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Dear Client,

We hope you and your family have been safe and healthy during these difficult times. While April 15th may seem like a long way off, we wanted to take the opportunity to highlight some changes to the federal tax laws for 2020. We are also continuing our refer a friend incentive of a $25 credit towards your 2020 tax return for each new referred tax client tax return we prepare.

To ensure the health and safety of our clients and staff we will not be conducting in person appointments for the 2020 tax season. All tax information, including your tax organizer, signed engagement letter and supporting tax documents can be dropped off at a designated area in our office building between 9am and 4pm Monday through Friday, mailed in or sent via e-mail through our secure client portal. We will be contacting you with any follow up questions to complete the tax return via email or phone call.

TAX UPDATES FOR 2020

Individual Taxes:

Tax Rate Brackets

In 2020 the 37% tax bracket applies to taxable income that exceeds $518,400 for single and head of household ("HOH") taxpayers, $622,050 for married individuals filing jointly ("MFJ") and surviving spouse, and $311,025 for married individuals filing separate ("MFS"). All of the other tax brackets have been adjusted for inflation.

Individuals with wages and other compensation in excess of $250,000 for MFJ, $125,000 for MFS, and $200,000 for all others are subject to the additional Medicare tax of .9%. Employers are obligated to withhold the additional tax beginning in the pay period when wages exceed $200,000 for the calendar year. The employer is obligated regardless of the filing status or income from other sources. If the taxpayer does not owe the additional withholding for Medicare, they can claim a credit on their 2020 income tax return.

Preferential Rates for Capital Gains and Qualified Dividends

Unchanged for 2020, qualified dividends and long-term capital gains can avoid tax totally under the 0% capital gains rate, or be subject to capital gains rates of 15% or 20%. The capital gains rate depends on taxable income, how much of the taxable income consists of qualified dividends and eligible long-term gains, and filing status. The 20% capital gain rate applies to single taxpayers with taxable income over $441,450, MFJ taxpayers with taxable income over $496,600, and for head of household taxpayers with income over $469,050.

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Net Investment Income Tax

The net investment income tax ("NIIT") is still applicable for 2020. This affects income tax returns of taxpayers who have net investment income and have modified adjusted gross income ("MAGI") over the following thresholds: $250,000 for MFJ or surviving spouse, $125,000 for MFS, $200,000 for single, and $200,000 for head of household.

If modified adjusted gross income ("MAGI") exceeds the threshold, a 3.8% tax applies to the lesser of the net investment income or the excess of MAGI over the threshold.

Required Minimum Distributions

Under the CARES Act, the required minimum distribution for 2020 has been suspended.

Retirement Plan Distributions and Loans

If the taxpayer is impacted by COVID-19, they may take a distribution of up to $100,000 and not be subject to the 10% early withdrawal penalty. The taxpayer can elect to include the distribution in income over a 3-year period. The taxpayer can also contribute the money back to a retirement plan within three years of the withdrawal and treat it as a rollover with no tax consequence once paid back.

Under the CARES Act, taxpayers impacted by COVID-19, may have taken a loan of up to the lesser of $100,000 less any outstanding loans, or 100% of their non-forfeited account balance from a qualified plan between March 27, 2020 and September 23, 2020.

Charitable Contributions

The CARES Act in 2020 allows taxpayers who do not itemize deductions to take a charitable deduction of up to $300 for cash contributions made to qualifying organizations.

Personal Exemptions and Itemized Deductions

The personal exemption continues to be eliminated for 2020. This elimination modifies the level of income which a taxpayer must file a return. Also continuing for 2020 for most taxpayers, the filing requirement will be based solely upon the standard deduction available to them.

We have outlined the itemized deductions continuing to be available for 2020 as follows:

- Deduction for state and local income taxes, personal property taxes and real estate taxes will be limited to $10,000 in total.
- Mortgage interest up to $750,000 is allowed on new mortgages entered into on or after December 15, 2017. Interest on the portion of the mortgage not used to buy, build or remodel your personal residence is not allowed.
- Mortgage insurance premiums paid or accrued in connection with debt that qualifies as acquisition indebtedness is deductible for 2020 as qualified residence interest.

- Charitable donations of cash that are limited to 60% of AGI will have no limitations in 2020 due to the CARES Act.
- All miscellaneous deductions formerly subject to the 2% threshold are still no longer available on your federal tax return. Some examples of these expenses are employee business expenses, tax preparation fees, investment expenses. However, these expenses may be available on your state tax return.
- Casualty losses will now only be allowed for presidentially declared disaster areas.
- Gambling losses remain deductible as a miscellaneous itemized deduction not subject to the 2% limitation. The IRS has determined that an entry fee paid by individuals to participate in a fantasy sports contest is a wagering transaction and therefore subject to the gambling loss limitation.
- The overall itemized deduction limitation of 3% of the excess of adjusted gross income over the threshold amount is still suspended.

Patient Protection and Affordable Care Act

Still in effect for 2020, the Tax Cuts & Jobs Act repealed the tax on individuals that fail to carry minimum health coverage for themselves and their dependents, although there are still some states (such as MA, NJ and DC) that still have health insurance mandates and may apply penalties for not having coverage. Individuals and families are still able to acquire coverage through the Patient Protection and Affordable Care Act market place. Individuals with marketplace coverage may be entitled to the §36B premium assistance tax credit when filing their 2020 tax return. If a taxpayer received an advanced payment of the credit, they are required to file a 2020 Form 1040.

For 2020 the §36B premium assistance tax credit is available for taxpayers who meet certain household income criteria.

