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Tax Planning for Contractors for 2021 & Beyond

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Federal Income Tax Update for Businesses

Employee Retention Credit (ERC)

Employee Retention Credit

Overview

- The Employee Retention Credit (ERC) is a fully refundable tax credit for eligible employers based upon eligibility and payment of qualified wages and health plan expenses.
- The ERC applies to qualified expenses paid after 3/12/20 and **was set to expire on 12/31/21.**
  - **However, the recently House passed Infrastructure Investment and Jobs Act changed it to end on 9/30/21**.

Eligible Employer

- An eligible employer is any employer carrying on a "trade or business" during the ERC period (3/12/20 – 9/30/21), that either:
  - **<u>Fully or partially suspend operations</u>** during any calendar quarter in 2020 or 2021 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
  - **<u>Experience a "significant decline in gross receipts"</u>** during the calendar quarter.

Employee Retention Credit

CARES Act (3/27/20)

- **Wages Covered:** Wages paid from 3/13/20 – 12/31/20.
- **Credit Amount**: 50% of qualified wages.
- **Wage Cap**: $10,000 per employee for all quarters.
- **Maximum Credit**: $5,000 per employee for 2020.
- **Gross Receipts Eligibility Test:** 50% decline in calendar quarter gross receipts when compared to same quarter in 2019.
- **PPP Loan Recipients:** Not eligible for ERC.

Employee Retention Credit

Consolidated Appropriations Act (12/27/20) and American Rescue Plan Act (3/11/21)

- **Wages Covered:** Wages paid from **1/1/21 – 12/31/21 (now ends 9/30/21).**
- **Credit Amount**: 70% of qualified wages.
- **Wage Cap:** $10,000 per employee per applicable quarter.
- **Maximum Credit:** $7,000 per employee per quarter up to $21,000 per employee for 2021.
- **Gross Receipts Eligibility Test:** 20% decline in calendar quarter or prior calendar quarter gross receipts when compared to same quarter in 2019.
- **PPP Loan Recipients:** Eligible for ERC **(retroactive to 3/13/20)** but only with respect to wages not used for PPP loan forgiveness.

The Build Back Better Act

The Build Back Better Act

- Legislation first introduced by House Ways and Means Committee on September 27, 2021. The U.S. House of Representatives passed the Build Back Better Act on November 19, 2021, which will now move to the Senate. The legislation will likely undergo several more changes to get all of the Senate Democratics on board.
  - Original cost was $3.5 trillion
  - Revised cost is down to $1.75 trillion

- Tax Foundation Report – increase Federal revenues by $1.5 trillion
  - Revenues will be reduced by $500 billion of expanded tax credits
  - Includes revenue anticipated from increased tax compliance
  - Excluding increased compliance only $637 billion raised

The Build Back Better Act

- **Enhances IRS Tax Enforcement**
  - Increase staff by 87,000.
  - Focus on taxpayers with incomes over $400,000.
  - Assumes increased audits will result in increased revenue.
  - Projected to generate $120 billion in revenue.
  - Estimated cost - $45 billion.

The Build Back Better Act

Business Tax Provisions Removed from Original Version

- **Corporate Tax Rate Increase**
  - Return to a progressive corporate income tax rate structure.
    - $0 - $400,000 = 18%
    - $400,001 - $5,000,000 = 21%
    - > $5,000,000 = 26.5%

- **Limit on Qualified Business Income Deduction (QBID) under IRC Section 199A**
  - Limit the maximum value of the Section 199A passthrough deduction to **$500,000 for joint filers and $400,000 for single filers**, $250,000 MFS, $10,000 trusts.

The Build Back Better Act

- **Applies NIIT to Trade or Business Income of Certain High-Income Individuals**
  - Expands the NIIT to cover **active business income** derived in the ordinary course of a trade or business **for taxpayers with greater than $400,000 in taxable income** (single filer) or **$500,000 (joint filer),** as well as for trusts and estates.
    - The provision clarifies that this tax is not assessed on wages on which FICA is already imposed.
- **Limits Excess Business Losses of Noncorporate Taxpayers**
  - Amends Code Sec. 461(l) to permanently disallow excess business losses (i.e., net business deductions that exceed business income **above the $250,000 (single) and $500,000 (married) thresholds)** for noncorporate taxpayers for tax years beyond 2025.
    - The provision allows taxpayers whose losses are disallowed to carry those losses forward to the next tax year.
    - This section applies to **tax years beginning after December 31, 2020**.

