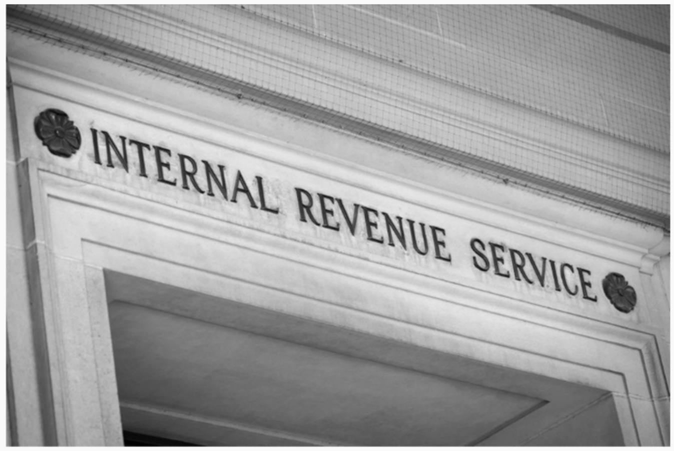
Welcome to Thursday Tax Topics!

JUNE 10, 2021



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Today's Discussion

- Advance Child Tax Credit Update
- Unemployment Correction Update
- New Form 941, Instructions
- Green Book and Tax Reform Proposals
- Quick Iowa Update

Advance Child Tax Credit News

- Families of 88 percent of U.S. children will receive advance payments of child tax credit, **beginning July 15** (May 17 news).
  - The American Rescue Plan increased the *maximum* Child Tax Credit **in 2021** to \$3,600 for children under the age of 6 and to \$3,000 per child for children between ages 6 and **17 (17 year olds are in)**.
  - **Eligible families will receive a payment of up to \$300 per month for each child under age 6 and up to \$250 per month for each child age 6 and above (~1/2 CTC).**
    - Payment will be made on the 15th of each month unless 15th falls on a weekend. (direct deposit, but some will receive paper check or card)
  - Payment will be based upon 2020 return, if available. If not, 2019 return.

Advance Child Tax Credit

- Increased amounts are reduced (phased out), for incomes over $150,000 for married taxpayers filing a joint return and qualifying widows or widowers, $112,500 for heads of household, and $75,000 for all other taxpayers.
  - The phase-out reduces the increase by $50 for each $1,000 by which the modified AGI exceeds the threshold amount.
    - The $2,000 portion of the credit continues to phase out using the thresholds of $400,000 for MFJ and $200,000 for other taxpayers.
    - https://www.irs.gov/credits-deductions/advance-child-tax-credit-payments-in-2021
- 2021 CTC is fully refundable, no earned income requirement.

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June 7 Announcement

- **IRS sending letters to more than 36 million families who may qualify for monthly Child Tax Credits**
- The letters are going to families who may be eligible based on information they included in either their 2019 or 2020 federal income tax return or who used the Non-Filers tool on IRS.gov last year to register for an Economic Impact Payment.
  - A second, personalized letter will follow giving an estimate of the monthly payment, which begins July 15.
  - Payment based upon 2020 return, unless it is not on file.
  - Dates: July 15, Aug. 13, Sept. 15, Oct. 15, Nov. 15 and Dec. 15.

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June 7 Announcement

- **Throughout the summer**, the IRS will be adding additional tools
  - One tool will enable families to "unenroll from receiving these advance payments" and instead receive the full amount of the credit when they file their 2021 return next year.
  - "**Later this year**," individuals and families will be able to go to IRS.gov and use a **Child Tax Credit Update Portal** to notify IRS of changes in their income, filing status, or number of qualifying children; update their direct deposit information; and make other changes to ensure they are receiving the right amount as quickly as possible.

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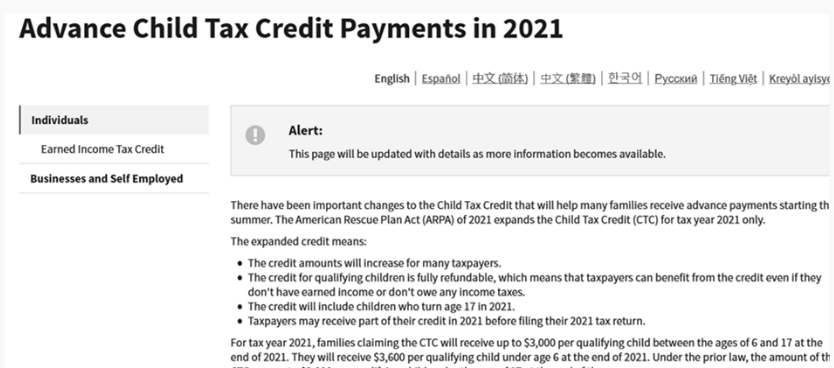
This will be the resource page…

