

Tax Law Updates, Tips, and Tools

Timber Tax Presentation 2023

Trent Cook, CPA & Matthew P. Broyles, CPA

Tax Law Updates

During last year's session....

- ▶ Big tax law change ambitions, little hope for success going into 2022
- ▶ Build Back Better died early 2022
- ▶ Covid business and individual provisions coming to a close

So, what happened in 2022?

- ▶ Very little, mostly insignificant to most taxpayers
 - ▶ Inflation Reduction Act of 2022 (Passed 8/16/22)
 - ▶ Corporate Alternative Minimum tax for earners of greater than \$1 Billion
 - ▶ Increased funding to IRS
 - ▶ Renewed Energy Credits
 - ▶ Healthcare provisions not related to tax
 - ▶ Secure Act 2.0 (Passed 12/29/22)
 - ▶ Numerous changes to retirement plan for individuals and businesses
 - ▶ Stricter rules on Conversation Easements
 - ▶ Possible limitation on amount of deduction
- ▶ Maybe we are getting back to normal

Tax Law Changes for 2022 & Forward

- ▶ Child Tax Credit is lower for 2022 than in 2021.
 - ▶ ARPA increased this to \$3,600 (age 0 -5) and \$3,000 (age 6-17) for 2021
 - ▶ For 2022 this amount is \$2,000 (age 16 or younger)
- ▶ IRA contributions remained the same at \$6,000 per individual
- ▶ 401(k) contributions increased to \$20,500
- ▶ Tax brackets, standard deduction and others items either had an incremental shift or no change at all
- ▶ Effective January 1, 2023 age to Required Minimum Distribution (RMD) is increased to 73. Must take by April 1 of the year after turning 73.

2022 & Forward - Continued

- ▶ Net Operating Loss Carryback
 - ▶ Farms only - 2 years back
 - ▶ All others must carry forward
- ▶ Meals deduction is back to 50% (100% in 2021/2022)
- ▶ No more charitable deduction in addition to standard deduction
 - ▶ Previously \$300 (\$600 MFJ) - 2021

Form K-2 and K-3

- ▶ New reporting requirement for Partnerships & S-Corporations
- ▶ Introduced for 2021 filings but had broader exceptions
- ▶ If entity has any foreign partners or foreign assets, have to file this
- ▶ If individual files Form 1116 with personal return, Partnership or S-Corporation has to file this
- ▶ Combined, these two forms are an additional 39 pages per partner or shareholder

Tax Cuts & Jobs Act - 2017

- ▶ Several provisions in this were only temporary and are set to expire after 2025
 - ▶ Section 199A (QBI) deduction
 - ▶ Bonus Depreciation - 100% for 2018 - 2022, 80% - 2023, 60% - 2024, 40% - 2025
 - ▶ Increased lifetime estate and gift tax exemption from \$5.6 to \$11.18 million per individual, indexed for inflation. For 2023, the exemption is 12.92 million per person.
 - ▶ If allowed to sunset after 2025, it will revert to around \$7 million per person

Future Tax Law Changes?

- ▶ With split Congress, high probability of little change
- ▶ Election 2024
- ▶ Taxes will be effectively “raised” by letting Tax Cuts & Jobs Act expire after 2025

Proposed Tax Plans

- ▶ All of the following are proposals from campaigns of people who are now in office or chairing a committee in Congress. Not all of these will pass but are potentially on the table:
 - ▶ Income Tax Rates
 - ▶ Increase rates on individuals with the top bracket going from 37% to 39.6%
 - ▶ Capital Gains
 - ▶ Taxing long term capital gains at ordinary rates instead of 0%, 15% or 20%
 - ▶ Step-Up Basis
 - ▶ Eliminates step-up in basis for capital gains taxation
 - ▶ Payroll Taxes
 - ▶ Impose a 12.4% Social Security payroll tax on earners over \$400,000

Proposed Tax Plans

- ▶ Corporate Income Tax Rate
 - ▶ Increase the corporate rate from 21% to 28% (some are proposing an increase to 35%)
- ▶ Corporate Minimum Tax Plan
 - ▶ A flat 15% tax on “book income” for corporations with large book to tax adjustments
- ▶ Double the tax rate on GILTI
 - ▶ This is the tax when you bring overseas profits back into the US
- ▶ Cap the overall benefit of itemized deductions to 28%
 - ▶ This will effect individuals with high charitable donations

