GBQuarterly: Year-End Business Tax Update

December 8, 2021

Note

1. This presentation is intended to make participants aware of tax issues that may apply to this audience.

2. Information presented herein is not intended to be tax advice.

3. Please consult with a qualified practitioner for tax advice related to specific transactions.

Speakers

Chris Dean
Director, Tax & Business Advisory Services
614.947.5232
cdean@gbq.com

Kevin Dunn
Director, Tax & Business Advisory Services
614.947.5201
kdunn@gbq.com

Agenda

- Update on Build Back Better Act
- Tax Provisions in The Infrastructure Investment and Jobs Act
- Upcoming Changes to Current Tax Provisions
- Tax Planning Strategies

Build Back Better Act

Build Back Better Act was passed by the House of Representatives. There may be significant changes proposed during the Senate review, but here are some of the key business provisions:

Corporate Alternative Minimum Tax

- Imposes a minimum tax of 15% on book income over the corporate AMT foreign tax credits for corporations with 3-year average annual adjusted financial statement income in excess of $1 billion
- If a corporation is a member of an international financial reporting group with a common foreign parent, the corporate alternative minimum tax would apply to corporations with more than $100 million in average annual adjusted financial statement income

Surcharge on Corporate Stock Buybacks

- For public companies, a tax equal to 1 percent of the fair market value of stock that is repurchased
- Applies to any repurchase after December 31, 2021

Amortization of Research Expenses

- Under the TCJA, research expenses incurred in 2022 and later were no longer immediately deductible and would be capitalized and amortized over 5 years (15 if incurred outside the U.S.)
- The BBBA proposes to defer the effective date of this provision until Jan. 1, 2026

Build Back Better Act

Limitation on Deductions for Interest Expense

- For domestic corporations or foreign corporations with effectively connected income that are members of an international financial reporting group, limits the amount of interest expense deduction allocable to the domestic corporation to 110 percent of the net interest expense
- The domestic corporation's allocable interest expense is the group's interest expense multiplied by a ratio of the corporation's EBITDA to the group's EBITDA

FDII and GILTI Changes

- The FDII deduction is reduced from 37.5% to 24.8% resulting in an effective rate of 15.8%
- The GILTI deduction is reduced from 50% to 28.5% resulting in an effective rate of 15%
- GILTI would apply on a country-by-country basis rather than a global blended basis

Foreign Tax Credits

- Determined on a country-by-country basis
- The foreign tax credit computations would be done at a taxable unit level (controlled foreign corporation)
- The GILTI category foreign tax credit carryforward limitation is repealed

Build Back Better Act

Individual Provisions that may impact business owners of flow-through entities

Applies the 3.8% Net Investment Income Tax (NIIT) to Trade or Business Income of Certain High-Income Individuals

- Expands the 3.8% NIIT to include income derived in the ordinary course of a trade or business of the taxpayer when AGI is greater than $400,000 for individuals ($500,000 for joint filers)
- Excludes income already subject to self-employment taxes or wages subject to FICA
- Effective for taxable years beginning after Dec. 31, 2021

Surcharge on High-Income Individuals, Estates and Trusts

- Imposes a 5% surcharge on the modified Adjusted Gross Income (AGI) that exceeds $10 million for individuals and joint filers ($200,000 for a trust or estate)
- Imposes an additional 3% surcharge on modified AGI that exceeds $25 million for individuals and joint filers ($500,000 for a trust or estate)
- Effective for taxable years beginning after Dec. 31, 2021

Modification of Limitation on Deduction for State and Local Taxes (SALT)

- Increases the deduction for state and local taxes from $10,000 to $80,000 through 2030
- After 2030, the limitation reverts to $10,000 (under current law, the $10,000 limitation was set to sunset at the end of 2025)
- Effective for tax years 2021-2030

Infrastructure Investment and Jobs Act

Infrastructure Investment and Jobs Act was passed by both the House and Senate and signed into law by President Biden on November 15, 2021. The Act contained many non-tax provisions but below is the relevant tax provision:

Retroactive termination of employee retention credit

- Originally extended for qualified wages paid through December 31, 2021, the Infrastructure Investment and Jobs Act modified the definition of qualified wages to those paid through September 30, 2021.
  - As discussed in detail later, you can still claim the employee retention credit for wages paid from March 13, 2020, through September 30, 2021
- A recovery startup business that was added by the American Rescue Plan Act may still claim the employee retention credit for wages paid during the 3rd and 4th quarters of 2021
  - A recovery startup business is defined as:
    - A business that began operations after February 15, 2020, and
    - Had average gross receipts of less than $1 million using the principles of 448(c)(3)
  - Employee retention credit is limited to $50,000 per quarter
- It is unknown how the IRS will deal with taxpayers that were already claiming the employee retention credit in the 4th quarter

IRS Requiring Taxpayer's to Disclose More Information

New Schedules K-2 and K-3

- Requires partnership and S-corporations with international operations to provide additional information
- Notice 2021-39 provides transition relief to eliminate penalties if the taxpayer makes a good faith effort to comply with the requirements

Cryptocurrency Reporting

- Infrastructure Investment and Jobs Act expands the definition of broker subject to reporting requirements of Form 1099-B