- **https://www.irs.gov/credits-deductions/advance-child-tax-credit-payments-in-2021**


Advance Child Tax Credit Payments in 2021

English | Español | 中文 (简体) | 中文 (繁體) | 한국어 | Русский | Tiếng Việt | Kreyòl ayisy

Individuals
Earned Income Tax Credit
Businesses and Self Employed

Alert:
This page will be updated with details as more information becomes available.

There have been important changes to the Child Tax Credit that will help many families receive advance payments starting th summer. The American Rescue Plan Act (ARPA) of 2021 expands the Child Tax Credit (CTC) for tax year 2021 only.

The expanded credit means:

- The credit amounts will increase for many taxpayers.
- The credit for qualifying children is fully refundable, which means that taxpayers can benefit from the credit even if they don't have earned income or don't owe any income taxes.
- The credit will include children who turn age 17 in 2021.
- Taxpayers may receive part of their credit in 2021 before filing their 2021 tax return.

For tax year 2021, families claiming the CTC will receive up to $3,000 per qualifying child between the ages of 6 and 17 at the end of 2021. They will receive $3,600 per qualifying child under age 6 at the end of 2021. Under the prior law, the amount of th CTC was up to $2,000 per qualifying child under the age of 17 at the end of the year.

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Child Tax Credit *Reconciliation*

- In January of 2022, IRS will provide taxpayers with a report of the advance payments they received.
- Taxpayers will then **reconcile** their **advance payments** with their **eligible credits** on their 2021 return.
  - The **credit** will be reduced, but not below zero, by the payments received throughout the year.
- If, however, the ***amount of advance payments exceeds the eligible credit***, taxpayers with income **above a certain income threshold must generally *repay the excess as a tax***.

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Child Tax Credit *Reconciliation*

- This repayment requirement is **reduced or eliminated** entirely according to a complex "**safe harbor**" formula for taxpayers whose income **does not exceed 200 percent** of the following applicable income thresholds:
  - $60,000 for joint returns or surviving spouses
  - $50,000 for heads of household
  - $40,000 for single taxpayers

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Child Tax Credit *Reconciliation - Considerations*

- **Shared custody situations**
- Income near thresholds
- Only 2019 on file and child aging out
- Managed withholding to accommodate child tax credit
- Children must have SSN

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Unemployment Return Corrections

- IRS announced on June 4 that it had already reviewed over 3.1 million returns, with more than 2.8 million receiving refunds.
- The IRS plans to issue the next set of refunds in mid-June. T
- he review of returns and processing corrections will continue during the summer as the IRS continues to review the simplest returns and **then turns to more complex returns**.
- Taxpayers should receive a letter within 30 days of the correction explaining the action.

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New Draft Form 941 and Instructions

- IRS has released a new draft Form 941, with instructions. These updates incorporate lots of ARPA changes to ERC, FFCRA, COBRA.
  - "Don't use an earlier revision of Form 941 to report taxes for 2021. Don't use the March 2021 revision of Form 941 to report taxes for any quarter ending before January 1, 2021, or beginning after March 31, 2021. Don't use the June 2021 revision of Form 941 to report taxes for any quarter ending before April 1, 2021."

https://www.irs.gov/pub/irs-dft/i941--dft.pdf

https://www.irs.gov/pub/irs-dft/f941pr--dft.pdf

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Temporary Allowance of a Full Deduction for Business Meals

- After December 31, 2020, Section 210 of the Act allows a 100 percent deduction for business meals where food or beverages is provided **by a restaurant**, and paid or incurred beginning January 1, 2021, and before January 1, 2023.
  - Notice 2021-25, issued April 8, explains new provision.

- Includes meetings with potential clients, as well as travel meals.

