GBQuarterly: Year-End Individual Tax Update

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Agenda

- Overview of SECURE Act
- SECURE Act Planning Considerations
- Overview of CARES Act
- Other Tax Planning & Year-end Charitable Giving Strategies
- Estate & Gift Tax Update & Planning
- Odds and Ends for 2020 and Beyond

Setting Every Community Up for Retirement Enhancement (SECURE) Act

- SIGNIFICANT changes to the retirement planning landscape
- Was passed by attaching to a year-end appropriations package
- Signed into law by President Donald Trump on December 20, 2019

SECURE Act Overview: Changes to IRAs

- Raised retirees' beginning age of RMDs from IRAs and other qualified plans from 70 ½ to 72
- For tax years beginning after December 31, 2019, the SECURE Act eliminated "stretch" IRAs

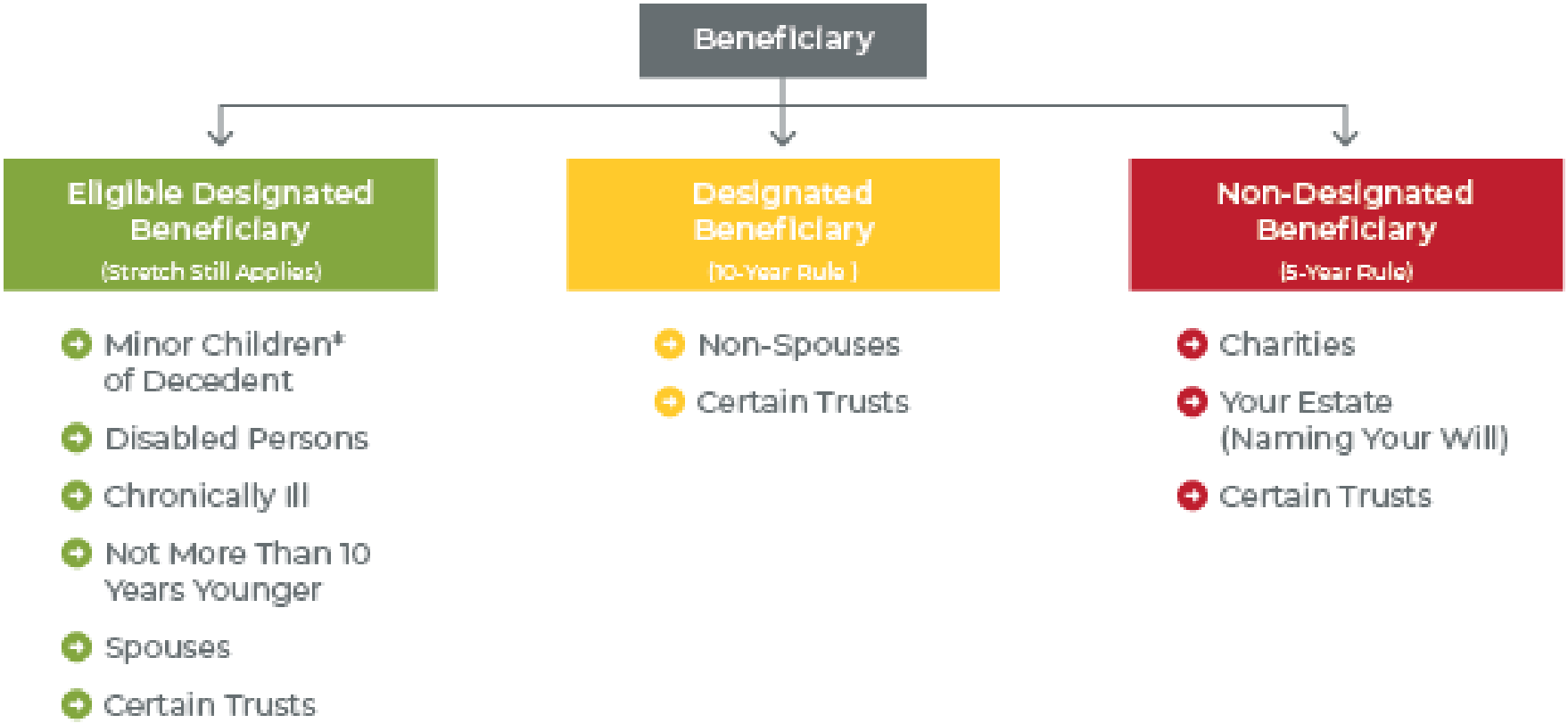
How the SECURE Act Changes Post-Death Distribution Rules For Stretch IRAs

- Prior to SECURE Act, beneficiaries of IRAs and employer plans fell into two categories: Designated Beneficiaries and Non-Designated Beneficiaries.

