HITT AND COMPANY, LLC

CLIENT TAX NEWSLETTER - Fall 2020

CALENDAR

- **OCTOBER 15, 2020**
PERSONAL AND CORPORATION RETURNS – EXTENDED DEADLINE

- **OCTOBER 31, 2020**
HALLOWEEN

- **NOVEMBER 1, 2020**
DAYLIGHT SAVINGS TIME ENDS

- **NOVEMBER 26, 2020**
THANKSGIVING DAY

Election 2020: Comparing the Biden and Trump Tax Plans

Now that the conventions of both major parties have wrapped up, we're heading into the home stretch of the presidential election race. Naturally, taxes will be a major point of contention. Although President Trump hasn't released a formal plan yet, he has generally expressed his intent to preserve, and expand on, the Tax Cuts and Jobs Act (TCJA) passed in 2017. Conversely, former Vice President Biden has cobbled together a series of proposals on certain specific points. Following is a brief comparison.

Joe Biden's Tax Plan

- **Individual tax rates**: Currently, the top tax rate is 37%, down from the highest rung of 39.6% prior to the TCJA. Biden wants to restore the 39.6% rate for folks with taxable income above $400,000.

- **Itemized deductions:** The TCJA limited certain itemized deductions while raising the standard deduction. Biden has proposed a provision that would cap the tax benefit of itemized deductions at the 28% rate.

- **Capital gains and dividends**: The tax law provides favorable tax treatment for long-term capital gains and qualified dividends. Under Biden's plan, the breaks would disappear for capital gains and dividends above $1 million.

- **Individual tax credits**: Current law includes a maximum $2,000 Child Tax Credit (CTC), plus a $500 dependent credit, and a maximum dependent care credit of $600 ($1,200 for two or more children). Among other changes, Biden would hike the CTC to $8,000 ($16,000 for two or more children).

- **Education**: Generally, student loan debt that is forgiven is taxable to the taxpayer obligated to pay the debt. One of Biden's proposals relating to higher education would provide a special tax exclusion for student loan forgiveness.

- **Corporate tax rates**: The TCJA replaced the graduate corporate structure with a flat 21% rate and repealed the corporate alternative minimum tax (AMT). Biden has proposed raising the flat rate to 28% and reinstating the corporate AMT on profits of more than $100 million

- **Payroll taxes**: Biden has floated the idea of a 12.4% Social Security payroll tax, split between employers and employees, on earned income above $400,000. It would feature a "donut hole" between the prevailing wage base ($137,700 for 2020) and $400,000.

- **Estate tax**: Under the TCJA, the $5 million estate tax exemption was doubled from $5 million to $10 million ($11.58 million for 2020). It is scheduled to revert to $5 million after 2025. Biden would leave the reversion and eliminate the current step-up in basis on inherited assets.

Donald Trump's Tax Plan

- **Individual tax rates**: Trump intends to keep the top 37% tax rate right where it is. In addition, he would implement a 10% rate cut for middle-income taxpayers, effectively lowering the 22% rate to 15%.

- **Itemized deductions**: Under Trump's plan, the TCJA changes for itemized deductions would be extended beyond 2025, when they are set to expire, and be made permanent.

- **Capital gains and dividends**: Although he has not offered any specifics, Trump has indicated he would reduce tax rates for capital gains, index gains for inflation and create a capital gains tax holiday for a limited time.

- **Individual tax credits**: Essentially, Trump hasn't proposed any major changes for the CTC and dependent credit and the dependent care credit. However, he would require Social Security numbers to be eligible for any of these credits.

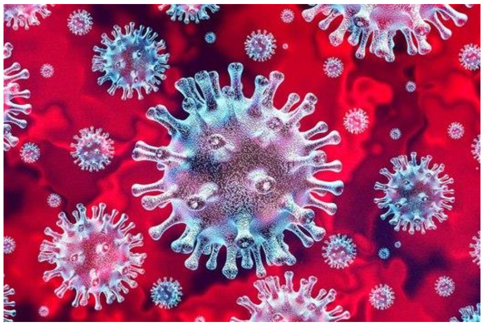
- **Education**: Under current law, you generally can't realize tax benefits for contributions to state-authorized organizations sponsoring scholarships (other than a possible charitable deduction). Trump would provide a tax credit for individual and corporate donations to such organizations.

