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Dear Clients and Friends:

With the year-end fast approaching, I wanted to review some recent tax law changes, some pending tax legislation and some moves that may help lower your tax bill for this year and next. This year's planning is more challenging than usual due to the uncertainty surrounding pending legislation that could, among other things, add new surcharges on high-income taxpayers' taxable income, increase capital gains for certain stock sales or impact your state and local income tax deductions. I hope you find the following discussion of recent tax law changes, pending tax legislation and possible year-end tax moves in the face of all this uncertainty useful.

<u>TAX CHANGES IN THE INFRASTRUCTURE INVESTMENT AND JOBS ACT</u>: The Infrastructure Investment and Jobs Act ("IIJA") was signed into law on November 15, 2021. The IIJA did not include many significant tax provisions for individual taxpayers and business except for the following:

- The IIJA retroactively ended the Employer Retention Tax Credit ("ERTC") for employee wages paid after <u>September 30, 2021</u>, unless the employer is a recovery startup business. As a result of the retroactive termination of the ERTC, employers may need to review their payroll tax compliance (including tax deposits) to make sure that the employer conforms with these changes. The IRS has now issued guidance for employers who received advance payment of the ERTC for the fourth quarter, or who reduced employment tax deposits in anticipation of the ERTC to avoid penalties. This guidance also alerts employers that penalty relief will not be given to employers for reduced employment tax deposits made after December 20, 2021.

- In connection with the continued availability of the ERTC for recovery startup businesses in the fourth quarter of 2021, the IIJA also modified the definition of a recovery startup business so that a recovery startup business is one that (i) began operating after February 15, 2020, and (ii) has average annual gross receipts of less than $1 million. The pre-IIJA prerequisite that a recovery startup business must not have otherwise met the requirements for an eligible employer qualifying for the ERTC, i.e., having experienced a significant decline in gross receipts or having been subject to a full or partial suspension under a government order, no longer applies. Thus, because of the modified definition, an employer that was not a recovery startup business in the third quarter of 2021 might now qualify as a recovery startup business in the fourth quarter of 2021 and be able to claim the ERTC for this period.

- If you have a stock brokerage account, then whenever you sell stock or other securities you receive a Form 1099-B at the end of the year. Your broker uses that form to report details of transactions such as sale proceeds, relevant dates, your tax basis for the sale, and the character of gains or losses. Furthermore, if you transfer stock from one broker to another broker, then the old broker is required to furnish a statement with relevant information, such as tax basis, to the new broker. <u>The IIJA expands the definition of brokers who must furnish Forms 1099-B to include businesses that are responsible for regularly providing any service accomplishing transfers of digital assets on behalf of another person ("Crypto Exchanges")</u>. Thus, any platform on which you can buy and sell cryptocurrency will be required to report digital asset transactions to you and the IRS at the end of each year. For the reporting requirements, a "digital asset" is any digital representation of value which is recorded on a cryptographically secured distributed ledger or any similar technology. This definition will capture most cryptocurrencies and potentially include some non-fungible tokens (NFTs) that are using blockchain technology for one-of-a-kind assets like digital artwork. You may be aware that when a business receives $10,000 or more in cash in a transaction, that business is required to report the transaction, including the identity of the person from whom the cash was received, to the IRS on Form 8300. The IIJA will require businesses to treat digital assets like cash for purposes of this reporting requirement. Generally, these rules will apply to digital asset transactions starting in 2023.

- The IIJA also made changes to clarify extensions of filing deadlines for taxpayers in declared disaster areas or combat zones, to give the IRS broader authority to declare disaster areas and to extend the deadlines for filing tax court litigation for taxpayers when the tax court is inaccessible or unavailable (whether due to emergency or shut-down due to a lapse in funding).

- The IIJA extends the period for employer defined pension plans to use interest-rate smoothing when calculating the employer's contribution requirements through 2034. During periods of volatile interest rates, use of interest-rate smoothing reduces the year-to-year volatility of the employer's required contributions.