- The SECURE Act changes this by effectively splitting the pre-SECURE Act group of "Designated Beneficiaries" into two sub-groups; Eligible Designated Beneficiaries, and Designated Beneficiaries who are NOT Eligible Designated Beneficiaries (i.e., Non-Eligible Designated Beneficiaries).

- Thus, there are now a total of three categories of IRA (and other retirement account) beneficiaries: Non-Designated Beneficiaries, Eligible Designated Beneficiaries, and Non-Eligible Designated Beneficiaries.

IRA Beneficiaries After the SECURE Act



Source: Michael Kitces, www.kitches.com

New 10-Year Rule for Distributions

- SECURE Act subjects Non-Eligible Designated Beneficiaries to a new 10-Year Rule. This 10-Year Rule requires that such beneficiaries distribute the balance of an inherited account by the end of the 10th year after the year of death.

- For example, a Non-Eligible Designated Beneficiary who inherits an IRA during 2020 would have 10 years to distribute the balance of their inherited account beginning on January 1, 2021 (the year after the year of death) and ending on December 31, 2030.

- A Non-Eligible Designated Beneficiary could choose to take the distributions ratably or take a large one-time distribution in the final 10th year following death or anything in between.

Planning Around the 10-Year Rule

Planning Around the Elimination of the "Stretch" IRA:

- Increase the number of beneficiaries to spread out income subject to 10-year rule
- Consider giving more weight to beneficiaries' tax situations
- Bypass the spouse at the first death to create two separate 10-year distribution windows
- Use partial Roth conversions to reduce taxes for future beneficiaries
- Utilize a Charitable Remainder Trust

SECURE Act Overview: For Students

- Allows distributions from a 529 plan to be used to pay principal and interest on student loans of the designated beneficiary or the beneficiary's sibling, up to a lifetime limit of $10,000

- 529 plans may now be used to pay for fees, books, supplies, and equipment required for participation in certain apprenticeship programs

- Taxable stipends and non-tuition fellowships are treated as compensation for purposes of making deductible IRA contributions, allowing graduate students to begin saving for retirement

SECURE Act Overview: For Qualified Employee Retirement Plans

- Effective for distributions made after Dec. 31, 2019, penalty-free withdrawals from qualified plans may be made for birth or adoption expenses, up to $5,000 per child. The distribution must be taken within the one-year period beginning on the date of birth or the date on which a legal adoption is finalized. The withdrawal can be repaid to the plan.

- Effective for tax years beginning after Dec. 31, 2019, the act provides a general business credit under new Sec. 45T of $500 to employers that establish a qualified employer plan. The plan must have an automatic enrollment feature, and the credit is available for up to three years. In addition, the act increased the maximum Sec. 45E credit for qualified startup costs of pension plans offered by small employers to $5,000.

- Employers may treat a qualified retirement plan they adopt after the end of a tax year, but no later than the due date (including extensions) of their federal income tax return for the tax year as having been adopted as of the last day of the tax year, effective for plans adopted for tax years beginning after Dec. 31, 2019.

SECURE Act – Kiddie Tax Changes

- Retroactively eliminated requirement to use trust tax brackets back to 2018
- Back to being taxed at parents' marginal rate
- For 2020 the top trust rate of 37 percent applies to ordinary income starting at $12,951 and for individuals doesn't start until income exceeds $518,400.
- The top trust tax rate of 20 percent for qualified dividends and capital gains applies to income starting at $13,151 and for individuals doesn't start until income exceeds $441,450.

SECURE Act Overview: Tax Extenders

- Discharge of certain qualified principal residence indebtedness is excluded from gross income
- Allowance of mortgage insurance premium deduction
- Deduction for qualified tuition and related expenses
- AGI threshold for deducting qualified medical expenses to remain at 7.5%
- Other incentives for economic growth, energy production and green/renewable initiatives