Bank Reporting for Accounts with Annual Deposits and Withdrawals above Threshold

- Democrats originally included a provision to require banks to report annual deposits or withdrawals in excess of $600 in the Build Back Better Act
- Major uproar among banks

Upcoming Change to Current Tax Provisions

Tax Cuts and Jobs Act Provisions

163(j) – Interest Deduction Limitation

For 2021

- Generally limited to 30% of ATI which is defined as EBITDA For 2022
- The definition of ATI changes to be EBIT after 1/1/2022

100% Bonus Depreciation

- 2022 is the last year to claim 100% bonus depreciation on qualified property
- In 2023, only 80% of the cost of qualified property is eligible for bonus depreciation
- The rate decreased by 20% each subsequent year until phased out in 2027

Research and Development Expenses

- R&D expenses are currently a deductible expense
- Beginning in 2022, any amount of R&D expense (even if you don't claim an R&D credit) would be capitalized and amortized
  - U.S. R&D expenses are amortized on a straight-line basis over 5 years
  - R&D expenses related to foreign activities are amortized on a straight-line basis over 15 years

Upcoming Change to Current Tax Provisions

Tax Cuts and Jobs Act Provisions (Cont.)

Limitations on Excess Business Losses of Noncorporate Taxpayers (461(l))

- Provision will apply to losses in 2021 through 2026

CARES Act

Deferral of employment tax deposits and payments

- Employers were allowed to defer the deposit and payment of the employer's portion of Social Security taxes from March 27, 2020 through December 31, 2020
- 50% must be repaid by January 3, 2022, since December 31, 2021, is a legal holiday

Consolidated Appropriations Act of 2021

Meals and Entertainment Expenses

- Allowed a temporary exception to the 50% disallowance of meals and entertainment expenses incurred in 2021 and 2022
- IRS has issued two notices providing guidance on the application of this rule change
  - Notice 2021-25: Provides a definition of "restaurant" as a business that prepares and sells food and beverages
  - Notice 2021-63: Allows the meal portion of per-diem rate to qualify for 100% deduction

Tax Planning Strategies

Accounting Method Changes

Income Deferral

- Look at the possibility of deferring the recognition of advanced payments
  - IRS and Treasury released final regulations on December 21, 2020
  - IRS released Revenue Procedure 2021-34 for procedures on obtaining automatic consent for the method change
- Changing from the overall accrual method to cash method of accounting

Expensing prepaid expenses under the "12-month rule"

Depreciation Optimization

- **Bonus Provisions**
  - Evaluate capital expenditures in the upcoming year to maximize bonus depreciation before percentage begins to decrease in 2023
- **Cost Segregation Studies**
  - Ability to break out costs of major constructions projects into its components to optimize amounts eligible for bonus depreciation
- **Qualified Improvement Property**
  - CARES Act technical correction to define qualified improvement property as 15-year property
  - Since 15-year property, eligible for bonus depreciation

Tax Planning Strategies

Employee Retention Credit

What is the Employee Retention Credit?

- The Employee Retention Credit is a federal payroll tax credit that encourages businesses financially impacted by COVID-19 to keep employees on their payroll.
- For 2020, the refundable tax credit is 50% of qualified wages up to $10,000 for the year. For 2020, the maximum credit is $5,000 per employee for the year.
- For 2021, the refundable tax credit is 70% of qualified wages up to $10,000 *per quarter*. For 2021, the maximum credit is $7,000 per employee *per quarter* (so $28,000 total for all quarters).
- For 2020, for businesses with 100 or fewer full-time employees, qualified wages include wages and health plan expenses paid to ***all*** employees, whether they provided services or not. For 2021, the 100-person threshold was increased to 500 or fewer full-time employees.

Tax Planning Strategies

Employee Retention Credit (Cont.)

Who qualifies?

Employers in the private-sector and tax-exempt organizations that carry on a trade or business, and either:

- Have operations that were fully or partially suspended due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19; **OR**
- Experienced a significant decline in gross receipts during the calendar quarter. A significant decline means gross receipts for a calendar quarter in 2020 are less than 50% of gross receipts for the same calendar quarter in 2019. For 2021, a significant decline means gross receipts for a calendar quarter in 2021 are less than 80% of gross receipts for the same calendar quarter in 2019.

Consider evaluating the work opportunity tax credit if you are in the process of hiring new employees as your business recovers

Tax Planning Strategies

UNICAP

263A Final Regulations- issued in November 2018

- Eliminates the use of the Simplified Production Method of capitalizing costs for tax purposes for companies with average annual gross receipts exceeding $50 million

- Replaced the Simplified Production Method with a Modified Simplified Production Method
  - It requires the calculation of two ratios, pre-production and production
  - Pre-production ratio would be applied to raw materials and goods purchased for resale
  - Production ratio would apply to work-in-process and finished goods

- Companies are required to file an automatic accounting method change to elect the Modified Simplified Production Method

Questions

Contact Information

Chris Dean
Director, Tax & Business Advisory Services
614.947.5232
cdean@gbq.com

Kevin Dunn
Director, Tax & Business Advisory Services
614.947.5201
kdunn@gbq.com