The Build Back Better Act

- **Corporate Alternative Minimum Tax**
  - The corporate alternative minimum tax (AMT) proposal imposes a **15% minimum tax on corporations** with adjusted financial statement income **(AFSI) in excess of $1 billion.**
  - An applicable corporation's minimum tax is equal to the **amount by which the tentative minimum tax exceeds the corporation's regular tax** for the year.
  - **Tentative minimum tax is determined by applying a 15% tax rate to the AFSI** of the corporation for the tax year (after accounting for the AMT foreign tax credit and the financial statement net operating losses).
  - For these purposes, AFSI is the net income or loss of the taxpayer stated on the taxpayer's applicable financial statement with certain modifications.
    - Generally, an applicable financial statement is a corporation's form 10-L filled with the Securities and Exchange Commission, and audited financial statement, or other similar financial statement.
  - This section is effective for **tax years beginning after December 31, 2022**.

The Build Back Better Act

- **Research and Experimental Expenditures**
  - This provision delays the effective date of the provision in the **Tax Cuts and Jobs Act** which provides for **amortization of research and experimental expenditures over 5 years for tax years beginning after December 31, 2021**.
  - Under this provision of the Bill, the amortization of research and experimental expenditures **will begin for amounts paid or incurred in tax years beginning after December 31, 2025**.
  - This section is effective on the date of enactment.

The Build Back Better Act

- **Limitations on Certain Special Rules for Section 1202 Gains**
  - This provision amends Code Sec. 1202(a) **so that the special 75% and 100% exclusion** rates for gains realized from certain qualified small business stock **will not apply** to taxpayers with adjusted gross income equal or exceeding $400,000.
  - The baseline **50% exclusion** in Code Sec . 1202(a)(l) **remains available** for all taxpayers.
  - This section applies to sales and exchanges after September 13, 2021, subject to a binding contract exception.

The Build Back Better Act

- **Possessions' Economic Activity Credit**
  - The provision creates a new economic activity credit related to active businesses conducted in a U.S. possession or possessions.
  - The new credit is a **general business credit equal to 20%** of, for wages, the sum of qualified possessions wages and fringe benefits paid or incurred by a qualified domestic corporation for a tax year.
  - For purposes of this credit, "possessions" include the fiscally autonomous territories of American Samoa, Guam, Commonwealth of Northern Marianas, Commonwealth of Puerto Rico, and the U.S. Virgin Islands.
  - This provision is effective for tax years beginning after date of enactment.

The Build Back Better Act

- **Energy Efficient Commercial Buildings Deduction**
  - The proposal temporarily modifies the Code Sec. 179D energy efficient commercial buildings deduction.
  - The modifications are in effect for tax years beginning after December 31, 2021, and ending before January 1, 2032.
  - Among other things, the proposal **reduces, from 50% to 25%,** the amount by which a building must increase its efficiency relative to a reference building to be eligible for the Code Sec. 179D deduction.
  - Under the proposal, in general, the maximum energy efficient commercial buildings deduction is changed to an amount equal $0.50 per square foot increased (but not above $1.00) by $0.02 for each percentage point by which the total annual energy and power costs for the building are certified to be reduced by a percentage greater than 25%.
  - The provision also provides an alternative deduction for energy efficient retrofit property.

The Build Back Better Act

- **Extension, Increase, and Modifications of New Energy Efficient Home Credit**
  - **<u>Extends for ten years</u>**, through December 31,2031, the Code Sec. 45L credit for new energy efficient homes.
  - Replaces the existing credit amounts with a $2,500 credit for new homes that meet certain energy efficiency standards and a $5,000 credit for new homes that are certified as zero-energy ready homes.
  - Changes the credit for multifamily dwelling units.

The Build Back Better Act

- **Refundable New Qualified Plug-in Electric Drive Motor Vehicle Credit for Individuals**
  - The proposal creates a new Code Sec. 36C credit that effectively extends and modifies the Code Sec. 30D credit for new qualified plug-in electric drive motor vehicles (the "EV credit").
  - **The proposal eliminates the limitation on the number of credit eligible EVs each manufacturer can sell**.
  - Beginning January 1, 2022, the proposal makes the EV credit **a refundable personal income tax credit** for vehicles acquired on or after that date.
- **Credit for Previously Owned Qualified Plug-in Electric Drive Motor Vehicles**
  - The proposal creates a new credit for each previously owned qualified plug-in electric drive motor vehicle placed in service by a qualified buyer (the "previously owned EV credit").
  - The base amount of the credit is $2,000.

The Build Back Better Act

- **Qualified Commercial Electric Vehicles**
    - The proposal creates a new credit for each qualified commercial electric vehicle ("qualified commercial EV") placed in service by the taxpayer.
    - Generally, the credit amount is the lesser of 5% (30% in the case of a vehicle not powered by a gasoline or diesel combustion engine) of the basis of a qualified vehicle or the incremental cost of the vehicle.

- **Qualified Fuel Cell Motor Vehicles**
    - The proposal **extends the sunset date** for the credit for new qualified fuel cell motor vehicles in Code Sec. 30B **for ten years** (through December 31, 2031).
    - The definition of a new qualified fuel cell motor vehicle is modified such that the vehicle may not be of a character subject to an allowance for depreciation.