<u>TAX CHANGES WHICH IMPACT ESTATE AND GIFT TAXES (AND SOME POSSIBLE CHANGES TO KEEP AN EYE ON)</u>:

- Every taxpayer has a federal estate & gift tax credit (the "E&G Tax Credit") which can be used to shelter both lifetime taxable gifts from gift tax and the remaining estate from estate tax at the taxpayer's death. For taxpayers dying in 2021, the E&G Tax Credit is $11,70,000 (less any E&G Tax Credit used to shelter prior gifts from gift tax). For 2022, the E&G Tax Credit is scheduled to rise to <u>$12,060,000</u>.

- Every taxpayer can give annual gifts to an unlimited number of recipients, up to a specified maximum value, each year without the gift counting as a "taxable gift". These so-called "annual exclusion" gifts are an excellent method to slowly transfer significant wealth to your desired beneficiaries without using your E&G Tax Credit. For 2021, the maximum "annual exclusion amount" which could be given to any recipient is $15,000, but the "annual exclusion amount" will rise to <u>$16,000</u> per recipient for 2022.

- The big news in 2021 is that <u>none</u> of the various estate and gift tax legislation proposals which were discussed earlier in the year have been enacted or included in the pending legislation still being considered by Congress. These proposals included:

    - Proposals to reduce the estate and gift tax credit to $5,000,000 (or lower).

    - Proposals to eliminate the adjustment of the tax basis of a decedent's assets to their date-of-death values (often referred to as a "stepped-up tax basis").

    - Proposals to restrict or eliminate the use of annual exclusion gifts for gifts made in trusts or for contributions to trusts created to hold insurance.

    - Proposals to include the assets of grantor trusts to be included in a decedent's estate and to treat grantor trusts as separate taxpayers for the recognition of taxable gain or loss for asset sales between the grantor and the grantor trust. These proposals included grandfather rules for grantor trusts created prior to the date of enactment, but the grandfather rules were cumbersome and potentially inadequate to protect existing grantor trusts.

    - Proposals to substantially restrict or eliminate the use of valuation discounts in the valuation of partial interests in businesses or real estate for estate and gift tax purposes.

- Although <u>none</u> of the estate and gift tax proposals listed above have been included in the IIJA or pending legislation still being discussed in Congress, there is still a risk that these proposals might be added back into pending or future legislation in 2022. In addition, there is always a risk that the Treasury may seek to reintroduce regulations to restrict valuation discounts or the use of trusts for estate and gift tax planning. Accordingly, taxpayers should remain vigilant.

<u>POSSIBLE TAX LAW CHANGES UNDER THE BUILD BACK BETTER ACT</u>: The House has passed the Build Back Better Act (the "BBBA"), and the Senate is now discussing whether to enact the BBBA in the form enacted by the House or to make amendments. The margin for passage of the BBBA in the Senate is razor-thin (at least 50 votes, plus Vice-President Harris's tie-breaking vote), and no one can predict which provisions will stay in, which new provisions might be added or even if the BBBA will pass the Senate in any form. Obviously, this uncertainty makes for difficult year-end tax planning. To help you weigh your year-end tax planning options and to prepare you for what might be coming in 2022, here is a summary of the more significant tax proposals in the <u>House-passed version</u> of the BBBA:

- The House-passed version of the BBBA does <u>not</u> change the income tax bracket rates for individuals, trusts or estates. Tax revenue is raised primarily through the imposition of new tax surcharges on high-income taxpayers, the expansion of the 3.8% net investment income tax, a minimum corporate tax on highly-profitable publicly-traded corporations.

- Significant new tax surcharges would be imposed on high-income taxpayers, effective as of 2022:

  - A surcharge of 5% would be imposed on married taxpayers filing jointly with AGI exceeding $10,000,000 (single taxpayers and married taxpayers filing separately would be surcharged 5% for AGI exceeding $5,000,000). An additional 3% surcharge (for a total of 8%) would be imposed on married taxpayers filing jointly with AGI exceeding $25,000,000 (single taxpayers and married taxpayers filing separately would be surcharged 5% for AGI exceeding $12,500,000).

