption amounts are as follows:

State	Exemption Amount
Minnesota	$3,000,000
New York	$5,850,000
Oregon	$1,000,000
Rhode Island	$1,579,922
Vermont	$5,000,000
Washington	$2,193,000

State Inheritance Tax Rates

2021 state estate tax exemption amounts are as follows:

State	Exemption Amount
Iowa	0% to 15%
Kentucky	0% to 16%
Maryland	0% to 10%
Nebraska	1% to 18%
New Jersey	0% to 16%
Pennsylvania	0% to 15%

Lower Estate Tax Exemptions

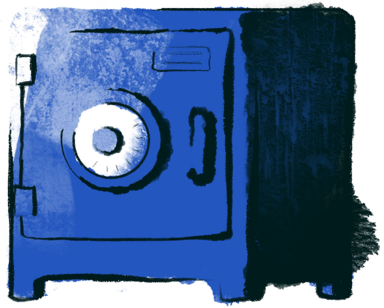
- Biden’s tax plan would possibly regress to 2009 amounts of $3.5 million for individuals and $7 million for married couples (no portability).

- Gift tax exemption would return back to $1 million for individuals and $2 million for married couples.

- Estates above exemption amounts would be taxed at 45%.

Securing a Strong Retirement Act of 2020

- The Securing a Strong Retirement Act of 2020 (or "SECURE Act 2.0") includes:
  - Expanding automatic enrollment in retirement plans;
  - Enhancement of 403(b) plans;
  - Increase in age for required beginning date for mandatory distributions to age 75;
  - Deferral of tax for certain sales of employer stock to ESOPs sponsored by S-Corporations (currently C-Corporations);



House Committee on Ways and Means "The Securing a Strong Retirement Act of 2020"
(https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/2.0Sectionbysection_final.pdf)

Securing a Strong Retirement Act of 2020

- Indexing IRA catch-up limit;
- Higher catch-up contribution to apply at age 60;
- Treatment of student loan payments as elective deferrals for purposes of matching contributions;
- Remove RMD barriers for life annuities;
- Qualifying Longevity Annuity Contract (or “QLAC”) limit up to $200,000 with spousal survival rights;
- Retirement plan distributions for charitable purpose;
- and more.

House Committee on Ways and Means "The Securing a Strong Retirement Act of 2020"
(https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/2.0Sectionbysection_final.pdf)

Additional Deductions

Business Car Deduction

- Car only used for business purposes can be deducted in its entirety (subject to limits).
- Car used for both business and personal purposes, its business use can only be deducted.
- The two methods include (Publication 463):
  - Standard mileage rate; or
  - Actual expenses.

IRS Topic No. 510 “Business Use of Car” (https://www.irs.gov/taxtopics/tc510)

Business Car Deduction

- For standard mileage rate, car must be leased or owned and:
  - Must not operate 5 or more cars at the same time;
  - Must not have deducted depreciation using any method other than straight-line
  - Must not have claimed a Section 179 deduction
  - Must not have claimed special depreciation allowance
  - Must not have claimed actual expenses after 1997 for a lease

IRS Topic No. 510 “Business Use of Car” (https://www.irs.gov/taxtopics/tc510)

Business Car Deduction

- For actual expenses, determine costs with business miles, including gas, oil, repairs, tires, insurance, registration fees, licenses, and depreciation (or lease payments).

- Modified Accelerated Cost Recovery System (or "MACRS") only depreciation method after 1986.

- Special rules applicable to leased cars.

IRS Topic No. 704 "Depreciation" (https://www.irs.gov/taxtopics/tc704)

Home Office Deduction

- For self-employed individuals and small business owners.

- Tax Cuts and Jobs Act disallowed employees to deduct home office expenses.

- The two options include:
  - Simplified method (up to $1,500) or
  - Regular method (actual expenses)

IRS "Home Office Deduction" (https://www.irs.gov/businesses/small-businesses-self-employed/home-office-deduction)

Home Office Deduction

- Expenses may include mortgage interest, insurance, utilities, repairs, and depreciation.

- Based on percentage of home used for business.