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Temporary Allowance of a Full Deduction for Business Meals

Notice 2021-25

- Section 274(n)(1) provides that a deduction for any expense for food or beverages generally is limited to 50 percent of the amount otherwise deductible under chapter 1.
  - 1) such expense is not lavish or extravagant under the circumstances; and (2) the taxpayer (or an employee of the taxpayer) is present at the furnishing of such food or beverages.
- **Restaurant** = a business that prepares and sells food or beverages to retail customers for immediate consumption, regardless of whether the food or beverages are consumed on the business's premises.
  - However, a restaurant **does not include** a business that primarily sells pre-packaged food or beverages not for immediate consumption, such as a **grocery store; specialty food store; beer, wine, or liquor store; drug store; convenience store; newsstand; or a vending machine or kiosk**.

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Temporary Allowance of a Full Deduction for Business Meals

Notice 2021-25

- May not treat as a restaurant for purposes of § 274(n)(2)(D):
  - any eating facility located on the business premises of the employer and used in furnishing meals excluded from an employee's gross income under § 119, or
  - any employer-operated eating facility treated as a de minimis fringe under § 132(e)(2), even if such eating facility is operated by a third party under contract with the employer as described in § 1.132-7(a)(3).

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Current Business Meals Law

Takes into account T.D. 9925) in response to TCJA changes

Can you deduct meals & entertainment expenses?
It depends on the type and timing.

Expense type	Pre-overhaul (%)	Post-overhaul (%)	2021-2022 (%)
Business meals provided by a restaurant	**50**	**50**	**100**
Business travel meals provided by a restaurant	50	50	100
Other business meals	50	50	50
Entertainment expenses	50	0	0
Meal expenses during entertainment	50	50	100 *
Personal meals	0	0	0
Company picnics & holiday parties	100	100	100
Food & drink available to the public	100	100	100

Source: IRC section 274 and related IRS guidance
* Only if separately stated from entertainment expenses

Bloomberg Tax

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What did we learn from the Green Book about Tax Reform Proposals?

- **Green Book was released on May 28.**
  - Treasury Department provides details of revenue proposals within the administration's budget.
  - It provided a few more details, but many questions remain.

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American Families Plan

Increase Top Tax Rate

- **Beginning in 2022**, AFP would increase the top individual tax rate and lower the income thresholds at which the rate is triggered.

Top Tax Rate Increase

	2021 (37 percent)	2022 (39.6 percent)
MFJ	$628,301	$509,301
Single	$523,601	$452,701
HOH	$523,601	$481,001
MFS	$314,151	$254,651

- ***Green Book explanation***: This change would raise revenue while increasing the progressivity of the tax system.

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Eliminate Preferential Capital Gains Rate

- **Beginning April 28, 2021**, eliminate the Preferential Capital Gain Tax Rates for Taxpayers with > $1 million in Income.
  - The Plan proposes to subject long-term capital gain to **ordinary income tax rates** where overall income (including gain) exceeds $1 million.
    - **2021 – 37 percent**
    - **2022 – 39.7 percent**
  - "Reforms to the taxation of capital gains and qualified dividends will reduce economic disparities among Americans and raise needed revenue." **Green Book**

Current Rates – Max Cap Gain Rate = 20%

Tax Rates - 2021

Ordinary Income Tax Rates					**Long-Term Gain**		
Single		**MFJ**			**Single**	**MFJ**	
0	9950	0	19,900	**10%**	0	0	
9951	40,525	19,901	81,050	**12%**	40,400	80,800	**0%**
40,526	86,375	81,051	172,750	**22%**	40,401	80,801	
86,376	164,925	172,751	329,850	**24%**			
164,926	209,425	329,851	418,850	**32%**			
209,426	523,600	418,851	628,300	**35%**	445,850	501,600	**15%**
523601+		628,301+		**37%**	445,851	501,601	**20%**

Eliminate Preferential Capital Gains Rate

Result:

A taxpayer with $900,000 in labor income and $200,000 in preferential capital income would have $100,000 of capital income taxed at the current preferential tax rate and $100,000 taxed at ordinary income tax rates.

- *In 2021, $100,000 taxed at 37 percent*
- *In 2022, $100,000 taxed at 39.7 percent*

Taxpayers would also owe the **3.8 percent Net Investment Income Tax** on higher gain, increasing the 2022 tax rate to **43.4 percent**.