  - For trusts and estates, these "high-income" surcharges would kick in at significantly lower AGI level. The 5% surcharge would apply to trusts and estates with AGI exceeding $200,000, and the additional 3% surcharge (for a total surcharge of 8%) would apply to trusts and estates with AGI exceeding $500,000. <u>If these surcharges go into effect for trusts and estates in 2022, it will be more important than ever for trusts and estates to consider the appropriate use of beneficiary distributions to shift taxable income to beneficiaries and the timing of administration expenses and fiduciary fees</u>. In particular, trusts and estates which anticipate substantial AGI will need to act quickly before the end of each tax year (or at least within 65 days of the close of a tax year) to evaluate the benefits of shifting taxable income out to beneficiaries. In some cases, trustees may want to consider modifications to the trust to qualify the distribution of capital gains distributions for a distribution deduction for tax purposes.

  - There hasn't been a great deal of public discussion of these surcharge provisions, so practitioners expect these provisions to remain in the Senate version of the BBBA.

- Currently, federal tax law imposes a 3.8% surcharge on net investment income (the "3.8% NIIT") for higher-income taxpayers, but this 3% NIIT surcharge does not apply to an individual's income which is earned in the ordinary course of a trade or business of a pass-through entity and which is not subject to employment ("FICA") taxes (generally, income earned through an S corporation, limited partnership or LLC). For example, as long as an S corporation owner pays himself or herself a reasonable salary (subject to FICA taxes), the S corporation owner can avoid both self-employment taxes and the 3.8% NIIT on the remaining income derived from the S corporation's trade or business. The House-passed version of the BBBA would extend the 3.8% NIIT to all income earned in the ordinary course of a trade or business (if the income is not otherwise subject to FICA taxes) for taxpayers with modified AGI exceeding $400,000 (or married taxpayers filing jointly with modified AGI exceeding $500,000, married taxpayers filing separately with modified AGI exceeding $250,000). Non-grantor trusts and estates would be subject to the 3.8% NIIT on all income derived from a trade or business once the trust or estate reaches the top marginal bracket ($13,450 for 2022). There hasn't been a great deal of public discussion of this provision, so practitioners expect it to remain in the Senate version of the BBBA.

- The onerous limits on the deduction of state and local taxes (the "SALT limit") would be loosened by raising the SALT limit from $10,000 per return (married or single) to $80,000 for married taxpayers filing jointly, and $40,000 for single taxpayers married taxpayers filing separately, trusts and estates. These increased SALT limits would be effective for 2021 and extend through 2031. The amount of the SALT limit (as well as its retroactive effective date to the start of 2021) is an area of heated discussion in the Senate, so we'll see if this provision survives unchanged.

- The House-passed version of the BBBA also contains numerous provisions which may impact the retirement plans of certain high-income individuals who have large retirement assets:

  - An individual would be prohibited from making further contributions to a Roth or traditional IRA for a tax year if the contributions would cause the total value of the individual's IRA and defined contribution retirement accounts as of the end of the prior tax year to exceed (or further exceed) $10 million. Each individual is treated separately for purposes of applying this $10 million test (which means married individuals aren't penalized by aggregating their retirement accounts for purposes of applying the $10 million test). This limitation would apply to single taxpayers and married taxpayers filing separately with income over $400,000, heads of households over $425,000, or married taxpayers filing jointly over $450,000.

  - If an individual's combined traditional IRA, Roth IRA, and defined contribution retirement account balances exceed $10 million at the end of a tax year and the individual meets these same income thresholds (single taxpayers and married taxpayers filing separately with income over $400,000, heads of households over $425,000, or married taxpayers filing jointly over $450,000), a minimum distribution would be required for the following year.

  - These retirement plan provisions for high-income taxpayers would be effective for tax years beginning after Dec. 31, 2028. However, if these provisions pass, taxpayers may need to carefully consider their retirement plan options well in advance of 2028. For example, a surviving spouse may need to consider whether to keep the deceased spouse's retirement plans as inherited IRAs (which wouldn't count towards the $10,000,000 threshold) or roll the deceased spouse's retirement assets into the surviving spouse's own IRA (which would count towards the $10,000,000 threshold). In addition, high-income taxpayers may want to consider Roth Ira conversion strategies well in advance of 2028 to take advantage of years in which they are eligible to do Roth conversions.

- The House-passed version of the BBBA would also eliminate Roth conversions for both IRAs and employer-sponsored plans for single with taxable income over $400,000, married taxpayers filing jointly with taxable income over $450,000, and heads of household with taxable income over $425,000 (all indexed for inflation). This provision would apply to distributions, transfers, and contributions made in tax years beginning after Dec. 31, 2031.