- The two basic requirements for home to qualify as a deduction:
  - Used regularly and exclusively for business and
  - It's the principal place of business

IRS "Home Office Deduction" (https://www.irs.gov/businesses/small-businesses-self-employed/home-office-deduction)

Health Insurance Deduction

- Self-employed individuals and small business owners can deduct health insurance premiums.

- Deductible health insurance premiums include:
  - Employees
  - Spouse
  - Dependents and
  - Children under age 27 as of end of year.

IRS Publication 535 (https://www.irs.gov/publications/p535)

Health Insurance Deduction

- One of the following statements must be true:
  - Self-employed and had a net profit for the year reported on Schedule C or Schedule F.
  - Partner with net earnings from self-employment for the year reported on Schedule K-1.
  - Used one of the optional methods to figure net earnings from self-employment on Schedule SE.
  - Wages from S-Corporation with more than 2% shareholder (premiums paid are wages).

IRS Publication 535 (https://www.irs.gov/publications/p535)

Health Insurance Deduction

- Self-employed individuals and small business owners can deduct all Medicare premiums including:
  - Medicare Part A and B
  - Medigap
  - Medicare Advantage (or “Part C”)
  - Part D

- Can include spouse.

IRS Publication 535 (https://www.irs.gov/publications/p535)

Health Insurance Deduction

- Profitable self-employed individuals can deduct Medicare premiums on Schedule 1 (“above-the-line” deduction), effectively lowering AGI.

- Can’t deduct more than earned.

- Self-employed individuals with no profit can still itemize on Schedule A, subject to 7.5% AGI.

IRS Publication 535 (https://www.irs.gov/publications/p535)

Business Meals

- Taxpayer Certainty and Disaster Tax Relief Act of 2020 as part of Consolidated Appropriations Act, 2021 allows 100% deduction in 2021 and 2022 for business meal expenses (increase from 50%).

- Section 274 was amended by Tax Cuts and Jobs Act of 2017 effective January 1, 2018 or later.

- Includes any carry-out or delivery meals.

The COVID-Related Tax Relief Act of 2020 (https://crsreports.congress.gov/product/pdf/R/R46649)

Solo 401(k) vs. SEP IRA

Here are the differences between a Solo 401(k) and SEP IRA:

Account Type	Employer Contributions	Employee Contributions	Formation Date	Loan Provision	Roth Contributions	Catch-Up Contributions
Solo 401(k)[1]	Yes	Yes	12/31	Yes	Yes	Yes
SEP IRA[2]	Yes	No	Business Tax Return Filing	No	No	No

1. IRS “SEP IRA” (https://www.irs.gov/retirement-plans/plan-sponsor/simplified-employee-pension-plan-sep)
2. IRS “One-Participant 401(k) Plans” (https://www.irs.gov/retirement-plans/one-participant-401k-plans)

Health Savings Account

- Health Savings Account (or “HSA”) is owned by employee and funded by employee or employer.

- Requires high-deductible health insurance plan.

- In 2021, the maximum contribution limits are $3,600 for employee and $7,200 for family.

- Form 5498 lists contributions and paid expenses.

IRS Publication 969 (https://www.irs.gov/publications/p969)

Flexible Spending Arrangement

- Flexible Spending Arrangement (or “FSA”) is owned by employer and funded by employer and employee.

- Tax-free for eligible out-of-pocket medical expenses.

- In 2021, maximum contribution limit is $2,750.

IRS Publication 969 (https://www.irs.gov/publications/p969)

Health Reimbursement Arrangement

- Health Reimbursement Arrangement (or “HRA”) is owned and funded by employer.

- Employer match and interest are tax-free for eligible out-of-pocket medical expenses.

- There are no maximum contribution limits (depends on employer’s rules).