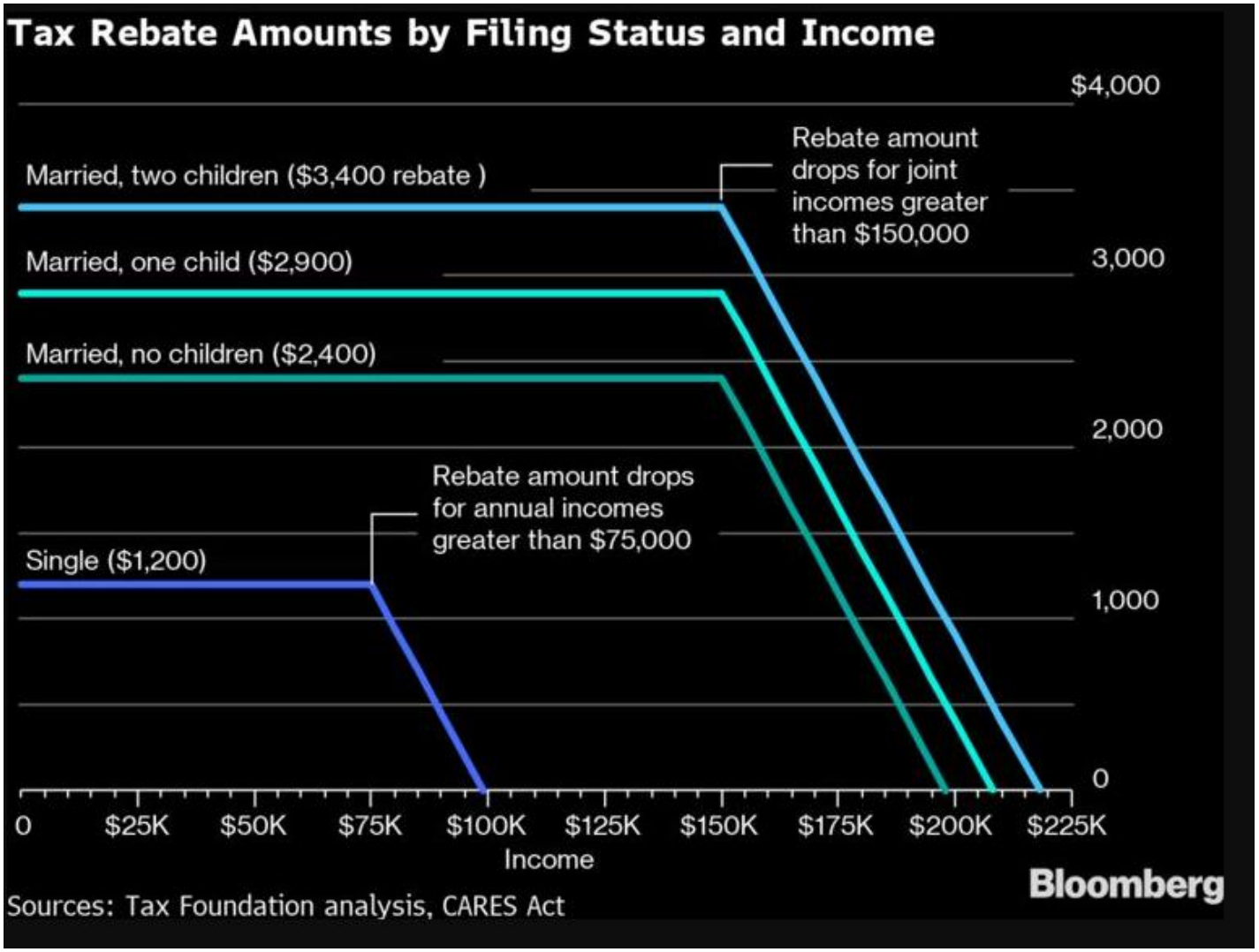
CARES Act: Overview

- The Coronavirus Aid, Relief, and Economic Security (CARES) Act was passed on March 27th
- $2 trillion economic relief package
- Economic Impact Payments
- Changes to charitable contributions and retirement plans
- Changes to net operating loss rules and excess business loss limitations

CARES Act: Economic Impact Payments

- Eligible individuals are allowed a credit of $1,200 ($2,400 for joint filers), plus $500 for each qualifying child, for the first taxable year beginning in 2020
- Under Section 6428(a), is treated as refundable credit and eligible recipients received an "advance payment" of this credit
- If advance payment is less than actual credit, the taxpayer will receive additional benefit on 2020 return
- If advance payment is more than actual credit, there is no mechanism for the taxpayer to either report the excess advance payment as income or repay excess

CARES Act: Economic Impact Payments



CARES Act: Economic Impact Payments

- On Oct 5, IRS extended deadline to register for EIP to November 21, 2020
- Only available to those that have not received their EIP and don't normally file a tax return
- Use the "Non-Filers: Enter Info Here" tool on IRS.gov
- If you didn't receive a payment, check:
  - Income levels didn't exceed thresholds
  - Claimed as dependent on someone else's return (example of college-aged student)
  - SSA recipients – check accounts where SSA is deposited

