



THE LARGO GROUP

# Breaking Down our Tax Liability in 2021

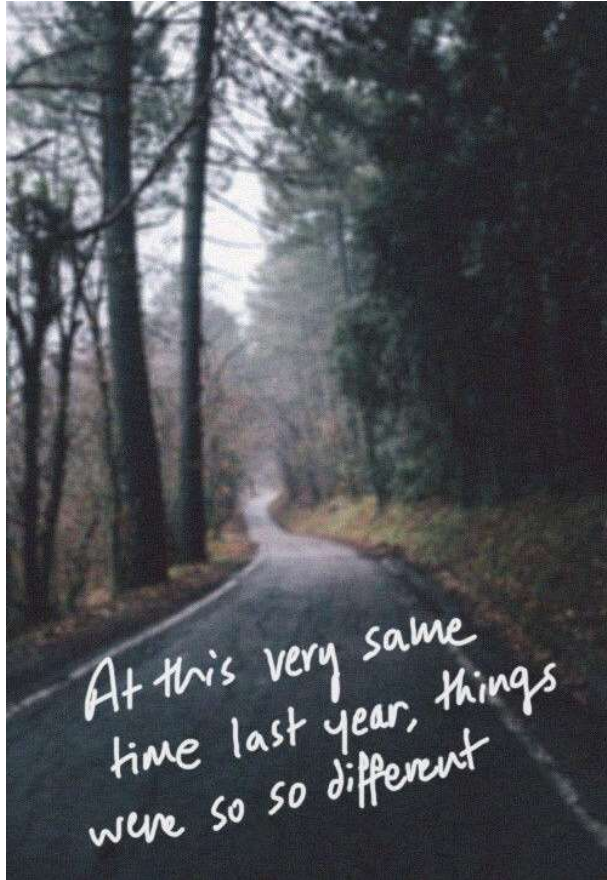
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Principal

## Why is it important to plan for taxes this year?

MANY moving parts in 2021

- PPP
- ERTC
- RRF
- State/Local Grants
- Rising Prices
- Rising COSTS





## This year *MAY NOT* look like prior years!

### December 2020:

- Businesses were dealing with COVID resurgence
- Holiday parties were cancelled
- Indoor Dining Restrictions were back in place

### December 2021:

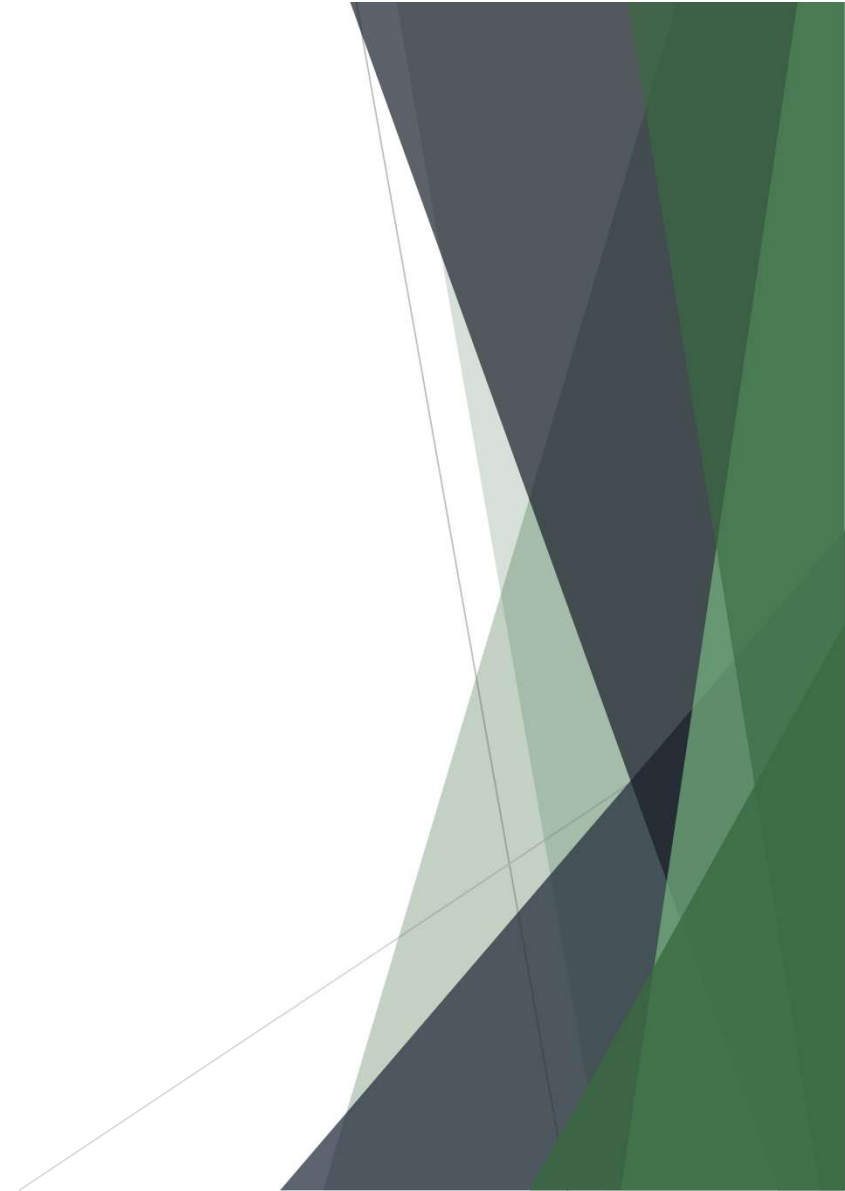
- Holiday parties may be happening again?
- Prices have increased
- Cost of product has increased
- Received relief money
- Labor has been LOW