- The House-passed version of the BBBA would also prohibit all employee after-tax contributions in qualified plans and after-tax IRA contributions from being converted to a Roth IRA regardless of income level, effective for distributions, transfers, and contributions made after Dec. 31, 2021.

- Currently, capital gains recognized on the sale of "qualified small business stock" is eligible for a 50%, 75% or 100% capital gain exclusion from tax (determined by reference to the date of issuance of the qualified small business stock). The House-passed version of the BBBA would eliminate these "qualified small business stock" capital gain exclusions for taxpayers with AGI exceeding $400,000 and for trusts and estates (regardless of the trust's or estate's AGI).

- The temporary expanded child tax credit (enacted in the American Rescue Plan Act earlier this year) would be extended through 2022 and the earned income limits and phaseout amounts for this tax credit would be indexed for inflation. The refundability of the child tax credit would be made permanent.

- Similarly, the temporary expanded earned income tax credit (enacted in the American Rescue Plan Act earlier this year) would be extended through 2022 and the earned income limits and phaseout amounts for this tax credit would be indexed for inflation.

- The House-passed version of the BBBA would impact the health care premium assistance provisions (enacted in the American Rescue Plan Act earlier this year) by: (i) increasing the amounts available for health care premium assistance through 2025, (ii) extending through 2025 the rule that allows the premium tax credit to certain taxpayers whose household income exceeds 400% of the poverty line, (iii) modifying the employer-sponsored coverage affordability test in the premium tax credit through 2025, (iv) excluding a portion of lump-sum Social Security benefit payments when determining household income for purposes of the credit, and (v) excluding the first $3,500 of income of dependents who have not reached the age of 24. The House-passed version of the BBBA would also allow certain low-income employees who are offered employer-provided health coverage to claim the premium tax credit.

- The House-passed version of the BBBA contains a wide variety of incentives in the form of tax credits for electric vehicle purchases, green energy investments, residential and commercial energy-efficient property. If you are contemplating the purchase of any items of this type before the close of 2021, you may want to explore waiting until 2022 to see if you can qualify for a tax credit.

- The House-passed version of the BBBA would extend the constructive and wash sale rules to commodities, foreign currencies and crypto-currencies.

- A minimum 15% tax would be imposed on corporations (but not S corporations, regulated investment companies or real estate investment trusts) which report more than $1 billion in profit annually for three consecutive years. The House-passed version of the BBBA does not raise the current corporate tax rate of 21%.

- A 1% surcharge would be imposed on the fair market value of any stock buy-backs by a domestic publicly-traded corporation.

YEAR-END TAX PLANNING FOR INDIVIDUAL TAXPAYERS: You should carefully consider whether any of the provisions currently included in the House-passed version of the BBBA might impact your year-end tax planning. The standard year-end approach of deferring income and accelerating deductions to minimize taxes will continue to produce the best results for all but the highest income taxpayers, as will the bunching of deductible expenses into this year or next to avoid restrictions and maximize deductions.

However, if the provisions currently included in the House-passed version of the BBBA do pass the Senate and are signed into law, high-income taxpayers may find that the opposite strategies produce better results: Pulling income into 2021 to be taxed without surcharge or at potentially lower rates (if you think you will be in a higher tax bracket next year), and deferring deductible expenses until 2022 (when they can be taken to offset what would be higher-taxed income). This will require careful evaluation of all relevant factors.

Here is a list of actions based on current tax rules that may help you save tax dollars if you act before year-end (whether or not the BBBA is enacted into law). Not all of these actions will apply to you, but you (or a family member) may benefit from many of them. Again, if you believe that provisions of the BBBA might impact you, you should be more wary of those actions which would pull taxable income into 2021 or defer deductions until 2022. These potential tax-savings actions include:

- Even if the BBBA doesn't pass, higher-income individuals must be wary of the 3.8% NIIT on certain unearned income. The surtax is 3.8% of the lesser of: (1) net investment income (NII), or (2) the excess of MAGI over a threshold amount ($250,000 for joint filers or surviving spouses, $125,000 for a married individual filing a separate return, and $200,000 in any other case).