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Extend NIIT and SECA – Current Law

- Extend the Application of the Net Investment Income Tax and SECA ***beginning in 2022***.
  - Current 3.8 percent NIIT applies to net investment income > $200,000 for singles and $250,000 for MFJ. It currently applies to:
    - Most interest, dividends, rents, annuities, and royalties
    - Income derived from a trade or business in which the taxpayer does not materially participate
    - Income from a business of trading in financial instruments or commodities
    - Net gain from the disposition of property other than property held in a trade or business in which the taxpayer materially participates
- Although called the “Medicare tax,” money flows into the general fund.

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Extend NIIT and SECA – Current Law

- **Current law**: While general partners and sole proprietors pay SECA tax on earnings from their businesses, S corporation owner-employees and limited partners pay employment taxes on only a portion of their earnings. LLC members often pay little or no SECA tax at all.

- ***Green Book explanation***: Different treatment is unfair, inefficient, distorts choice of organizational form, and provides tax planning opportunities for business owners, particularly those with high incomes, to avoid paying their fair share of taxes.

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Extend Net Investment Income Tax and SECA (Self-Employment Tax)

- Ensure that all trade or business income of high-income taxpayers (>$400K AGI) is subject to the **3.8 percent** Medicare tax, **either the NIIT or SECA tax**
- Make the application of SECA to partnership and LLC income more consistent for high-income taxpayers (>$400K AGI)
- Apply SECA to the ordinary business income of high-income non-passive S corporation owners (>$400K AGI)
- Redirect NIIT funds to the Hospital Insurance Trust Fund

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New Tax at Death or Gift

- ***Beginning in 2022***, the AFP would treat the **transfer of appreciated property at death or by gift as a sale**, meaning that unrealized capital gain would be taxed at the time of death or gift.
- Dying with or gifting appreciated property would trigger taxable income to the decedent on the Federal gift or estate tax return or on a separate capital gains return.
  - Note this is in conjunction with **increase in top tax rate**, subjecting gains to **ordinary income tax rates where income is more than $1 million**, and **applying the NIIT to gain from the sale of business assets, like farmland, if overall AGI > $400K**.

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New Tax at Death or Gift

- Each deceased person would be allowed to exclude **up to $1 million (indexed for inflation) in gain from recognition at death or at the time of gift**.
- Married couple would each get their own exemption, which is **portable**, meaning that a couple could exempt $2 million in gain from tax.
  - $250,000 in gain from taxation for the sale of a personal residence ($500,000 for married filing jointly)would also be excluded
    - A married couple could potentially exempt up to $2.5 million in gain from taxation at death.

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New Tax at Death - Basis

- If property is transferred at death, the recipient's basis in the property would be the FMV of that property at the decedent's death.
  - **Example**: Transfer $5 million parcel of land with $3 million in appreciation ($2 million basis) at death.
    - Heir receives the land with a $5 million basis. Tax is due on $2 million of gain ($1 million exemption).
    - Basis steps up, just not tax free!

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New Tax at Gift - Basis

- If property is transferred by gift, the recipient would receive a carryover basis, to the extent that the $1 million exclusion applies.
  - For gifts that trigger a transfer tax, the basis would adjust to FMV for that portion of the property subject to the tax.
    - **Example**: Gift $5 million parcel of land with $3 million in appreciation ($2 million basis).
      - Donee receives the land with a $4 million basis. Tax is due on $2 million of gain.

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New Tax at Death

- **This is not an estate tax (taxed upon value of estate).**
- Current estate tax would **still apply** if value of estate exceeds basic exclusion amount (currently $11.7 million, will reset in 2026).
  - New tax would be deductible from estate value.
- **This would be a new tax at death, *never before used in our country.***

New Tax at Death - Basis

- Gain on unrealized appreciation would be recognized by a trust, partnership, or other non-corporate entity (LLC) that is the owner of property if that property has not been the subject of a recognition event **within the prior 90 years**, with such testing period beginning on January 1, 1940.
- The first possible recognition event for any taxpayer under this provision would be **December 31, 2030** (90 years from January 1, 1940).

Entities/Charities

- **Beginning in 2022**, transfer to partnership, irrevocable trust, or LLC would be taxable event.
- Gain on transfer to Charitable Remainder Trust would be taxed, with the exception of Charity's interest.
- Deduction for donation to charity would be limited to basis, not FMV.

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New Tax at Death or Gift - Basis

- A transfer would be defined under the gift and estate tax provisions and would be valued using the methodologies used for gift or estate tax purposes.
- Transfers of property into, and distributions in kind from, a trust, partnership, or other non-corporate entity (LLC), **other than a grantor trust** that is deemed to be wholly owned and revocable by the donor, would be recognition events.
- A transferred partial interest would be its proportional share of the fair market value of the entire property (no minority discounts).