Where do I  
begin?



## 4 Questions to start building a tax plan...

1. Total taxable BUSINESS income for the year
2. Income from various sources:
  - Business Income
  - W-2 Income
  - Investment Income
  - Government assistance (taxable and non-taxable)
3. Deductions
4. Tax Status (Married/Single/Head of Household)



# 1. Total BUSINESS Income for the year

- For tax planning - we will want to breakdown any OTHER INCOME received to determine its impact on tax liability.
- Net income may be significantly higher than prior years!

	2021	2020
Sales	\$950,000.00	\$875,000.00
COGS	\$285,000.00	\$236,250.00
Labor	\$266,000.00	\$280,000.00
Operating Expenses	\$266,000.00	\$250,000.00
Operating Income	\$133,000.00	\$108,750.00
Other Income:		
PPP	\$58,400.00	\$0.00
ERTC	\$102,000.00	
Local Grant	\$25,000.00	\$0.00
Other Expenses:		
Owner Compensation	-\$85,000.00	\$0.00
Net Income	\$233,400.00	\$108,750.00

## What about ERTC (ERC)?

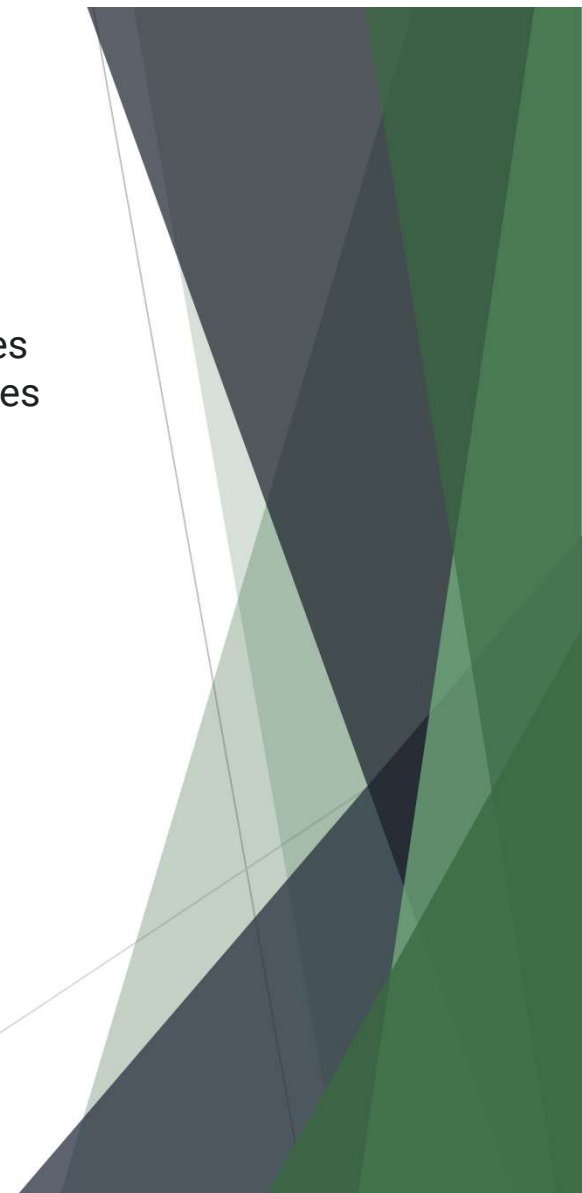
- Tax Returns. The tax code has always been such that if you claim the ERC for tax year 2020, you were supposed to file an amended 2020 income tax return to report the income in that year (which also may require you to file amended personal returns as well). While it was hoped that the IRS would fix this so that you didn't have to report the credit as income until the year it was received, this latest guidance they *confirmed* that you do indeed need to do this. While it's important to be aware of the requirement, **it is recommended that you hold off on any action for a little while to see if Congress intervenes**. Many have not even received credits that were applied for months ago. In the meantime, just be aware that this may be coming.
- Also, an important reminder: Regardless of timing, **ERC is still taxable income (unlike PPP which ended up being tax free)**. It may be advantageous to update your tax plan or projection, especially if you carried the credit forward as opposed to requesting a check.
- **No response and/or confirmation from CONGRESS as of 11/30/2021.**

