

MARCH 2022 WEBINAR

Talking Taxes

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Tax season is in full swing, and Perry Ghilarducci, founding partner of Avaunt, shared a wealth of information spanning a variety of topics relevant to individuals and business owners, including Federal Economic Impact Payments, Child Tax Credit, Passthrough Entity Tax Credit and COVID-19 Credits for small businesses.

STIMULUS CHECKS

The third round of Federal Economic Impact Payments (stimulus checks), which provided \$1,400 per taxpayer and dependent in 2021, were calculated using 2020 tax returns. These were considered advanced payments toward your 2021 tax return. During the filing of your 2021 return, you need to reconcile the total amount you received with the amount you are eligible to claim.

The government sent Letter 6419 in late January to households verifying the stimulus amount you received from the IRS. If that letter is different from what you received, contact the IRS. They don't always get it right, so Ghilarducci recommends checking to ensure what the government says it sent is indeed what you received.

If you don't know if you received EIP funds, set up an account on IRS.gov. Once you have created the account, you can see what funds were sent to you. You can also check your bank statements for automatic deposits from the IRS.

If you received more money than you should have, (e.g., a taxpayer received too much of an EIP relative to their 2021 Adjusted Gross Income), the good news is there is no repayment requirement.

Ghilarducci pointed out that you do need to review how much you received. If your 2021 income fell below your 2020 income (which is what the EIPs were calculated on), you may qualify for additional money.

CHANGES IN THE CHILD TAX CREDIT FOR 2021 (ARPA)

The Child Tax Credit got a boost with enhanced payments in 2021. In 2020, the credit for children under age six was \$2,000/child. In 2021, there is an enhanced payment of \$1,600 per child, so the total credit is \$3,600/child. The credit for children 6-17 was \$2,000 in 2020, and with the \$1,000 enhancement, the credit increased to \$3,000 in 2021.

The income ceiling to be eligible for those enhancements (\$1,600 or \$1,000) increased to \$162,500. Those who make less than \$162,500 would still be eligible for the standard \$2,000 or \$3,000 credit.

IRS sent Letter 6419 verifying the amount you received. If it indicates a different amount, contact the IRS. If you didn't get the advance payments, and you are entitled to the credit, you can claim the full amount on your 2021 return, even if you don't normally file a tax return.

If you had a baby in 2021, and your stimulus check was based on the number of dependents in 2020, you would be eligible for additional \$3,600 in Child Tax Credits.

CHILD TAX CREDIT REPAYMENT PROTECTION

Since this was an advance payment, if your income changed, and you are above the threshold range, you may have to repay part of the Child Tax Credit. The amount could be decreased based on Adjusted Gross Income (\$60,000-\$120,000). If your income is over \$120,000, you would not qualify for repayment protection.

CALIFORNIA PASS-THROUGH ENTITY TAX CREDIT

In July, California joined 13 other states that have enacted a Pass-through Entity Tax (PTE), which is a workaround for the federal \$10,000 state tax limitation. This credit applies to businesses in California taxed as a partnership or S corporation and has only partners, shareholders, or members – those who receive a K-1; it does not apply to single-owner LLC, independent contractors, self-employed individuals, or publicly traded partnerships. Owners of qualifying entities that elect to pay the PTE tax can claim a tax credit on their California individual income tax returns.

Businesses who receive a K-1 don't get a federal deduction for state and local taxes (SALT) that exceed \$10,000; this is the SALT cap. This PTE credit allows California business owners to have the entity pay the state taxes for its shareholders or members. The business takes 9.3% of the pass-through income that appears on their K-1 and sends that money to the government on the shareholder's behalf.

By allowing the California state taxes to pass through the business, owners pay less federal income tax and avoid the SALT cap. Payments by the entity are credited against the taxpayer's state income taxes like an estimated tax payment.

The PTE tax is retroactive, available for the tax years January 1, 2021 through December 31, 2025 for qualifying companies.

Note that the timing of the payment is critical. If payment is made after year end, deduction for Federal tax does not occur until the year it is paid. For tax year 2021, the PTE tax payment is due on the due date of the original tax return, not including extensions. For tax years 2022-2025, taxpayers must submit the PTE tax in two payments. The first payment is due on June 15th of the taxable year, or on the 15th day of the sixth month for fiscal year taxpayers.

SB113 CHANGES TO THE PASSTHROUGH ENTITY TAX

There was an amendment to the definition of “qualified entity” to include a partnership as an eligible partner, shareholder, mentor, single-member LLCs (SMLLCs) owned by an individual, estate, or trust. SMLLCs can now consent to the PTE tax, and the owner of the SMLLC will receive the PTE tax credit.

This includes guaranteed payments defined by IRC Section 707© as qualified net income, so they can qualify for the credit. If you work in a partnership, you aren’t supposed to get a W-2, which Ghilarducci points out is a common mistake, but you get guaranteed payments. These can be included in the pass-through calculations.

The changes also removed a provision that prohibits credits for PTE tax paid from

reducing tax owed below a taxpayer’s tentative minimum tax, effective for tax years beginning on or after 1/2/21. Requiring the elective tax credit to be applied against the net tax after credits for taxes paid to other states, effective for tax years beginning on or after 1/2/22. This is one of the reasons why people originally didn’t use the pass-through option, but with this change, it removed the limitation of the state tax credit to a tentative minimum tax. Ghilarducci believes there is now no real reason why you wouldn’t participate in it.

This also allows businesses – owned by individuals using a limited liability company that is disregarded for federal income purposes and meets certain conditions – to elect the PTE tax and credit.

COVID-19 FUNDS FOR BUSINESSES

Businesses that were trying to retain their employees during COVID-19 will be happy to hear that the Employee Retention Credit (ERC), the Paid Sick Leave Refundable Credit (PSLRC,) and the Paid Family Leave Refundable Credit (PFLRC) are still available. If your business income dropped in 2020 or 2021, know that a payroll tax credit is still available. These all came out of COVID-19 relief funds, and businesses can claim the credits on an amended return.

Finally, if you are a business owner, and you were on the wait list for California Small Business COVID-19 Relief Grant Program, the government, through SB113, made \$150 million in funding available for the remaining eligible applicants, and these grants are state-tax-free.

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