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2021 Year-End Tax Planning for Businesses

Though the Build Back Better Act (BBBA) hasn't passed yet, there are still some considerations you'll want to think about for your business tax planning. Current versions of the bill do not include an increase from the 21% corporate flat rate.

Business Interest Deduction Limitations

No matter the form, every business in the U.S. is subjected to disallowance of deductions of net interest expenses exceeding 30% of the company's adjusted taxable income, or ATI. The specific disallowance is decided at the tax filer's specific level, but there are special rules that are applied to pass-through entities, requiring a determination at the partnership level rather than at the partner level.

For the 2021 tax year, the ATI is usually computed without looking at deductions that are allowed for depletion, depreciation or amortization. However, there are some exemptions you can take on limits to the deduction of business interest. These include:

- Election to be excepted from these rules can apply to taxpayers outside of tax shelters who have average annual gross receipts over the two prior and one current tax year not exceeding $26 million.
- If businesses or real property trades elect out of the rule, they must use ADS to depreciate their applicable real property used in real estate trades or in business, rather than bonus depreciation.
- Floor planning financing for acquisition of farm machinery, boats or motor vehicles that are for lease or sale, which are secured by this type of inventory, can also receive an exception from the business interest deduction limitation.

Small businesses can expand by using cash methods rather than accrual methods of tax accounting. However, the definition of small business is defined by its qualifications, including average annual gross receipts not exceeding $26 million over three years. This also benefits this type of accounting as income can be shifted into the next year by deferring billings to the next year or by accelerating expense payments, such as paying bills early.

Other Aspects of Small Business Accounting to Consider for the Upcoming Tax Year

If your business qualifies as a small business, there are other benefits you may be able to enjoy. Here's a quick look at some benefits your company can realize by carefully approaching your company's accounting process.

- UNICAP – Small businesses don't have to capitalize additional costs for inventory.
- Inventory can be treated as non-incidental materials and supplies. You can also use other methods that represent this financial accounting treatment of your inventory.
- For long-term construction contracts, the percentage-of-completion method isn't required.

The liberalized business property expensing option is something you should consider spending towards. It allows you to make some additional expenditures that can boost your business while making it easier to regain those expenses in your taxes. Factors to consider in this situation include:

- For the 2021 tax year, the limit on expensing is $1,050,000, with phaseout beginning at $2,620,000. Essentially, beyond this phaseout, you'll see a dollar-for-dollar reduction in the expensing limit, disappearing entirely once your spending exceeds $3,670,000, though you can still claim bonus depreciation past this point.
- This type of expensing is generally used for most property that can be depreciated (with the exception of real estate), off-the-shelf computer software and vehicles for business use, though you may have some restrictions.
- This expensing type can also be used for what is referred to as a qualified improvement property, which generally covers improvements to a building's interior, but not the structure's enlargement, escalators or elevators or changes that are made to the structural framework of the interior.
- In these situations, improvements in HVAC, roofing, alarms, security systems and fire protection are also covered.
- The deduction for expensing isn't prorated over the course of the year, so property that is purchased and placed into service by December 31, 2021, can receive a full expensing deduction just as much as property purchased on January 1, 2021.

There are some other options you could consider for your tax planning purposes, though you'll want to act quickly to benefit from them. They include:

- 100% First-Year Depreciation: Companies can deduct 100% of the expense of purchasing new or, with a few exceptions, used equipment or machinery that's placed into service by December 31, 2021, with no proration of time used during the year. This means that equipment used for a few hours on the last day of the year can still be completely written off.
- De Minimis Safe Harbor Election: Otherwise known as the book-tax conformity election, this option provides a convenient way for businesses to deduct small-dollar expenditures, usually up to either $2,500 or $5,000 on each invoice, for acquiring or producing property that otherwise would need to be capitalized. However, it doesn't apply to money paid for land or inventory.
- Cost Segregation Benefits: Cost segregation allocates building costs into tangible personal property to speed up depreciation deduction schedules. Buildings are generally depreciated over 39 years for commercial property or 27.5 years for residential property, but segregating the costs between building and tangible personal property, such as equipment, fixtures and furniture, allows a faster write-off than the costs allocated to the building itself.

There are also some impacts to business income to be considered. These include:

- Income acceleration may happen when a corporation anticipates small net operating losses for 2021 and substantial net income for 2022. In this case, the company accelerates enough of its 2022 income, or defers 2021 deductions, to provide small amounts of net income in 2021. This allows the company to base 2022 estimated income tax installment payments on the small income shown in 2021 instead of much larger 2022 taxable income.
- Need to reduce your 2021 taxable income and faced with a debt-cancellation event? Wait until 2022 to complete the event to reduce your net taxable income. Another option

to consider is disposing of passive activity in 2021 so that you can deduct the suspended passive activity losses to show lower levels of income.

- What's happening with the Employee Retention Tax Credit? Companies that had a 20% or larger reduction in their gross receipts in any of the three initial calendar quarters in 2021 as compared to the same quarter in 2019, or who have been impacted by government orders due to COVID-19, may be able to claim credits of up to $7,000 per employee per quarter during the first three fiscal quarters of 2021.
- What about Employee Retention Credits (ERC) for startup businesses? If your business started on or after February 15, 2020, they may receive ERC of up to $50,000 for quarters 3 and 4 in 2021, with a maximum 2021 credit of $100,000. Because of their new status, they do not need to show reductions in gross receipts or that they were subjected to government orders to qualify for the credit.

Obviously, all of these changes and factors will need to be considered for the benefit of your business, but at the same time, you'll want to act quickly to take advantage of these benefits.

If you're wondering what your company's best options are in today's uncertain regulatory environment, the experienced professionals at Frankel Zacharia, LLC. at 402.496.9100, we are happy to help.