## What about RRF?

- **Funds received from the RRF are not treated as taxable income**, and expenditures paid with these funds are tax deductible. In the NIPAs, RRF payments to businesses for eligible expenses are classified as subsidies and are recorded on an accrual basis based on when the funds are used by the business for expenses.
- Will want to allocate funds to months used for allowable business expenses.
- \$1,000,000 Received in RRF – **have until MARCH 11, 2023 to use funds**


## What about PPP?

- On January 6, 2021, the IRS officially reversed its position on deductions to conform with this change in law via Rev. Rul. 2021-2. Section 276 also provides that forgiven PPP loan **amounts are treated as tax exempt income** for purposes of Sections 705 and 1366 of the Internal Revenue Code (the Code)



## What this means for my business income:

2021	
Sales	\$950,000.00
COGS	\$285,000.00
Labor	\$266,000.00
Operating Expenses	\$266,000.00
Operating Income	\$133,000.00
Other Income:	
<i>PPP</i>	\$58,400.00
ERTC	\$102,000.00
<i>Local Grant</i>	\$25,000.00
Other Expenses:	
Owner Compensation	-\$85,000.00
Taxable Income	\$150,000.00
Net Income	\$233,400.00



May be the case that net income and cash balance are significantly HIGHER than taxable income in 2021.

## 2. Personal Income from other sources

Tax planning focuses on the individual returns for the business owner, as each owner will have their own unique tax situation. For a meaningful tax projection, need to be aware of **individual owner's effective tax rates.**

Income from ALL sources received in 2021:

- Wages from business: \$42,500 - will want to also note WITHHOLDINGS
- Business Income: \$75,000 - 50% of total business income
- Interest Income: \$1,500
- Dividend Income: \$500
- **Total INCOME: \$119,500**

## Deductions & Tax Status

**Qualified Business Income Deduction** - tax deduction that allows for self employed and small business owners to deduct up to 20% of their qualified business income.

BUSINESS INCOME MUST BE UNDER \$164,900 for single filers and \$329,800 for joint filers to qualify!

Itemized v. Standard Deduction - vast majority of taxpayers utilize the standard deductions. Increased in 2021 to the following:

- Single Filers: \$12,950
- Married Filing Jointly: \$25,100

## How does this all work?

- 2021 Tax Projection:
- Business income higher = higher overall tax bracket than prior years.
- **What can I do to lower tax liability before year-end?**

	2021
Wages	\$42,500.00
Business Income	\$119,500.00
Investment Income (assume same tax rate)	\$2,000.00
<b>Adjusted Gross Income</b>	<b>\$164,000.00</b>
QBI Deduction (20% Business Income)	\$23,900.00
Standard Deduction	\$12,550.00
Total Taxable Income	\$127,550.00
Total Tax Liability (assume 25% tax rate)	\$31,887.50
Withholdings from W-2	\$4,000.00
<b>Tax Due</b>	<b>\$27,887.50</b>

## Capital Improvements

**Capital Improvements:** Section 179 expense allows you to decrease taxable income by writing off the FULL value of business assets all at once.

- \$40,000 in capital improvements would save **\$10,000 in taxes**





## Expense Acceleration

**Expense Acceleration:** Purchase of small items can add up to tax savings if purchased before 12/31/2021. Examples include office supplies, paper products, software renewals, or employee bonuses.