- As year-end nears, the approach taken to minimize or eliminate the 3.8% surtax will depend on the taxpayer's estimated MAGI and NII for the year. Some taxpayers should consider ways to minimize (e.g., through deferral) additional NII for the balance of the year, others should try to reduce MAGI other than NII, and some individuals will need to consider ways to minimize both NII and other types of MAGI. An important exception is that NII does not include distributions from IRAs or most other retirement plans.

- As discussed above, the BBBA would amend the 3.8% NIIT effective after this tax year for high income (e.g., phased-in starting at $500,000 on a joint return; $400,000 for most others) S shareholders, limited partners, and LLC members to NIIT on their pass-through income and gain that is not subject to payroll tax. Accelerating some of this type of income into 2021 could help avoid NIIT on it under the potential 2022 rules, but would also increase 2021 MAGI, potentially exposing other 2021 investment income to the tax.

- The 0.9% additional Medicare tax also may require higher-income earners to take year-end action. It applies to individuals whose employment wages and self-employment income total more than an amount equal to the 3.8% NIIT thresholds, above. Employers must withhold the additional Medicare tax from wages in excess of $200,000 regardless of filing status or other income. Self-employed persons must take it into account in figuring estimated tax. There could be situations where an employee may need to have more withheld toward the end of the year to cover the tax. This would be the case, for example, if an employee earns less than $200,000 from multiple employers but more than that amount in total. Such an employee would owe the additional Medicare tax, but nothing would have been withheld by any employer.

- Long-term capital gain from sales of assets held for over one year is taxed at 0%, 15% or 20%, depending on the taxpayer's taxable income. If you hold long-term appreciated-in-value assets, consider selling enough of them to generate long-term capital gains that can be sheltered by the 0% rate. The 0% rate generally applies to net long-term capital gain to the extent that, when added to regular taxable income, it is not more than the maximum zero rate amount (e.g., $80,800 for a married couple; estimated to be $83,350 in 2022). If, say, $5,000 of long-term capital gains you took earlier this year qualifies for the zero rate then try not to sell assets yielding a capital loss before year-end, because the first $5,000 of those losses will offset $5,000 of capital gain that is already tax-free.

- Postpone income until 2022 and accelerate deductions into 2021 if doing so will enable you to claim larger deductions, credits, and other tax breaks for 2021 that are phased out over varying levels of AGI. These include deductible IRA contributions, child tax credits, higher education tax credits, and deductions for student loan interest. Postponing income also is desirable for taxpayers who anticipate being in a lower tax bracket next year due to changed financial circumstances. Note, however, that in some cases, it may actually pay to accelerate income into 2021. For example, this may be the case for a person who will have a more favorable filing status this year than next (e.g., head of household versus individual filing status), or who expects to be in a higher tax bracket next year. That's especially a consideration for high income taxpayers who may be subject to higher rates next year under proposed legislation.

- If you believe a Roth IRA is better for you than a traditional IRA, consider converting traditional-IRA money invested in any beaten-down stocks (or mutual funds) into a Roth IRA in 2021 if eligible to do so. Keep in mind that the conversion will increase your income for 2021, possibly reducing tax breaks subject to phaseout at higher AGI levels. This may be desirable, however, for those potentially subject to higher tax rates under pending legislation.

- It may be advantageous to try to arrange with your employer to defer, until early 2022, a bonus that may be coming your way. This might cut as well as defer your tax. Again, considerations may be different for the high-income individuals.

- Many taxpayers won't want to itemize because of the high basic standard deduction amounts that apply for 2021 ($25,100 for joint filers, $12,550 for singles and for marrieds filing separately, $18,800 for heads of household), and because many itemized deductions have been reduced or abolished, including the current $10,000 SALT limit; miscellaneous itemized deductions; and non-disaster related personal casualty losses. You can still itemize medical expenses that exceed 7.5% of your AGI, state and local taxes up to $10,000, your charitable contributions, plus mortgage interest deductions on a restricted amount of debt, but these deductions won't save taxes unless they total more than your standard deduction. In addition to the standard deduction, you can claim a $300 deduction ($600 on a joint return) for cash charitable contributions.

- Some taxpayers may be able to work around these deduction restrictions by applying a bunching strategy to pull or push discretionary medical expenses and charitable contributions into the year where they will do some tax good. For example, a taxpayer who will be able to itemize deductions this year but not next will benefit by making two years' worth of charitable contributions this year. The COVID-related increase for 2021 in the income-based charitable deduction limit for cash contributions from 60% to 100% of MAGI assists in this bunching strategy.