Proposed Tax Plans

- ▶ Repeal Tax Cuts & Jobs Act
 - ▶ Phase out the Qualified Business Deduction
- ▶ Increase the generosity of the Child Tax Credit and Dependent Credit
- ▶ Expand the Earned Income Tax Credit
- ▶ Expand and restore renewable-energy-related tax credits and residential energy efficiency credits
- ▶ Re-establish the First-Time Homebuyers' Tax Credit
- ▶ Reduce estate and gift tax thresholds to 2009 levels
 - ▶ \$3.5 mil and 45% (currently at \$11.7 mil and 40%)

Proposed Tax Plans

- ▶ Implement a 4% “income-based premium” on households making over \$100,000 (This is part of the Medicare for All plan)
- ▶ Imposing a Financial Transaction tax on stock trades, bond trades and derivative transactions (0.1% - 0.2% per trade)
- ▶ Increased Social Security earnings limits - some pushing for a jump to \$250k of wages

Timber Taxation - Strategizing

Employed vs. Self-employed

- ▶ Employees
 - ▶ Not much room to wiggle unless another business venture is present
 - ▶ No deduction of employee business expenses
- ▶ Self-Employed
 - ▶ Deduction of business related expenses
 - ▶ Trump tax laws currently still in place - quickly fading
 - ▶ Aggressive capital asset depreciation
 - ▶ Qualified Business Income deduction (20% haircut)

Investment vs. Business

- ▶ Passive investments, hobbies, and non-active participation
 - ▶ Produces little to no current tax benefit on dollars spent
 - ▶ Most dollars spent are either lost or held until the major capital assets are sold
- ▶ Active trade or business
 - ▶ Opens the door to numerous tax advantages
 - ▶ Typically considered a “Self-employed” activity
 - ▶ Cash inflows/outflows more closely line up with taxable income

Business like

- ▶ Paint the right picture
 - ▶ Make sure expenses such as interest expense, property taxes, utilities, etc. are being used appropriately and effectively where blurred lines exist
 - ▶ These types of expenses not used in conjunction with a business are just lost
 - ▶ Keep distance between recreation and operations
 - ▶ Does it look, smell and taste like a business?
 - ▶ Material participation - keep a log of time, work, and travel
 - ▶ Profit making intentions - stay active with foresters, organizations, and training/knowledge
 - ▶ Adequate record keeping - management plans, receipt records, etc.

Common tax deductible expenditures (including depreciable purchases)

- ▶ Property Taxes
- ▶ Insurance
- ▶ Legal & Professional
- ▶ Repairs & Maintenance
- ▶ Supplies
- ▶ Auto
- ▶ Equipment purchases
- ▶ Custom Hire
- ▶ Reforestation
- ▶ Dues & Subscriptions
- ▶ Continuing Education
- ▶ Chemicals
- ▶ Certain Property improvements
- ▶ Fuel & Oil
- ▶ Interest
- ▶ Contract Labor
- ▶ Equipment Rental
- ▶ Utilities

Business entities - why and which one?

- ▶ Key factors in determining what entity structure to use:
 - ▶ Legal liability
 - ▶ Ownership
 - ▶ Succession
 - ▶ Federal and state taxes
 - ▶ Complexity and cost benefit
 - ▶ Payroll and benefits
 - ▶ Growth and buying power

Business entities

- ▶ Often asked - how should I structure my business?
 - ▶ Options
 - ▶ Sole-proprietor business or farm (1040 Schedule C or F)
 - ▶ Partnership (1065)
 - ▶ S-Corporation (1120S)
 - ▶ C-Corporation (1120)
 - ▶ Trust (1041) *typically used for estate & succession planning first & foremost
 - ▶ What about an LLC?
 - ▶ Most commonly used entity structure - came into existence after federal tax law structure
 - ▶ An LLC can fall under any federal taxing structure given the right circumstances

Adequate Record Keeping - Income taxes

- ▶ How long?
 - ▶ IRS statute of limitations = 3 years
 - ▶ We recommend keeping records 4-5 years with overlap of filing periods
 - ▶ Might retain longer for special purposes - Capital Gains(Losses) & basis
- ▶ What records?
 - ▶ Bank statements, Credit Card statements, receipts, invoices, mileage logs
 - ▶ Images - recently aided in one of our timber farm audits
- ▶ Clear Separation
 - ▶ Not a bad idea to have separate bank accounts/credit cards for each business activity
- ▶ Not the same for other taxes, such as estate or sales.