- **Corporate tax rates:** Trump wants to preserve the status quo under the TCJA. He has no plans to reinstate a corporate AMT.

- **Payroll taxes:** The president recently issued an executive order that postpones Social Security tax for employees for September 1 through the end of 2020. He has said that this reprieve could turn into a permanent extension.

- **Estate taxes:** Trump has stated that he will push to extend the more generous estate tax exemption and would not change the rules relating to a step-up in basis.

This is hardly the end of the story. We will update you on any important developments as the candidates of the two major political continue to shape their tax plans before the election.



Coronavirus Unemployment Payments are Taxable: Be Prepared by Withholding

By law, unemployment compensation is taxable and must be reported on a 2020 federal income tax return. Taxable benefits include any of the special unemployment compensation authorized under the Coronavirus Aid, Relief, and Economic Security (CARES) Act.

With millions of Americans now receiving taxable unemployment compensation, many of them for the first time, people receiving unemployment compensation can have tax withheld from their benefits now to help avoid owing taxes on this income when they file their federal income tax return next year. By law, unemployment compensation is taxable and must be reported on a 2020 federal income tax return. Taxable benefits include any of the special unemployment compensation authorized under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, enacted this spring.

Withholding is voluntary. Federal law allows any recipient to choose to have a flat 10% withheld from their benefits to cover part or all of their tax liability. To do that, fill out Form W-4V, Voluntary Withholding Request (PDF), and give it to the agency paying the benefits. Don't send it to the IRS. If the payor has its own withholding request form, use it instead.
If a recipient doesn't choose withholding, or if withholding is not enough, they can make quarterly estimated tax payments instead. The payment for the first two quarters of 2020 was due on July 15.

Third and fourth quarter payments are due on Sept. 15, 2020, and Jan. 15, 2021, respectively. For more information, including some helpful worksheets, see Form 1040-ES and Publication 505, available on IRS.gov.
Here are some types of payments taxpayers should check their withholding on:

- Unemployment compensation includes: Benefits paid by a state or the District of Columbia from the Federal Unemployment Trust Fund
- Railroad unemployment compensation benefits
- Disability benefits paid as a substitute for unemployment compensation
- Trade readjustment allowances under the Trade Act of 1974
- Unemployment assistance under the Disaster Relief and Emergency Assistance Act of 1974, and
- Unemployment assistance under the Airline Deregulation Act of 1978 Program

Recipients who return to work before the end of the year can use the IRS Tax Withholding Estimator to make sure they are having enough tax taken out of their pay. Available only on IRS.gov, this online tool can help any worker or pension recipient avoid or lessen their year-end tax bill or estimate the refund they want.

In January 2021, unemployment benefit recipients should receive a Form 1099-G, Certain Government Payments (PDF) from the agency paying the benefits. The form will show the amount of unemployment compensation they received during 2020 in Box 1, and any federal income tax withheld in Box 4. Taxpayers report this information, along with their W-2 income, on their 2020 federal tax return.

Health-Related Benefits Under the CARES Act

The Coronavirus Aid, Relief and Economic Security (CARES) Act was signed into law on March 27, 2020, and provides broad economic relief to families (stimulus payments, expanded unemployment compensation, and other provisions) and small businesses (Paycheck Protection Program loans and payroll tax credits, among others) impacted by COVID-19. The following article discusses some of the health-related benefits under the CARES Act; review the benefits and share these with your clients.