- Increase expenses by \$10,000 would save **\$2,500 in taxes**

# Missing Deductions



- **Missing Deductions:** creating accountable plan for company could increase expenses and incentivize employees for business expenses incurred but not reimbursed throughout the year.
- Example: Manager uses cell phone for work throughout the year. Could reimburse manager \$1,000 before 12/31 for use of phone and save **\$300 in taxes**.
- Plan should be well documented and applied to employees and owners in an equitable way.
- Other reimbursements include:
  - Travel (mileage to catering events, etc.)
  - Home office
  - Continuing education
  - Supplies
  - Uniforms



## Employing Children in family business

**Employing your children:** If you have children between the ages of 7-22, you can use this strategy to save money.

- Each child can be employed by business and paid up to \$12,550 TAX FEE.
- Business receives deduction for the payment - reducing tax liability by \$3,137 per child.
- Child files return, but they pay no federal income tax because they are below the standard deduction.

## Retirement Planning

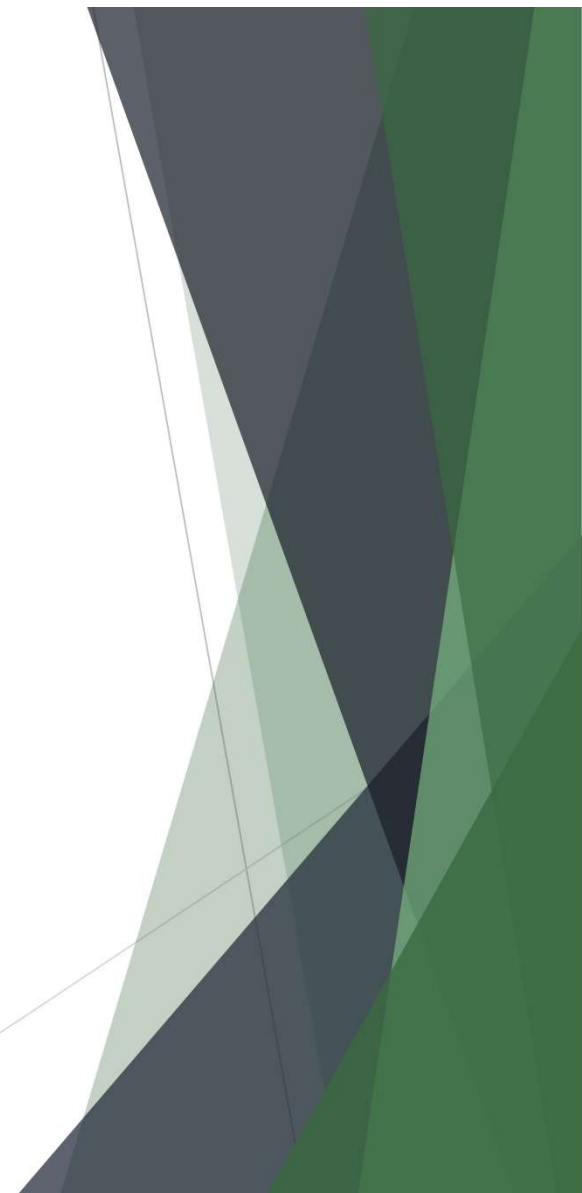
**Retirement planning:** If you find yourself with extra cash, it may be a year to think about your retirement strategy.

- Increase wages to \$142,800 - MAX social security cap. If within 5 years of retirement, this may increase benefit received when retired? *Would increase tax liability but may be worth it if concerned about social security contributions in prior years.*
- Make pre-tax retirement contribution through SEP IRA. Can contribute up to \$58,000 to SEP IRA which would generate a savings of \$14,500 in taxes.



## All comes back to CASH FLOW

- Business Cash as of 11/30/2021: \$215,000
- Taxable Business Income: \$119,500
- Projected Tax Liability: \$26,612
- Free Cash: \$188,388
  
- Biggest Lesson of COVID for business owners: IRS ASSUMES ALL business income is YOUR income.
- Would it make sense to take a distribution equal to the amount of the TAXABLE business income?
- If S Corp or Partnership - DISTRIBUTION is NOT taxable!



## Owner Cash flow:

2021	
Owner Wages	\$42,500.00
Distribution	\$110,000.00
Less Tax Liability	-\$26,612
Owner free cash from business	\$179,112.00
Business Cash Flow	
Projected 12/31 Balance	\$215,000.00
12/31 Owner Distribution	\$110,000.00
Adjusted Business Cash Flow	\$105,000.00
Tax Liability on Distribution	\$0.00

Already included in tax calculation

## FREE Tax Seminar in December

Please visit

[www.thelargogroup.com/academy](http://www.thelargogroup.com/academy) to register for our TAX PLANNING 101 course focused on helping you build your tax plan for 2021 and beyond!

Feeling lost: please visit

[www.thelargogroup.com](http://www.thelargogroup.com) today for a free one-on-one 30 minute session to walk through your tax picture in 2021.



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Thank You

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