Adequate Record Keeping - Cost Basis

- ▶ Cannot express the importance
 - ▶ Permanently store original cost records
 - ▶ Purchase settlement statements
 - ▶ Purchased or gifted
 - ▶ Estate tax returns/records for inherited properties
 - ▶ Distributions from other entities (k-1 statements / 1099-div liquidating)
- ▶ Inherited property
 - ▶ Property appraisals for highest values
 - ▶ Land & Timber

Timing is everything

- ▶ Avoid roller coaster tax rides
 - ▶ Averaging out income over time results in lower tax paid over time
 - ▶ Higher Income results in loss of certain deductions and credits (phase-outs)
 - ▶ Higher Income results in additional types of taxes
 - ▶ Additional investment & Medicare taxes
 - ▶ Alternative Minimum Taxes (AMT)
 - ▶ Utilize additional expenses/losses in years of additional income
 - ▶ Example - purchase of equipment in a year of a major cut/sale
- ▶ Plan, Plan, Plan
 - ▶ October - December
- ▶ IRS works off cash basis by default

Tips for smooth tax filings

- ▶ Submit all filings and payments electronically if possible
 - ▶ Not perfect, but seeing more errors and delays with regards to general postage
- ▶ Be sure to provide ALL important tax documents received
 - ▶ With more 1099's being issued, taxpayers need to be sure that what the IRS has matches what is being reported
- ▶ File an extension just in case if you are filing and paying near the deadline
- ▶ Be patient

Handy Tools

▶ Mile IQ

- ▶ <https://www.mileiq.com/>
- ▶ A pencil free business mileage log
- ▶ Automatic tracking
- ▶ Year end reports
- ▶ Multiple classifications
- ▶ Can be used from your smartphone or computer

▶ QuickBooks Online

- ▶ <https://quickbooks.intuit.com/online/>
- ▶ Real time, cloud based accounting
- ▶ Anytime Accountant assistance
- ▶ Automatic bank feeds and transaction memorization
- ▶ App integration
- ▶ Test Drive the system - <https://qbo.intuit.com/redirect/testdrive>

Handy Tools

- ▶ Local Appraisal District / Tax Assessor

- ▶ Depending on service provider, they may provide the following information:

- ▶ Owner Info
 - ▶ Deed transfer Dates
 - ▶ Appraised values breakdown
 - ▶ Map Tools and property lines
 - ▶ Appraisal Example - <https://polkcad.org/home>
 - ▶ Assessor Example - <http://polk-tax.com/>

- ▶ National Timber Tax

- ▶ <https://www.timbertax.org>
 - ▶ A wealth of information regarding timber tax for all levels of participants

Handy Tools

▶ Gusto Payroll

- ▶ <https://gusto.com/>
- ▶ Simplified payroll for small employers (I recommend 1-5 employees)
- ▶ Can be as easy as hands free
- ▶ Paperless system

▶ Texas Comptroller

- ▶ <https://comptroller.texas.gov/>
- ▶ Research and instructions for basically all Texas taxes
- ▶ Entity lookup - <https://comptroller.texas.gov/>
- ▶ Online filing - <https://mycpa.cpa.state.tx.us/securitymp1portal/displayLoginUser.do>

Handy Tools

▶ Office Lens mobile app

- ▶ Enhances, trims and straightens document images taken by phone
- ▶ Stores them and enables them to be transferred to other devices in readable workable formats
- ▶ Works with most documents, including business cards

▶ Rocket Book

- ▶ <https://getrocketbook.com/>
- ▶ Notebook style devices that convert written text into electronic readable and transferrable data

Handy Tools

▶ ShareFile

- ▶ <https://www.sharefile.com/>
- ▶ Secure document exchange
- ▶ Temporary data cloud based storage
- ▶ Able to send multiple and large files
- ▶ Can be paired with e-mail

▶ Local CPA's website

- ▶ May provide an available portal for secure document exchange and retention
- ▶ News on tax laws and changes that affect the local area (example - Covid pandemic tax laws)
- ▶ Links and resources

Contact Info

- ▶ Matt Broyles, CPA
- ▶ Livingston, TX
- ▶ mbroyles@axleyrode.cpa
- ▶ (936) 327-3166
- ▶ Trent Cook, CPA
- ▶ Lufkin, TX
- ▶ tcook@axleyrode.cpa
- ▶ (936) 634-6621

Questions?