The Build Back Better Act

- **Alternative Fuel Refueling Property Credit**
  - In general, the proposal **extends the sunset date** for the alternative fuel refueling property credit **for ten years** (through December 31, 2031).
  - The proposal also modifies the credit amount for certain fuel refueling property.

- **Reinstatement and Expansion of Employer-provided Fringe Benefits for Bicycle Commuting**
  - The proposal restores and modifies the exclusion for qualified bicycle commuting reimbursements.

The Build Back Better Act

- **Credit for Certain New Electric Bicycles**
  - The proposal creates a **new refundable credit for each qualified electric bicycle** placed in service by a taxpayer (the "electric bicycle credit").
  - The credit amount is 30% of the cost of a qualified electric bicycle.
  - This section applies to property placed in service after December 31, 2021, in tax years ending after that date. The credit does not apply to bicycles placed in service after December 31, 2025.
- **Labor Costs of Installing Mechanical Insulation Property**
  - The proposal creates a **new general business credit equal to 2% of the mechanical insulation labor costs** paid or incurred by the taxpayer during a tax year.

Federal Income Tax Update for Individuals

Present Legislation

Present Legislation – The Consolidated Appropriations Act of 2021

- ***<u>New Recovery Rebate</u>***
  - **Additional 2020 Refundable Credit**
    - $600 per family member
    - Phase-out starting at $75,000 ($112,500 for HoH, $150,000 for MFJ)
    - Credit reduced by $5 per $100 of income above threshold
    - Advance payments were distributed in early 2021 based on 2019 eligibility
    - Credit claimed on 2020 tax return

Present Legislation – The Consolidated Appropriations Act of 2021

- ***Income Exclusions***
  - **Qualified Disaster Distribution**
    - Extension to apply to Federally declared disasters through February 25, 2021 (COVID only relief expired December 2020)
    - Applies to qualified distributions on or before June 24, 2021
    - Must have experienced an economic hardship
    - Maximum distribution that can qualify is $100,000 (per disaster)
    - Qualified distribution can be re-contributed over a 3-year span

Present Legislation – The Consolidated Appropriations Act of 2021

- ***Income Exclusions***
  - **Discharge of Qualified Principal Residence Indebtedness -** Under pre-Act law, discharge of indebtedness income from qualified principal residence debt, up to a $2 million limit for married filing joint taxpayers ($1 million for MFS) for tax years beginning before January 1, 2021, was excluded from gross income.
  - The CAA extended this exclusion from gross income for discharge of principal residence indebtedness to tax years beginning before January 1, 2026, but reduced the maximum indebtedness limit to $750,000 for married filing joint taxpayers ($375,000 MFS).

Present Legislation – The Consolidated Appropriations Act of 2021

- ***Income Exclusions***
  - **Payments of Student Loans by Employers** - Under Code §127, educational assistance provided under an employer's qualified educational assistance program, up to an annual maximum of $5,250, is excluded from the employee's gross income.
  - The CARES Act added to the educational payments excludable from an employee's gross income "eligible student loan repayments" made after March 27, 2020, and before January 1, 2021.
  - The CAA extends this exclusion for loan payments made through 2025.

Present Legislation – The Consolidated Appropriations Act of 2021

- ***Deductions***
  - **Above-the-line Charitable Contributions Deduction** – For 2020, individuals who do not itemize deductions may take up to a $300 above-the-line deduction for cash contributions to qualified charitable organizations. The $300 limit applied to both single and married filing joint taxpayers.

  - The CAA extends the above-the-line deduction rule through 2021, and expands the deduction for married filing joint taxpayers to $600.

  - Charitable Contribution AGI Limitation – 100% rule extended through 2021.

Present Legislation – The Consolidated Appropriations Act of 2021

- ***Deductions***
  - **Reduction in Medical Expense Deduction Floor** – Under pre-CAA law, for tax years beginning before January 1, 2021, individuals could claim an itemized deduction for unreimbursed medical expenses to the extent such expenses exceeded 7.5% of their AGI.
  - The CAA makes the 7.5% threshold permanent, applicable for tax years beginning after December 31, 2020.

  - **$250 Educator Expense Deduction** – the above-the-line deduction for qualified educators is expanded to include the purchase of PPE, including masks, disinfectants, etc. for the classroom.