IRS Publication 969 (https://www.irs.gov/publications/p969)

HSA vs. FSA vs. HRA

Here are the differences between an HSA, FSA, and HRA:

Account Type	Ownership	Contributions & Tax Deductibility	IRS Reportable	Health Insurance Requirements	Portable
HSA	Employee	Employer, Employee, and Family	Yes	Yes (High Deductible)	Yes
FSA	Employer	Employer & Employee	No	No	No
HRA	Employer	Employer	No	Depends	No

IRS Publication 969 (https://www.irs.gov/publications/p969)

Health Savings Account

- HSAs offer three tax benefits:
    - **Tax-deductible contributions**: Reduces taxable income;
    - **Contributions grow tax-deferred**: No tax on interest as long as it remains in HSA; and
    - **Withdrawals possibly tax-free**: Withdrawals for qualified medical expenses (including long-term care) are tax-free.

Cafeteria Plan

- IRS Section 125 allows employees pay for certain qualified medical expenses on a pre-tax basis.
- Must be permitted to choose among at least one taxable benefit and one qualified benefit.
- Employer contributions are typically made pursuant to salary reduction agreements.

IRS Section 125: Cafeteria Plans (https://www.irs.gov/pub/irs-drop/n-05-42.pdf)

Cafeteria Plan

- Not considered wages for federal income taxes.

- Qualified benefits include the following:
  - Accident and health benefits
  - Adoption assistance
  - Dependent care assistance
  - Group-term life insurance coverage
  - Health savings accounts, including distributions to pay long-term care services

IRS Section 125: Cafeteria Plans (https://www.irs.gov/pub/irs-drop/n-05-42.pdf)

Long-Term Care Insurance Tax Benefits

- Premiums for “qualified” long-term care insurance are tax deductible along with other unreimbursed medical expenses exceed 7.5% of the insured's adjusted gross income (or “AGI”).

- Self-employed individuals can deduct the premium as long as business made a profit (“above-the-line” deduction).

Long-Term Care Insurance Tax Benefits

2021 long-term care tax-deductible premiums are as follows:

Age at the end of the tax year	Maximum deductible premium
40 or under	$450
41 to 50	$850
51 to 60	$1,690
61 to 70	$4,520
71 or older	$5,640

IRS Revenue Procedure 2020-45 (https://www.irs.gov/pub/irs-drop/rp-20-45.pdf)

Long-Term Care Insurance Tax Benefits

- Long-term care insurance contract must meet all the following requirements:
    - It must be guaranteed renewable.
    - It must provide that refunds, other than refunds on the death of the insured or complete surrender or cancellation of the contract, and dividends under the contract may be used only to reduce future premiums or increase future benefits.

Long-Term Care Insurance Tax Benefits

- It must not provide for a cash surrender value or other money that can be paid, assigned, pledged, or borrowed.
- It generally must not pay or reimburse expenses incurred for services or items that would be reimbursed under Medicare, except where Medicare is a secondary payer or the contract makes per diem or other periodic payments without regard to expenses.

Long-Term Care Insurance Tax Benefits

Example:

- Self-employed individual age 62 with an S-Corp
- Pays $4,300 per year for long-term care insurance policy

The entire amount is fully deductible as part of the
"Self-Employed Health Insurance Deduction."

Long-Term Care Insurance Tax Benefits

- HSA can be used to pay or be reimbursed for long-term care insurance premiums up to the age-based amount.

- With HSA, there's no need to itemize and meet the 7.5% of AGI threshold.

- Might be an optimal solution for those that don't itemize.

Defined Benefit Pension Plans

- Defined benefit pension plans include:
  - Traditional defined benefit plan (based on an employee's earnings, years of service, and age);
  - Cash balance plan (combination of investment with lifetime annuity); and
  - 412(e)(3) (permanent life insurance and annuities).

- Typically, 412(e)(3) can generate larger tax deductions than traditional defined benefit plans.

Why Divvy

Maximize deductions with Divvy

- Spenders share the burden of categorization—transactions are reconciled within seconds
- With receipt upload from the mobile app, you have all the documentation you need
- Free corporate cards let you separate business spend from personal for faster EOY accounting

Maximize deductions with Divvy

- Let’s take a look at the Divvy platform

(407) 801-2244
carlos@diaswealth.com
https://calendly.com/carlosdiasjr

(801) 850-2743
weston.hadlock@divvypay.com
https://getdivvy.com

Divvy®