- Consider using a credit card to pay deductible expenses before the end of the year. Doing so will increase your 2021 deductions even if you don't pay your credit card bill until after the end of the year.

- Required minimum distributions (“RMDs”) from an IRA or 401(k) plan (or other employer-sponsored retirement plan) have not been waived for 2021, as they were for 2020. If you were 72 or older in 2020 you must take an RMD during 2021. Those who turn 72 this year have until April 1 of 2022 to take their first RMD but may want to take it by the end of 2021 to avoid having to double up on RMDs next year.

- If you are age 70 or older by the end of 2021, and especially if you are unable to itemize your deductions, consider making 2021 charitable donations via qualified charitable distributions from your traditional IRAs. These distributions are made <u>directly</u> to charities from your IRAs, and the amount of the contribution is neither included in your gross income nor deductible on Schedule A, Form 1040. However, you are still entitled to claim the entire standard deduction. (The qualified charitable distribution amount is reduced by any deductible contributions to an IRA made for any year in which you were age 70 or older, unless it reduced a previous qualified charitable distribution exclusion.)

- Take an eligible rollover distribution from a qualified retirement plan before the end of 2021 if you are facing a penalty for underpayment of estimated tax and increasing your wage withholding won't sufficiently address the problem. Income tax will be withheld from the distribution and will be applied toward the taxes owed for 2021. You can then timely roll over the gross amount of the distribution, i.e., the net amount you received plus the amount of withheld tax, to a traditional IRA. No part of the distribution will be includible in income for 2021, but the withheld tax will be applied pro rata over the full 2021tax year to reduce previous underpayments of estimated tax.

- Consider increasing the amount you set aside for next year in your employer's FSA if you set aside too little for this year and anticipate similar medical costs next year.

- If you become eligible in December of 2021 to make HSA contributions, you can make a full year's worth of deductible HSA contributions for 2021.

- Make gifts sheltered by the annual gift tax exclusion before the end of the year if doing so may save gift and estate taxes. The exclusion applies to gifts of up to $15,000 made in 2021 to each of an unlimited number of individuals. You can't carry over unused exclusions to another year. These transfers may save family income taxes where income-earning property is given to family members in lower income tax brackets who are not subject to the kiddie tax.

- If you were in federally declared disaster area, and you suffered uninsured or unreimbursed disaster related losses, keep in mind you can choose to claim them either on the return for the year the loss occurred (in this instance, the 2021 return normally filed next year), or on the return for the prior year (2020), generating a quicker refund.

- If you were in a federally declared disaster area, you may want to settle an insurance or damage claim in 2021 to maximize your casualty loss deduction this year.

<u>YEAR-END TAX PLANNING FOR BUSINESSES</u>: Whether or not the provisions of the House-passed BBBA are enacted into law and become effective next year, the standard year-end approach of deferring income and accelerating deductions to minimize taxes will continue to produce the best results for most small businesses, as will the bunching of deductible expenses into this year or next to maximize their tax value. However, once again, if the BBBA is enacted, the highest income businesses and owners may find that the opposite strategies produce better results: Pulling income into 2021 to be taxed at currently lower rates, and deferring deductible expenses until 2022, when they can be taken to offset what would be higher-taxed income. This will require careful evaluation of all relevant factors.

Here is a list of actions <u>based on current tax rules</u> that may help you save tax dollars if you act before year-end. Again, not all of them will apply to you or your business, but you may benefit from many of these ideas:

- Taxpayers other than corporations may be entitled to a deduction of up to 20% of their qualified business income. For 2021, if taxable income exceeds $329,800 for a married couple filing jointly, (about half that for others), the deduction may be limited based on whether the taxpayer is engaged in a service-type trade or business (such as law, accounting, health, or consulting), the amount of W-2 wages paid by the business, and/or the unadjusted basis of qualified property (such as machinery and equipment) held by the business. The limitations are phased in; for example, the phase-in applies to joint filers with taxable income up to $100,000 above the threshold, and to other filers with taxable income up to $50,000 above their threshold. Taxpayers may be able to salvage some or all of this deduction, by deferring income or accelerating deductions to keep income under the dollar thresholds (or be subject to a smaller deduction phaseout) for 2021. Depending on their business model, taxpayers also may be able increase the deduction by increasing W-2 wages before year-end. The rules are quite complex, so don't make a move in this area without consulting your accountant or other tax advisor.