Present Legislation – The American Rescue Plan Act of 2021

- ***<u>Round 3 of Recovery Rebate</u>***
  - **Additional 2021 Refundable Credit**
    - $1,400 per family member
    - Phase-out starting at $75,000 ($112,500 for HoH, $150,000 for MFJ)
    - Fully phase-out at $80,000 ($120,000 for HoH, $160,000 for MFJ)
    - Advance payments were distributed in early 2021 based on 2019 or 2020 eligibility
    - Credit claimed on 2021 tax return
    - No repayment provision

Present Legislation – The American Rescue Plan Act of 2021

- ***Unemployment Benefits***
  - **Extended additional Federal unemployment of $300 through September 6, 2021**
    - 2020 Unemployment Benefits
      - Exclusion of $10,200 (IRS statement on March 12, 2021)
      - IRS was to make automatic adjustments if 2020 return was filed prior to the law passing
    - 2021 Unemployment Benefits are taxable

Present Legislation – The American Rescue Plan Act of 2021

- ***Changes to Credits***
  - **Additional Child Tax Credit**
    - $3,600 per child 6 and younger
    - $3,000 per child aged 7-17
    - Fully refundable (previous law credit was $2,000 and up to $1,400 refundable)
    - Phase-out starting at $75,000 ($112,500 for HoH, $150,000 for MFJ)
    - Advance payments began in July 2021
    - Repayment provision if not eligible when return is filed

Present Legislation – The American Rescue Plan Act of 2021

- ***Changes to Credits***
  - **Child and Dependent Care Credit**
    - Expanded and made refundable (applicable only in 2021)
    - 50% of eligible expenses up to $8,000 ($16,000 for two or more children)
      - 50% threshold phases down to 20%
      - Phase-out begins at $125,000
      - 20% applies at $185,000 and above
    - Dependent Care FSA threshold increased from $5,000 to $10,500 for 2021

Proposed Legislation

The Build Back Better Act

- ***<u>Provisions Removed from Original Draft</u>***
  - Raise the top individual income tax rate to 39.6 percent for single filers making above $400,000, for head of household filers above $425,000, and for joint filers above $450,000 (effective 1/1/2022).
  - Make permanent ARPA's modifications to the Child and Dependent Care Tax Credit (CDCTC).
  - Increase the top capital gains tax rate from 20 percent to 25 percent, and adjust the top capital gains tax bracket to $400,000 for single filers, $425,000 for head of household filers, and $450,000 for joint filers (effective 9/13/2021).

The Build Back Better Act

- ***<u>Provisions Removed from Original Draft</u>***

  - Extend the holding period for carried interest from three years to five years.

  - Limit the maximum value of the Section 199A passthrough deduction to $500,000 for joint filers and $400,000 for single filers, $250,000 MFS, $10,000 trusts.

Major Provisions of the Build Back Better Act

- ***Estate and Gift Taxes (Removed from Original Draft)***
  - Reduce the estate tax exemption beginning in 2022 (currently scheduled to occur in 2026) to $5,000,000 ($6,020,000 as adjusted for inflation).
  - Grantor Trusts – assets included in estate if deceased is deemed owner.
    - Effective for trusts created after the date of enactment.
  - Valuation discounts not eligible on transfer of interests holding nonbusiness assets.
    - Example: Family LP holding marketable securities

The Build Back Better Act

- ***<u>Individual Income Taxes</u>***
  - Create a 5 percent surcharge on modified gross adjusted income above $10 million (effective 1/1/2022).
    - $5 million for MFS
    - $200,000 for estates and trusts
  - Create a 3 percent surcharge on modified gross adjusted income above $25 million (effective 1/1/2022).
    - $12.5 million for MFS
    - $500,000 for estates and trusts

Major Provisions of the Build Back Better Act

- ***Individual Income Taxes Continued***
  - Prohibit IRA contributions when balances reach $10 million (effective 1/1/2022) – RMDs accelerated – modified to be effective beginning in 2029.
  - Extend the American Rescue Plan Act (ARPA) Child Tax Credit (CTC) expansion through 2025, and make the entire CTC fully refundable on a permanent basis.
  - Extend through 2022 ARPA's temporary expansion of the Earned Income Tax Credit (EITC) eligibility, phase-in rates, and amount.

Major Provisions of the Build Back Better Act

- ***<u>Individual Income Taxes Continued</u>***
  - SALT Deduction cap increased to $80,000 ($40,000 for estate, trust, and MFS)
  - Paid Leave Benefits excluded from gross income
  - Extension of period of limitation for certain legally married couples
  - Pell Grants not taxable if used for non-tuition expenses such as room and board
  - Deduction up to $250 for dues to labor organization

Major Provisions of the Build Back Better Act

- ***<u>Pass-through Business Taxes</u>***
  - Net Investment Income Tax (NIIT) – expand the NIIT to apply to the trade or business income of high-income individuals.
    - MFJ $500,000 (Single $400,000)
    - Top Tax Rate Above $10 million is 45.8%
    - Top Tax Rate Above $25 million is 48.8%
  - Make permanent the active pass-through loss limitation enacted in the 2017 Tax Cuts and Jobs Act (TCJA) – effective for 2021 retroactive.