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Family Business Deferral – Few Details

- Payment of tax on the appreciation of **certain family-owned and -operated businesses** would *not be due* **until** the interest in the business is sold or the business ceases to be **family-owned and operated**.
- Provides a 15-year fixed-rate *payment plan* for the tax on appreciated assets transferred at death, other than liquid assets such as publicly traded financial assets and other than businesses for which the deferral election is made.
  - IRS could require **security** at any time when there is a reasonable need for security to continue this deferral. That security could be provided from any person, and in any form, deemed acceptable by the IRS.

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Implementation Rules

- The full cost of appraisals of appreciated assets would be deductible.
- Liens would be imposed for unpaid tax.
- Underpayment of estimated tax penalty would be waived if underpayment is due to death.
- New rules would seek consistency in valuation for transfer and income tax purposes.
- New rules and safe harbors for determining the basis of assets in cases where complete records are unavailable would be created.
- New reporting requirements for all transfers of appreciated property including value and basis information would be imposed.

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American Families Plan Example

Lifetime Sale

- The American Families Plan would more than double their tax liability from **$1,267,800 (17.6 percent of sales price) to approximately $2,594,700 (36 percent of sales price)**.
  - This increase would flow from the taxation of most of the gain at a new higher ordinary income tax rate and the imposition of the 3.8 percent Medicare tax on the gain above $400,000.

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American Families Plan Example

Transfer at Death – Harris Only

The American Families Plan would treat the transfer of Harris' farmland at death as a **sale of the property**.

- If heir is not actively farming, this would trigger the taxation of $5,525,000 gain ($6,525,000 total capital gain minus $1,000,000 exemption), resulting in **a tax bill of approximately $2.19 million (or ~30 percent of the FMV).**
- The basis in the farmland would step up to $7,200,0000 (because of the $1 million exemption and the payment of the tax).
- Heir would likely have to sell a portion of the land to pay the tax.
  - Could not cash flow payment. 15-year payment plan?

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American Families Plan Example

Transfer at Death – Heir farming

- If heir is actively farming, the law may provide an exemption to **defer the tax liability** on the previously unrealized gain.
  - The Plan would *"defer* **any tax liability on family farms as long as the farm remains family-owned and operated."**
- If Jordan takes advantage of the active farming deferral, the basis in the farmland would step up by $1,000,000 (pursuant to the $1 million exemption), but no further basis adjustment would be made.
- If allowed the exemption, lien may impact ability to acquire credit or ability to depreciate assets may be impacted (if basis is not stepped up).

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American Families Plan Example

Transfer by Gift

- The Plan would also treat the transfer of Harris' farmland by gift as a sale of the property.
- Gift would trigger the taxation of $5,525,000 gain ($6,525,000 total capital gain minus $1,000,000 exemption), resulting in a tax bill of approximately **$2.19 million** (or ~30 percent of the FMV).
- The basis in the farmland would step up to $6,200,0000 (Donee would not get a step-up for the exemption amount).
  - This impending tax liability would likely end life-time gifting of highly appreciated assets.

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American Families Plan – Like-Kind Exchange

- Limit Section 1031 Exchange Deferral to $500,000 in Gain ($1 million for a married couple) **per year**
  - Although the Tax Cuts and Jobs Act eliminated like-kind deferral treatment for the exchange of personal property (farmers, for example, must now recognize gain on the trade-in value of a tractor), section 1031 for **real property** survived.
  - ***Green Book***: The change would raise revenue while increasing the progressivity of the tax system.

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End of Year Could Get Interesting…

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Iowa Updates

- Taxpayer advocate services contact: Jana.M.Baraks@irs.gov
- Last check, Governor has not signed SF 619.

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Discussion

Next Session

•Jun 24, 2021 (12:00 pm)
Thursday Tax Topics

September 21-22: Agricultural Law Seminar and Farm Tax Workshop (in-person and online)

Tax School Dates Set: Three in-person in Iowa, three in-person in Wisconsin, and three webinar options

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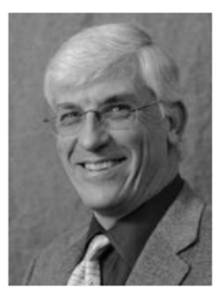

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