Expansion of qualified medical expenses

Effective for amounts paid after Dec. 31, 2019, the definition of "qualified medical expenses" for purposes of various tax-advantaged accounts has been expanded. These include health savings accounts (HSAs), Archer medical savings accounts (MSAs), health flexible spending accounts (FSAs), and health reimbursement arrangements (HRAs). Qualified medical expenses now permanently include over-the-counter medications without a prescription, such as pain and allergy medication, and the cost of menstrual care products, including tampons, pads, liners, cups, sponges, or other similar products. Taxpayers should save receipts from these purchases for their records and for submitting claims for reimbursements.

Safe harbor for telehealth services

For services provided on or after Jan. 1, 2020, and for plan years beginning on or before Dec. 31, 2021, high-deductible healthcare plans (HDHPs) with HSAs provide coverage for telehealth or other remote care services without a deductible or having to satisfy the plan's minimum deductible. In addition, an otherwise eligible individual with coverage under an HDHP may still contribute to an HSA, despite receiving coverage for telehealth and other remote care services before satisfying the HDHP deductible, or despite receiving coverage for these services outside the HDHP.

This measure encourages the use of remote health services, helps ease the burden on in-person facilities, and ultimately limits the spread of the virus.

Increased flexibility in Sec. 125 cafeteria plans

According to IR-2020-95, the IRS has temporarily loosened the rules around Sec. 125 cafeteria plans because of unanticipated changes in expenses due to COVID-19. The claims period for taxpayers to apply any unused amounts remaining in an FSA or dependent care assistance program for expenses incurred has been extended through Dec. 31, 2020. Previously provided temporary relief for high-deductible health plans may be applied retroactively to Jan. 1, 2020. The limit on unused health FSA carryover amounts increased from $500 to $550, as adjusted for inflation.

COVID-19 testing

The Families First Coronavirus Response Act requires health insurers and group health plans to cover COVID-19 testing and related provider visits, and thus eliminates patient cost-sharing obligations under employer-sponsored group health plans. This measure encourages more people to get tested for COVID-19.

Background information

HSA: An HSA is a tax-exempt trust or custodial account set up with a qualified HSA trustee to pay or reimburse certain medical expenses incurred. Your clients may deduct contributions made to an HSA (with certain limits) even if they don't itemize deductions on Form 1040, Schedule A, and contributions made by an employer (including contributions made through a cafeteria plan) may be excluded from income. Earnings on the assets accumulate in the account tax free, and distributions may be tax free if applied to qualified medical expenses. The HSA will stay with the taxpayer even if they change employers or leave the workforce.

FSAs: Health FSAs allow employees to use tax-free dollars to pay for medical expenses not covered by their health plans, such as premiums, deductibles, copayments, eyeglasses, and hearing aids. An employee needs to decide how much to contribute to the health FSA through payroll deductions before the plan year begins. The health FSA limit is $2,750 for 2020. The employee must spend any unspent amounts by the end of the plan year or forfeit the money. However, employers may allow employees more time through a carryover option (carryover up to $500 of unused amounts to the following plan year) or a grace period option (employee has until 2 ½ months after end of plan year to incur expenses).

Archer MSA: An Archer MSA is a tax-exempt trust or custodial account set up with a financial institution in which a taxpayer saves money that will be used for medical expenses incurred in the future. Plan holders are allowed to deduct contributions to these plans (with certain limits) even if they don't itemize deductions on Schedule A. Interest or earnings will grow tax free in the account, and distributions may be tax free if used for qualified medical expenses. The account will stay with the taxpayer even if they change employers or leave the workforce.

HRA: An HRA must be funded solely by an employer, and contributions cannot be paid through a voluntary salary reduction agreement. Employees are reimbursed tax free for qualified medical expenses up to a maximum dollar amount, and there are no reporting requirements on the individual's tax return. Any unused amounts in the HRA can be carried forward for reimbursements in later years.

10 Ways Your Taxes Will Change in 2021

Here's a look at some ways the federal tax return you will file in 2021 will differ from your prior return:

1. Waived RMDs

The Coronavirus Aid, Relief, and Economic Security Act of 2020, better known as the CARES Act, waived required minimum distributions (RMDs) from retirement accounts for 2020.