Major Provisions of the Build Back Better Act

- ***Energy Credits***
  - Extension and increase of nonbusiness energy credit (2022 – 2031)
    - 30% of qualified costs (was 10%)
    - Annual limit of $1,200 (was lifetime limit of $500)
  - Extension of residential energy efficient property credit (through 2033)
    - 2021 = 26%
    - 2022 – 2031 = 30%
    - 2032 = 26%
    - 2033 = 22%

New York State Tax Update for Businesses

New York State Corporate Tax Rates

- ***<u>Corporate Franchise Tax Rate Increases</u>***
  - The 2021-2022 New York State Budget, signed into law on April 19, 2021, included increases to the corporate tax, as follows:
    - For tax years beginning on or after January 1, 2021, and before January 1, 2024, the rate applicable for entities with a business income base allocated to New York in excess of $5 million is increased to 7.25%, up from 6.50% in 2020.
    - For tax years beginning on or after January 1, 2021, and before January 1, 2024, the capital base tax is increased to a rate of 0.1875% for every dollar of the taxpayer's business and investment capital allocated to New York, up from 0.025%.

New York State – Remote Employees

- ***Remote Employees***
  - Taxpayers that have required some or all their employees to work remotely as a result of the state disaster emergency caused by COVID-19, may designate that remote work as having been performed at the location where the work was performed prior to the declaration of the emergency for purposes of tax benefits based on maintaining a presence within the state or within specific areas of the state.

New York State Pass-Through Entity Tax (PTET)

- On August 25, 2021, the New York State Department of Taxation and Finance released guidance (Technical Memorandum, TSB-M-21(1)C, (1)I) addressing a recently enacted optional Pass-Through Entity Tax (PTET) that partnerships and New York S corporations may elect to pay for tax years beginning on or after January 1, 2021.
- Entities that elect to be subject to the PTET will pay a graduated tax of up to 10.9 percent on their NYS taxable income at the entity level, while their individual partners, members, and shareholders will receive a refundable tax credit equal to the pro rata share of taxes paid by the electing entity.

New York State PTET – Tax Rate Schedule

If the PTE taxable income is:	then the PTET due is:
$2 million or less	6.85% of PTE taxable income.
greater than $2 million but less than or equal to $5 million	$137,000 plus 9.65% of the excess of PTE taxable income greater than $2 million.
greater than $5 million but less than or equal to $25 million	$426,500 plus 10.30% of the excess of PTE taxable income greater than $5 million.
greater than $25 million	$2,486,500 plus 10.90% of the excess of PTE taxable income greater than $25 million.

New York State PTET (Continued)

- ***<u>Why would taxpayers want to elect to pay a pass-through entity tax</u>*?**
  - The PTET is intended to provide a workaround to the Federal SALT cap that was enacted with the Tax Cuts and Jobs Act (TCJA) of 2017. The TCJA limited deductions for state and local income taxes to $10,000, thus eliminating the deduction for state income taxes for the vast majority of business owners.
  - The PTET will now effectively allow pass-through entities to take a Federal income tax deduction for their state income taxes, which they were previously disallowed from taking.
  - The Federal deduction for the PTET also reduces the self-employment income for entities taxed as a partnership.

New York State PTET (Continued)

- ***Who Qualifies*?**
  - **Eligible partnership:** Any partnership [including a limited liability company (LLC) treated as a partnership for Federal income tax purposes] that has a filing requirement under Tax Law § 658(c)(1) and is not a publicly traded partnership. A partnership is eligible to make the election even if it has partners that are not eligible for the PTET credit, including, but not limited to, corporate partners.
  - **Eligible S corporation**: Any New York S corporation (including an LLC treated as an S corporation for New York and Federal income tax purposes) as defined by Tax Law § 208.1-A that is subject to the fixed dollar minimum tax under Tax Law § 209.

New York State PTET (Continued)

- ***<u>Who Does Not Qualify</u>*?**
  - **C Corporations:** Not eligible. Not a pass-through entity and are already allowed to deduct state income taxes at the Federal level.
  - **Important Caveat:** While Partnerships and New York S Corporations qualify to make the election, they cannot pass-through the PTET credit to certain partners/members/shareholders. These include:
    - S Corporation partners of a partnership
    - C Corporation partners of a partnership
    - Certain non-grantor style trusts
  - **Single-Member LLCs:** Not eligible, as they are a disregarded entity for tax purposes. A SMLLC would need to incorporate and elect S Corporation status for Federal and NYS tax purposes.

New York State PTET (Continued)

- ***<u>Making the Election</u>***
  - An eligible entity must elect to <u>opt into</u> the PTET online on an annual basis, and such election is irrevocable for the tax year it is made. The election must be made by an authorized person of the organization, which includes any member, partner, owner, or other individual with authority to bind the entity and sign tax returns. CPA's are not considered an authorized person, and therefore cannot make the election on the client's behalf.
  - **2021 Election:** Must have been made by October 15, 2021.
  - **2022 Election and Future Years:** Must be made on or after January 1st but no later than March 15th.

