Purk
& Associates, P.C.
CPAs and Business Advisors

Year-End Tax Planning For Businesses

As the end of the year approaches it is important to consider strategies to lower your tax liabilities for 2020. Here are ten strategies that may help in reducing your tax bill.

Timing of Income and Deductions

If you're a sole proprietor or an owner of a pass-through entity, your business net income flows through to your personal return and is taxed at personal rates. Taxpayers should consider whether or not they might fall into a higher or lower tax bracket in 2021 relative to 2020. Changes in the economy, your business, other income, and tax laws may have an effect on your tax bracket and tax rates.

If you expect your business income will be taxed at the same or lower rate next year, you may want to accelerate expenses for 2020 and defer revenue to next year. On the other hand, if you expect to be in a higher tax bracket next year, then you may want to take the opposite approach.

Section 179 Deductions

Section 179 allows a business to deduct the full cost of purchasing or leasing eligible new or used assets up to certain limits. The business can deduct up to $1.04 million of expense for assets placed into service in 2020. If the business purchases more than $2.59 million of eligible assets in 2020, then the amount it's able to deduct is reduced dollar for dollar for any expenditures in excess of $2.59 million. So each dollar spent over the $2.59 million limit reduces the $1.04 million deduction by a dollar. If you're able to take advantage of this deduction, it can only be used to offset net income and can't be used to create a net operating loss.

Bonus Depreciation

Under the Tax Cuts and Jobs Act, 100% first-year bonus depreciation is available for qualified business assets acquired and placed into service after September 27, 2017. This generally applies to depreciable business assets with a recovery period of 20 years or less and certain other property. Machinery, equipment, computers, appliances, and furniture generally qualify. The 100% depreciation will begin to phase out in 2023, so current law provides for the 100% cap for the next few years. If you believe that your tax rate will increase in future years, then it may be beneficial to delay asset purchases to next year or not take the bonus depreciation in 2020 on assets already purchased.

Bonus Depreciation for Qualified Improvement Property (QIP)

Qualified Improvement Property is generally defined as any improvement to a commercial building's interior after the building was placed into service. It does not include the enlargement of a building, any elevator or escalator or improvements to the internal structural framework of the building. The Tax Cuts and Jobs Act had assigned a 39-year depreciation to Qualified Improvement Property expenditures.

The CARES Act changed this by assigning a 15-year depreciation to Qualified Improvement Property placed into service after 2017. This means that Qualified Improvement Property placed in service in 2020 qualifies for the 100% first-year Bonus Depreciation. Additionally, Qualified Improvement Property placed into service in 2018 and 2019 retroactively qualifies for the Bonus Depreciation too.

Bonus Depreciation for Heavy SUV, Pickup, or Van

Heavy SUVs, pickups and vans qualify for 100% first-year bonus depreciation and Sec. 179 expensing if used more than 50% for business. The normal Section 179 expensing limit generally applies to vehicles with a gross vehicle weight rating of more than 14,000 pounds. A $25,900 limit applies to vehicles rated at more than 6,000 pounds, but no more than 14,000 pounds.

Modification of limitation on the business interest

The CARES Act temporarily increased the amount of interest expense that businesses are allowed to deduct on their tax returns, by increasing the 30% limitation to 50% of the taxable income for 2019 and 2020. Also, if 2020 is less profitable than 2019, then the business can use the 2019 taxable income amount for the 2020 filing.

Research and Development Tax Credits

Businesses that invest in research and development of new products and processes or have improved upon the performance, functionality, reliability, or quality of existing products or processes may be eligible for the research and development tax credit. The credit is based on specific types of R&D activities and expenditures and can be a bit complicated to calculate. However, this remains a very popular tax credit with both large and small companies. If you have a small start-up business, you may elect to use up $250,000 credit toward its FICA tax liability if your business had less than $5 million in gross receipts for the current and no more than five years of gross receipts.

Work Opportunity Tax Credit

If you have hired or are planning to hire employees in 2020, you'll want to look into the Work Opportunity Tax Credit. To qualify for this credit you must hire from targeted groups such as certain veterans, ex-felons, individuals who've been unemployed for 27 weeks or more and food stamp recipients. An employer can hire multiple members of a targeted group and receive a credit for each. The maximum credit amount is generally $2,400 per employee but can be as high as $9,600 per employee for certain targeted groups. This credit is set to expire on December 31, 2020.

Establish a Tax-Favored Retirement Plan

If you're a business owner and don't already have a retirement plan set up for your business, now may be a great time to get started. With a retirement plan, contributions can be made by the employer, employee, or both. Employer contributions are generally tax-deductible for business. With most plans, employee contributions are made pre-tax and grow tax-deferred until the employee takes qualified distributions. A retirement plan is a great way for a business owner to personally realize significant tax benefits from both the business and employee contributions. If you do establish a new qualified retirement plan for your business, you may be eligible for a tax credit of up to $5,000.

Net Operating Losses

Under the CARES Act, if you incur a Net Operating Loss in 2020 or incurred a Net Operating Loss in 2019 or 2018, you can choose to carry it back for up to the previous five years in order to recover taxes paid in those earlier years. Or you can choose to carry the loss forward to future years if you have losses in excess of taxable income or if you expect business tax rates to go up.

Pass-through Entity "Excess" Business Losses

For pass-through businesses, the CARES Act modifies the loss limitation for the noncorporate taxpayer. Normally, pass-through losses were limited to $250,000 per return for individuals or $500,000 per return for married filing jointly. Any excess losses were then carried forward. However, the CARES Act eliminates the limitation for 2018, 2019, and 2020.

Maximize QBI Deduction for Pass-Through Business Income

Section 199a of the Internal Revenue Code provides sole proprietorships and owners of pass-through entities with a deduction of up to 20% of qualified business income. There are limitations based on income level, type of business, and W2 compensation paid to employees of the business. Regardless, if you receive pass-through business income, you should determine if you qualify and if so, maximize the deduction.

Final Thoughts

As always, we encourage you to speak with one of our associates to discuss tax planning for your specific situation. Feel free to contact our office any time. We're always happy to help.

About Purk and Associates

We have hand-picked a team with tax, auditing, accounting, business and management advisory expertise in a multitude of fields, including healthcare, professional-services firms, commercial contractors, home builders, real estate companies, manufacturing and distribution companies, dealerships, non-profit organizations and pension funds.

We have the expertise and the resources to provide not only the critical services you need during these evolving economic times, but also, importantly, to build for the future. Our strategic alliances with professional organizations across the country allow us to bring our clients the talent and expertise of national firms with the high-touch service of a local firm. While we remain focused on the core services of tax, accounting and audit, we expand and offer you the business consulting needed to remain competitive. We believe the success of our clients is the greatest measure of our own.

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