RMDs generally count as taxable income. So, this one-time reprieve means that some retirees will have lower taxable incomes in 2020 and thus possibly owe less in federal income taxes in 2021.

2. Higher standard deductions

Standard deductions generally rise each year on account of adjustments for inflation. The IRS reports that for 2020, the standard deduction amounts for the following tax-filing statuses are:

- **Married filing jointly**: $24,800 — up $400 from 2019
- **Married individuals filing separately**: $12,400 — up $200
- **Head of household**: $18,650 — up $300
- **Single**: $12,400 — up $200

The standard deduction reduces the amount of your income that's subject to federal taxes. So, if a single person is eligible for and chooses to take the standard deduction (as opposed to itemizing deductions) on their 2020 tax return, they would not be taxed on the first $12,400 of their income from 2020.

3. A charitable deduction available to all
Usually, you can only write off tax-deductible donations to charity on your federal tax return if you itemize your deductions rather than take the standard deduction — and the latter has become far more common since the 2017 overhaul of the federal tax code.

But in an effort to encourage Americans to donate money to charity during the coronavirus pandemic, the CARES Act enabled taxpayers to deduct up to $300 in monetary donations in 2020 — even if they take the standard deduction.

4. Higher income brackets

Income tax brackets also tend to rise annually. For 2020, the income brackets are as follows for folks whose tax-filing status is single:

- **37% tax rate**: Applies to taxable income of more than $518,400
- **35%**: More than $207,350 but not more than $518,400
- **32%**: More than $163,300 but not more than $207,350
- **24%**: More than $85,525 but not more than $163,300
- **22%**: More than $40,125 but not more than $85,525
- **12%**: More than $9,875 but not more than $40,125
- **10%**: Income of $9,875 or less

5. Higher contribution limits for (some) retirement accounts

You can save more money in several types of workplace retirement accounts in 2020….
The base contribution limit for 401(k) plans, for example, is $19,500 — up from $19,000 for 2019. The limit for catch-up contributions, which taxpayers age 50 and older can make, is an additional $6,500 — up from $6,000. So, folks who are at least 50 can contribute a total of $26,000 to a 401(k) in 2020.

Unfortunately, 2020 did not bring any contribution limit increases for individual retirement accounts (IRAs).

6. Higher contribution limits for HSAs

Workplace retirement accounts are not alone. Contribution limits for health savings accounts (HSAs) also tend to increase each year — and 2020 is no exception.

The 2020 contribution limits for folks who are eligible for an HSA and have the following types of high-deductible health insurance policies are:

- **Self-only coverage**: $3,550 — up from $3,500 for 2019
- **Family coverage**: $7,100 — up from $7,000

7. Higher income limits for the Saver's Credit

For 2020, the Saver's Credit, formally known as the Retirement Savings Contributions Credit, has higher income limits. That effectively makes this little-known tax credit available to more people.

You might be eligible for this credit in 2020 if your adjusted gross income, or AGI (found on your tax return), is not more than:

- **Married filing jointly**: $65,000 — up from $64,000 for 2019
- **Head of household**: $48,750 — up from $48,000
- **All other tax-filing statuses**: $32,500 — up from $32,000

8. A more valuable adoption tax credit

The tax credit for qualified adoption expenses is more valuable in 2020. The maximum allowable credit amount is $14,300 — up from $14,080 for 2019.

9. A more valuable Earned Income Tax Credit

For 2020, both the income limits and the maximum credit amount for the Earned Income Tax Credit (EITC) are higher. You might be eligible for the EITC in 2020 if your AGI is not more than:

- **Married filing jointly**: $56,844 — up from $55,952 for 2019
- **All other tax-filing statuses**: $50,594 — up from $50,162

The maximum amount that the EITC is worth in 2020 is $6,660 — up from $6,557.

10. A higher cap on Social Security payroll taxes

One bit of bad news for some folks: The maximum amount of a worker's income that is subject to Social Security payroll taxes rose to $137,700 for 2020 — up from $132,900 for 2019.