New York State PTET (Continued)

- ***<u>Estimated Tax Payments and Annual Returns</u>***
  - **2021 Estimated Tax Payments:** Estimated PTET payments are optional in 2021 and may be made prior to December 31, 2021.
  - **Tax Planning Opportunity:** <u>Cash-basis entities</u> should compute their estimated PTET in December of 2021 and make an estimated tax payment by December 31, 2021, in order to receive an accelerated 2021 Federal income tax deduction.
  - <u>Accrual-basis entities</u> can compute and accrue the PTET, and still receive the deduction in 2021 even though the tax will not be paid until 2022.

New York State PTET (Continued)

- ***<u>Estimated Tax Payments and Annual Returns</u>***
  - **2022 and Future Years - Estimated Tax Payments:** Estimated tax payments must be made on a quarterly basis (due March 15, June 15, September 15 and December 15). Each payment should be equal to 25% of the required annual payment for the taxable year, which is the lesser of : 1) 90% of the current year tax; or 2) 100% of the prior year tax.
  - **Annual PTET Returns:** Electing entities **<u>must</u>** file an annual PTET return on or before March 15th of the following year. New York State has issued guidance on how the tax is computed, but we have not seen any tax returns as of yet.
    - What if my PTET computes to a loss? The electing entity is still required to file a "no balance due" PTET return.

New York State PTET (Continued)

- ***<u>Claiming the Credit</u>***
  - Eligible taxpayers must claim their PTET credit on Form IT-653, Pass-Through Entity Tax Credit, and attach the form to their individual New York State income tax return. The PTET credit may not be claimed on group returns filed for nonresident partners (i.e., Form IT-203-GR) or nonresident shareholders of S corporations (i.e., Form IT-203-S). **Taxpayers with PTET credits exceeding the tax due for the year may have the excess credit refunded.**

New York State PTET – Example – S-Corporations

ABC Corporation has 3 owners		
Federal Taxable income is 1.2 million		
NYS sales apportionment is 87%		
Ownership % are as follows:		
A	40%	
B	35%	
C	25%	
Total	100%	

	Step 1.	Net PTET Income		1,200,000	
	Step 2.	Net PTET Income		1,200,000	
		Apportionment %		87%	
		PTET Income		1,044,000	
	Step 3.	PTET Income		1,044,000	
		Tax		6.85%	
				71,514	
	Step 4.		Ownership	Total Credit	Allocated Credit
		A	40%	71,514	28,606
		B	35%	71,514	25,030
		C	25%	71,514	17,879

Note: The shareholders receive a combined Federal income tax deduction of $71,514. Assuming they are in the 32% tax bracket, they would recognize Federal income tax savings of approximately $23,000.

New York State PTET – Example – S-Corporations – Potential Pitfall

- What if the majority of my products are being shipped to other states and do not constitute New York State sales? Let's look at the previous example but change the New York State sales apportionment percentage to 5% instead of 87%.

New York State PTET – Example – S-Corporations - Potential Pitfall

ABC Corporation has 3 owners		
Federal Taxable income is 1.2 million		
NYS apportionment % is 5%		
Ownership % are as follows:		
A	40%	
B	35%	
C	25%	
Total	100%	

Step 1.	Net PTET Income		1,200,000	
Step 2.	Net PTET Income		1,200,000	
	Apportionment %		5%	
	PTET Income		60,000	
Step 3.	PTET Income		60,000	
	Tax		6.85%	
			4,110	
Step 4.		Ownership	Total Credit	Allocated Credit
	A	40%	4,110	1,644
	B	35%	4,110	1,439
	C	25%	4,110	1,028

Note: The shareholders receive a combined Federal income tax deduction of only $4,110 based on the decrease in apportionment. Assuming they are still in the 32% tax bracket, they would recognize Federal income tax savings of only approximately $1,300.

New York State PTET – Other State Considerations

- New York State is not the only state implementing a pass-through entity level tax to circumvent the SALT cap. The following two slides show the other states that have or will be implementing similar taxes in 2021 and 2022.
- If you are doing business in a multi-state environment, you may want to consider elections in the following states, as well as New York State:

New York State PTET – Other States with PTE Taxes

- Alabama – Elective PTE Tax effective 1/1/2021
- Connecticut – Mandatory PTE Tax effective 1/1/2018
- California – Elective PTE Tax effective 1/1/2021
- Idaho – Elective PTE Tax effective 1/1/2021
- Illinois – Elective PTE Tax effective 1/1/2021
- Louisiana – Elective PTE Tax effective 1/1/2019
- Maryland – Elective PTE Tax effective 1/1/2020
- Massachusetts – Elective PTE Tax effective 1/1/2021