- More small businesses are able to use the cash (as opposed to accrual) method of accounting than were allowed to do so in earlier years. To qualify as a small business a taxpayer must, among other things, satisfy a gross receipts test, which is satisfied for 2021 if, during a three-year testing period, average annual gross receipts don't exceed $26 million (next year this dollar amount is estimated to increase to $27 million). Not that many years ago it was $1 million. Cash method taxpayers may find it a lot easier to shift income, for example by holding off billings till next year or by accelerating expenses, for example, paying bills early or by making certain prepayments.

- Businesses should consider making expenditures that qualify for the liberalized business property expensing option. For tax years beginning in 2021, the expensing limit is $1,050,000, and the investment ceiling limit is $2,620,000. Expensing is generally available for most depreciable property (other than buildings) and off-the-shelf computer software. It is also available for interior improvements to a building (but not for its enlargement), elevators or escalators, or the internal structural framework), for roofs, and for HVAC, fire protection, alarm, and security systems.

- The generous dollar ceilings mean that many small and medium sized businesses that make timely purchases will be able to currently deduct most if not all their outlays for machinery and equipment. What's more, the expensing deduction is not prorated for the time that the asset is in service during the year. This means that expensing eligible items acquired and placed in service in the last days of 2021, rather than at the beginning of 2022, can result in a full expensing deduction for 2021.

- Businesses also can claim a 100% bonus first year depreciation deduction for machinery and equipment bought used (with some exceptions) or new if purchased and placed in service this year, and for qualified improvement property, described above as related to the expensing deduction. The 100% write-off is permitted without any proration based on the length of time that an asset is in service during the tax year. As a result, the 100% bonus first-year write-off is available even if qualifying assets are in service for only a few days in 2021.

- Businesses may be able to take advantage of the de minimis safe harbor election (also known as the book tax conformity election) to expense the costs of lower-cost assets and materials and supplies, assuming the costs aren't required to be capitalized under the UNICAP rules. To qualify for the election, the cost of a unit of property can't exceed $5,000 if the taxpayer has an applicable financial statement (AFS, e.g., a certified audited financial statement along with an independent CPA's report). If there's no AFS, the cost of a unit of property can't exceed $2,500. Where the UNICAP rules aren't an issue, and where potentially increasing tax rates for 2022 aren't a concern, consider purchasing qualifying items before the end of 2021.

- A corporation (other than a large corporation) that anticipates a small net operating loss (“NOL”) for 2021 (and substantial net income in 2022) may find it worthwhile to accelerate just enough of its 2022 income (or to defer just enough of its 2021 deductions) to create a small amount of net income for 2021. This allows the corporation to base its 2022 estimated tax installments on the relatively small amount of income shown on its 2021 return, rather than having to pay estimated taxes based on 100% of its much larger 2022 taxable income.

- Year- end bonuses can be timed for maximum tax effect by both cash- and accrual-basis employers. Cash basis employers deduct bonuses in the year paid, so they can time the payment for maximum tax effect. Accrual-basis employers deduct bonuses in the accrual year, when all events related to them are established with reasonable certainty. However, the bonus must be paid within two months after the end of the employer's tax year for the deduction to be allowed in the earlier accrual year. Accrual employers looking to defer deductions to a higher- taxed future year should consider changing their bonus plans before year end to set the payment date later than the 2.5-month window or change the bonus plan’s terms to make the bonus amount not determinable at year end.

- To reduce 2021 taxable income, consider deferring a debt-cancellation event until 2022.

- Sometimes the disposition of a passive activity can be timed to make best use of its freed-up suspended losses. Where reduction of 2021 income is desired, consider disposing of a passive activity before year- end to take the suspended losses against 2021 income. If possible 2022 top rate increases are a concern, holding off on disposing of the activity until 2022 might save more in future taxes.

If you or your accountant would like more details about any item discussed in this letter, please do not hesitate to call.

Very truly yours,

Linda C. Slider