CARES Act: Charitable Contributions

- Individuals that do not itemize can take a deduction of $300 against adjusted gross income (AGI) for 2020
- $300 limit is per return, not per person (per draft instructions released 10/23/20)
- Must be qualified charitable contribution
  - Made in cash
  - For which a charitable contribution deduction is otherwise allowed
  - Which is made to certain publicly supported charities (not to non-operating private foundation or a donor advised fund)
- For those that itemize, AGI limitation of 60% was suspended for qualifying cash contributions
  - Any excess is still carried forward as a charitable contribution for each of the succeeding five years

CARES Act: Retirement Plan Changes

- Required Minimum Distributions (RMD) requirement waived for calendar year 2020

- Eligible individuals can withdraw up to $100,000 for coronavirus-related purposes without incurring the usual 10% early distribution penalty
  - Taxpayers may elect to ratably spread the income over a 3-year period beginning with the 2020 tax year or include all in the year taken
  - May be repaid within 3 years – would need to amend prior year returns if repaid in year 3
  - Not subject to mandatory tax withholding

CARES Act: NOLs and Excess Business Loss Limitations

- Net operating losses for 2018, 2019, and 2020 can be carried back for up to 5 years and, if carried forward, can offset 100% (not 80%) of taxable income until 2021
- Come 2021, losses from pre-2018 can offset up to 100% of post-2020 taxable income, but losses from 2018 forward can only offset 80% of post-2020 income
- CARES Act suspended excess business loss limitation for 2018-2020
  - Old law (TCJA)– excess business losses limited to $250k for 2018-2025
  - If subject in 2018, needed to amend 2018 return
  - Still applies for tax years 2021-2025

Planning Strategies - Caveat

It's an unusual year for tax planning

- Uncertainty of tax rates in the future
- Taxpayers may have significant losses in 2020

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Biden's Tax Plan

- Increase top ordinary tax rate to 39.6%
- For income above $1MM, capital gains rate = ordinary rate
- Changes to itemized deductions
- Eliminate 199A deduction for high-income earners
- Expand existing tax credits and introduce new tax credits
- Modify payroll tax changes (including self employment tax)
- Modify estate and gift tax exclusions and rates

Accelerate Income to Lower Overall Tax Liability

- Convert a traditional IRA to a Roth IRA
- Elect out of installment sales
- Trigger an inclusion event for opportunity zone investments
- Harvest capital gains
- Forgo like-kind exchanges (actually or constructively receive cash or other boot, or sell replacement property)
- Exercise stock options
- Declare and pay c-corporation dividends

Planning Strategies - Traditional

Defer Income:

- Postpone Roth conversions
- Minimize retirement distributions
- Hold appreciated assets
- Convert taxable interest to tax-exempt interest
- Defer receipt of year-end bonuses to the extent possible

Accelerate Deductions:

- Increase contributions to 401(k) plans, pension plans, SEP, etc.
- Maximize contributions to a health savings account (HSA)
- Recognize capital losses in 2020
- "Bunching" strategy for charitable contributions or medical expenses

Year-end Charitable Giving Strategies

- Consider changes by CARES Act (100% AGI limit for cash donations in 2020)
- Donations of appreciated stock
- Qualified Charitable Distributions (QCD)
  - Donations out of IRA Required Minimum Distribution (RMD)
  - Especially powerful if taxpayer can't itemize
  - Direct transfer of funds from IRA payable to qualified charity
- Use a Donor-Advised Fund (DAF)
- Timing of donations

Method of Charitable Giving	Effective Date of Contribution
Gifts by check	Date the check is mailed
Gifts by credit card	Date the charge is made to the card

Gifting Appreciated Securities

- Limited to 30% of AGI
- Allows for more dollars to be contributed to a charity and avoids capital gains taxes
- Must be stock held for more than one year to deduct FMV (if held for less than one year, limited to tax basis)

Example if stock sold first:

- 1,000 Shares of ABC Company Stock worth $100,000 (basis is $50,000)
- If sold, capital gains taxes owed of 28.8% (including Ohio) on a $50,000 gain or $14,400, leaving remaining $85,600 to charity – a maximum tax savings of $31,672 (37%), a net savings of $17,272

Example if stock is donated to charity directly:

- 1,000 Shares of ABC Company Stock worth $100,000 (basis is $50,000)
- Income tax deduction of $100,000 – a tax savings of $37,000

IRA Charitable Rollover

- Allows taxpayers over age 70½ to shift as much as $100,000 of their required minimum distributions (RMDs) to qualified public charities
- Acts as an "above the line" deduction, by diverting otherwise taxable income directly to a qualified charity
- Generally not available for donor advised fund
- By excluding income, it may keep someone in a lower marginal tax bracket that also allows for Roth conversions, lower taxability of Social Security, etc.
- Provides state income tax benefit that would otherwise not be available for a charitable contribution