New York State PTET – Other States with PTE Taxes

- Minnesota – Elective PTE Tax effective 1/1/2021
- New Jersey – Elective PTE Tax effective 1/1/2020
- Oklahoma – Elective PTE Tax effective 1/1/2019
- Oregon – Elective PTE Tax effective 1/1/2021
- Rhode Island – Elective PTE Tax effective 1/1/2019
- South Carolina – Elective PTE Tax effective 1/1/2020
- Wisconsin – Elective PTE Tax effective 1/1/2019

Other States with PTE Taxes Becoming Effective 1/1/2022

STATES WITH PTE TAX IN EFFECT AFTER TY2021

State	Effective Date	Election Due Date	Estimate Due Date	Return Due
Arizona	1/1/2022	On or before the due date or extended due date of return	4/15, 6/15, 9/15, 12/15 (pending)	3/15
Arkansas	1/1/2022	On or before the original or extended due date of the return	4/15, 6/15, 9/15, 1/15	4/15
Colorado	1/1/2022	4/15 (pending)	Pending	4/15 (pending)
Georgia	1/1/2022	On or before the original or extended due date of the return	Pending	3/15

New York State PTET (Continued)

- ***<u>What Happens to PTET if the SALT Cap is Eliminated</u>*?**
    - New York State has not formally addressed this question, but other states such as California have it written into their PTE law. California's law automatically repeals itself if the Federal SALT cap is removed. It would seem likely that other states would follow suit, but we cannot be sure.

New York State Tax Update for Individuals

New York State Individual Tax Updates

- ***Continuing Middle-Class Tax Cuts***
  - This year's Enacted Budget continues to lower personal income tax rates for middle-class taxpayers:
    - For married filing joint taxpayers, the tax rate for taxable income over $27,000 but not more than $161,550, a phased-in reduction from two brackets at 5.9% and 6.09% to a single bracket at 5.5% will continue through 2025 (single taxpayers with taxable income over $13,900 but not more than $80,650).
    - For married filing joint taxpayers, the tax rate for taxable income over $161,550 but not more than $323,200, a phased-in reduction from 6.41% to 6.0% will continue through 2025 (single taxpayers with taxable income over $80,650 but not more than $215,400).

New York State Individual Tax Updates

- **<u>New Tax Rates for High Income Taxpayers</u>**
  - Effective for tax years beginning on or after January 1, 2021, NYS has added three new tax brackets for “high income taxpayers.” The new tax rates are, as follows:
    - For taxable income > $2,155,350 (MFJ) and > $1,077,550 (single), the 8.82% top rate is increased to 9.65%.
    - For taxable income > $5M (MFJ and single), a new 10.3% rate applies.
    - For taxable income > $25M, a new 10.9% rate applies.

2022 Tax Inflation Amounts

Tax Inflation Adjustments for Tax Year 2022

- The standard deduction for married couples filing jointly for tax year 2022 rises to $25,900, up $800 from the prior year. For single taxpayers and married individuals filing separately, the standard deduction rises to $12,950 for 2022, up $400, and for heads of households, the standard deduction will be $19,400 for tax year 2022, up $600.

- Marginal Rates: For tax year 2022, the top tax rate remains 37% for married couples filing jointly taxpayers with incomes greater than $647,850 ($539,900 for single taxpayers). The other rates are:
  - 35%, for incomes over $431,900 ($215,950 for single taxpayers);
  - 32% for incomes over $340,100 ($170,050 for single taxpayers);
  - 24% for incomes over $178,150 ($89,075 for single taxpayers);
  - 22% for incomes over $83,550 ($41,775 for single taxpayers);
  - 12% for incomes over $20,550 ($10,275 for single taxpayers); and
  - The lowest rate is 10% for married couples filing jointly with income of $20,550 or less ($10,275 for single taxpayers).

Tax Inflation Adjustments for Tax Year 2022

- Capital Gains Rates: For tax year 2022, the capital gains rates currently in effect are, as follows:
  - The 0%, rate applies to net capital gains up to $83,350 ($41,675 for single taxpayers);
  - The 15% rate applies to net capital gains over the above thresholds and up to $517,200 ($459,750 for single taxpayers); and
  - The 20% rate applies to net capital gains over $517,200 ($459,750 for single taxpayers).

Tax Inflation Adjustments for Tax Year 2022

- For 2022, the FICA tax rate for employers is 7.65%—6.2% for OASDI and 1.45% for HI (the same as in 2021).
- 6.2% Social Security tax on the first $147,000 of wages (maximum tax is $9,114.00 [6.2% of $147,000]); plus
- 1.45% Medicare tax on the first $250,000 of wages ($200,000 for single taxpayers; $125,000 for married taxpayers filing a separate return); plus
- 2.35% Medicare tax (regular 1.45% Medicare tax + 0.9% additional Medicare tax) on all wages in excess of $250,000 ($200,000 for single taxpayers; $125,000 for married taxpayers filing a separate return).