Donor Advised Funds (DAF)

- A separately identified fund or account that is maintained and operated by a 501(c)(3) organization (i.e. The Columbus Foundation, The Catholic Foundation, Fidelity, Schwab, etc.)
- Each DAF is composed of contributions made by separate donor
- Once the donor makes the contribution, the sponsoring organization has legal control over it
- The donor retains advisory privileges with respect to the distribution of funds and the investment of assets
- DAF provides a fairly affordable option to individuals to help them accomplish their charitable goals

Capital Gains Planning – Qualified Opportunity Zones Tax Benefits

- To be able to elect to defer gain, a taxpayer must generally invest in a QOF during the 180-day period beginning on the date of the sale or exchange giving rise to the gain.

- A QOF is, generally, an investment vehicle organized as a corporation or a partnership for the purpose of investing in QOZ property (other than another QOF), that holds at least 90% of its assets in QOZ property. Such property includes any QOZ stock, any QOZ partnership interest, and any QOZ business property.

- In the case of any investment in a QOF held by the taxpayer for at least 10 years and with respect to which the taxpayer makes a permanent exclusion election under Section 1400Z-2(c), the basis of the property equals the fair market value of the investment on the date that the investment is sold or exchanged.

Capital Gains Planning – Qualified Opportunity Zones Tax Benefits

Tax deferral	Tax deferral on capital gain invested in QOF to the earlier of the sale from the QOF or Dec. 31, 2026
10% tax reduction	Hold the fund for 5+ years
15% tax reduction	Hold the fund for 7+ years
Tax exemption	Hold the fund for 10+ years and appreciation of QOF investment (not the original gain, but post-acquisition gain) is exempt from taxes (sell by Dec. 31, 2047)
Tax basis in investment	Tax basis in investment is $0

Estate and Gift Tax Exemption

- For estates of decedents and gifts made after Dec. 31, 2017, and before Jan. 1, 2026, the base estate and gift tax exemption amount is doubled from $5 million to $10 million.
- The exemption amount is indexed for inflation and is $11.58 million for 2020 ($23.16 million per married couple). For 2021, these amounts increase to 11.7 million per person
- The increase in exemption amount also applies to generation-skipping transfer taxes.
- The annual gift tax exclusion amount is $15,000 for 2020 (no change from 2018 or 2019)

Odds and Ends for 2020 and Beyond

- QR bar codes on IRS notices to make payments easily online
- Amended tax returns for 2019 can be electronically filed
- IRS Notice 2020-46
  - Released June 11, 2020
  - If employees forgo sick, vacation, or personal leave time because of the COVID-19 pandemic, they do not need to pick up the value of the leave as income if the employer donates the value of this leave to charitable organizations that provide relief to victims of the COVID-19 pandemic
  - Employers may deduct these cash payments as a business expense or charitable contribution deduction

Odds and Ends for 2020 and Beyond

- Interest payments received for 13.9M individual taxpayers who timely filed their 2019 federal income tax returns and are receiving refunds (IR-2020-183)
  - Average of $18 per refund
  - Interest payments are taxable and should be included in income for 2020

- 2021 annual inflation adjustments were announced October 26th (see Revenue Procedure 2020-45)
  - Updated 2021 tax rate tables
  - Standard deduction for 2021 increases to $25,100 for MFJ, up from 24,800 in 2020
  - For single taxpayers, standard deduction will be 12,550, up from 12,400

Draft Form 1040 for 2020

- Released August 18, 2020
- Virtual currency question on page 1

At any time during 2020, did you receive, sell, send, exchange, or otherwise acquire any financial interest in any virtual currency? ☐ Yes ☐ No

- Charitable contribution above the line

10	Adjustments to income:				
a	From Schedule 1, line 22	10a			
b	Charitable contributions if you take the standard deduction. See instructions	10b			
c	Add lines 10a and 10b. These are your **total adjustments to income** ▶			10c	
11	Subtract line 10c from line 9. This is your **adjusted gross income** ▶			11	

- Recovery Rebate Credit on page 2

26	2020 estimated tax payments and amount applied from 2019 return			26	
27	Earned income credit (EIC)	27			
28	Additional child tax credit. Attach Schedule 8812	28			
29	American opportunity credit from Form 8863, line 8	29			
30	Recovery rebate credit. See instructions	30			
31	Amount from Schedule 3, line 13	31			
32	Add lines 27 through 31. These are your **total other payments and refundable credits** ▶			32	
33	Add lines 25d, 26, and 32. These are your **total payments** ▶			33	

Questions

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