Tax Inflation Adjustments for Tax Year 2022

- **Contributions to a Traditional IRA, here are the phase-out ranges for 2022**
  - For single taxpayers covered by a workplace retirement plan, the phase-out range is $68,000 to $78,000, up from $66,000 to $76,000.
  - For married couples filing jointly, where the spouse making the IRA contribution is covered by a workplace retirement plan, the phase-out range is $109,000 to $129,000, up from $105,000 to $125,000.
- For an IRA contributor who is not covered by a workplace retirement plan and is married to someone who is covered, the deduction is phased out if the couple's income is between $204,000 and $214,000, up from $198,000 and $208,000.
  - For a married individual filing a separate return who is covered by a workplace retirement plan, the phase-out range is not subject to an annual cost-of-living adjustment and remains $0 to $10,000.
- The limit on annual contributions to an IRA (Traditional or Roth) remains unchanged at $6,000. The additional catch-up contribution limit for individuals aged 50 and over is not subject to an annual cost-of-living adjustment and remains $1,000.

Tax Inflation Adjustments for Tax Year 2022

- **Phase-outs for Roth IRA Contributions**
  - The income phase-out range for taxpayers making contributions to a Roth IRA is $129,000 to $144,000 for singles and heads of household, up from $125,000 to $140,000. For married couples filing jointly, the income phase-out range is $204,000 to $214,000, up from $198,000 to $208,000. The phase-out range for a married individual filing a separate return who makes contributions to a Roth IRA is not subject to an annual cost-of-living adjustment and remains $0 to $10,000.
- The limit on contributions by employees who participate in 401(k), 403(b), most 457 plans, and the Federal government's Thrift Savings Plan is $20,500, up from $19,500.
- The catch-up contribution limit for employees aged 50 and over who participate in these plans remains unchanged at $6,500.
- The limitation regarding SIMPLE retirement accounts is $14,000, up from $13,500. The catch-up contribution for those age 50 or older remains unchanged at $3,000.

Tax Inflation Adjustments for Tax Year 2022

- **Health Savings Account Deductions**
  - The annual limit on contributions to (and deductions for) Health Savings Accounts for high-deductible health plans is increased to $3,650 for self-only coverage and $7,300 for family coverage.
- **Kiddie Tax**
  - The exemption from the kiddie tax for 2022 will be $2,300, up from $2,200. A parent will be able to elect to include a child's income on the parent's return for 2022 if the child's income is more than $1,150 and less than $11,500, up from $1,100 and $11,000.

Questions

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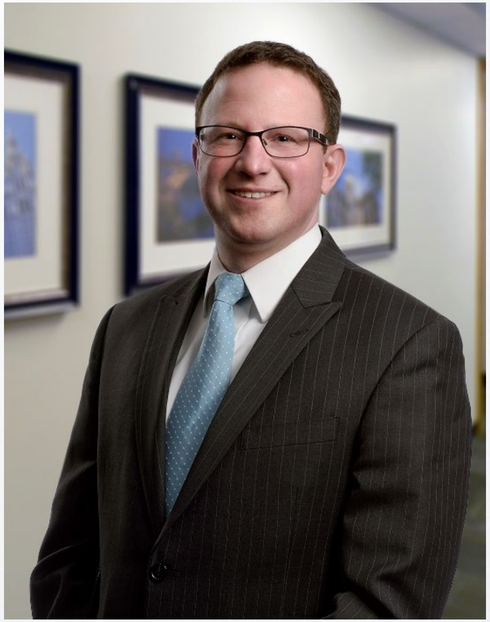

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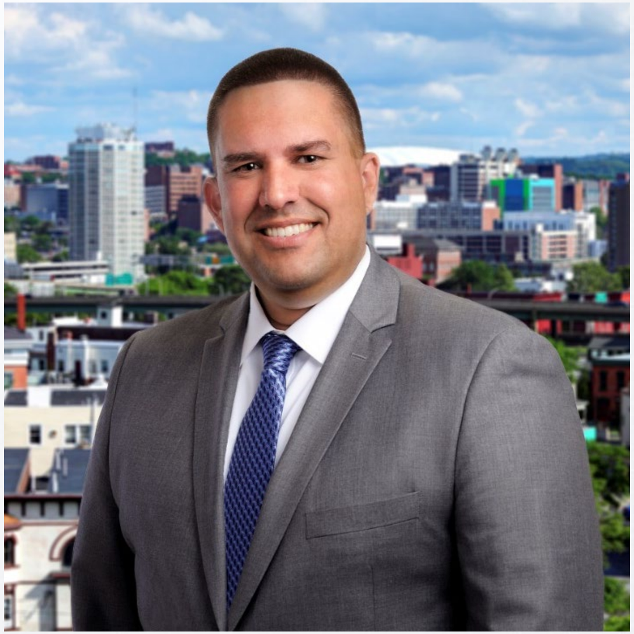

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