Taxpayers should receive one of the following forms which pertain to healthcare coverage and these forms should be utilized when filing your 2020 returns:

- Form 1095-A Health Insurance Marketplace Statement
- Form 1095-B Health Coverage (sent out on or before March 2, 2021)
- Form 1095-C Employer-Provided Health Insurance Offer and Coverage

Standard Deductions

The standard deduction for 2020 increases to $24,800 for MFJ and surviving spouse, $18,650 for head of household, or $12,400 for all other taxpayers. The additional standard deduction for being 65 or older or blind is $1,650 if single or head of household ($3,300 if 65 and blind). If MFJ, the additional standard deduction is $1,300 if one spouse is 65 or older or blind, $2,600 if both spouses are at least 65 (or one is 65 and blind).

Deduction Floor for Medical Expenses

Remaining for 2020, the floor for deducting medical expenses as an itemized deduction is 7.5% of AGI for all taxpayers.

Social Security Wage Base

For 2020, the tax rate on the employee portion of social security is 6.2% on wages up to $137,700; therefore, social security tax withholdings will not top $8,537. Medicare tax of 1.45% is withheld from all wages regardless of amount.

Self-employment taxes of 15.3% apply to earnings up to $137,700 after the earnings are decreased by 7.65%. The 15.3% rate equals 12.4% for social security plus 2.9% for Medicare. If net earnings are in excess of $137,700, the 2.9% Medicare rate applies to the total amount. One half of the self-employment tax may be taken as an above the line deduction. The maximum self-employment social security tax is reached at $17,075.

It should be noted, that if earnings exceed the applicable threshold, net self-employment earnings could be subject to the .9% additional Medicare Tax.

IRA and Roth IRA Contribution Phase-out

For 2020, the contribution limit for traditional IRAs and Roth IRAs is $6,000 or $7,000 for those age 50 or older. For 2021, the contribution limit will remain the same with an additional $1,000 if you are age 50 or older. The contribution deduction for traditional IRAs is phased-out for active plan participants with MAGI between $65,000 and $74,999 for a single person or head of household, or between $104,000 and $123,999 for MFJ. The phase-out range is $196,000-$205,999 for a spouse who is not an active plan participant and who files jointly with a spouse who is an active plan participant.

Under the SECURE Act for contributions made in 2020, taxpayers of any age including those over 70 ½ can contribute to a traditional IRA.

IRA Charitable Contribution

The IRA charitable contribution gives the taxpayer the ability to distribute to a charity directly from an IRA for an individual over the age of 70½ without including the distribution in income or deducting the amount as a charitable contribution. This distribution is taken into account when determining the taxpayers required minimum distribution and is a permanent rule by the IRS.

529 Plans

Continuing for 2020, all 529 plan savings may be used toward elementary or secondary public, private or religious school tuition. There is a $10,000 limitation for elementary, middle or high school expenses.

Depreciation

The maximum §179 deduction allowed is $1,040,000 for qualifying property placed in service in 2020, subject to a limitation based upon the qualified assets placed into service. For 2020, this threshold amount is $2,590,000. The §179 deduction also imposes an income limitation upon the deduction.

Bonus depreciation remains at 100% for 2020 through 2022. Bonus depreciation allows a taxpayer to take a deduction in the year that the acquired asset is placed in service. Continuing for 2020, property eligible for bonus depreciation was expanded to include used property. Bonus depreciation is mandatory unless you elect out of it.

Alternative Minimum Tax

The 2020 alternative minimum tax ("AMT") exemptions are increased to $113,400 for MFJ and surviving spouse, $72,900 for single and head of household, $25,400 for estates and trusts, and $56,700 for MFS. The 2020 AMT exemptions phase-out begins at $1,036,800 for MFJ and surviving spouse, $518,400 for all others. The AMT exemption amount is reduce one dollar for every four dollars of AMT income above the threshold amount for the taxpayer's filing status.

Eligibility for Saver's Credit

The saver's credit is 50%, 20% or 10% of your retirement plan or IRA or ABLE account contributions depending on your adjusted gross income. The maximum amount of the credit is $1,000 for single taxpayers and $2,000 for married filing joint taxpayers. Credits are not allowed when AGI reaches $32,500 for single taxpayers, $48,750 for head of household and $65,000 for MFJ and surviving spouse.

Adoption Credit

For adoptions finalized in 2020, taxpayers will see an increase in the credit and exclusion amounts for the adoption credit. The amount in 2020 is $14,300.

Deduction Limits for Long-Term Care Premiums

The maximum amount of age-based long-term care premiums that can be included as deductible medical expenses for 2020 (subject to the 7.5% of AGI floor) is $430 if you are age 40 or younger at the end of 2020; $810 for those age 41 through 50; $1,630 for those age 51 through 60; $4,350 for those age 61 through 70; and $5,430 for those over age 70.

Foreign Earned Income and Housing Exclusions

The foreign earned income exclusion for 2020 is $107,600. In addition, the housing expense limitation to use in calculating your maximum housing exclusion is generally $32,280. However, the housing expense exclusion is based on locality, so in some cases there will be adjustments to the $32,280 used to calculate the final housing exclusion. Due to the COVID-19 pandemic, the IRS is providing a waiver for 2020 of the time requirements that allow a qualified individual to exclude foreign earned income and the housing cost amounts from income. If the taxpayer reasonably expected and can establish that they would meet either the bona fide residence test or physical presence test if it had not been for the pandemic they may be entitled to this waiver.

Report of Foreign Bank and Financial Accounts ("FBAR")

The Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 provides, for tax years beginning after December 31, 2015, the TD-F-90-22.1 (Fin Cen Report 114) "Report of Foreign Bank and Financial Accounts (FBAR)" is usually electronically filed to the Treasury Department on or before April 15th with an automatic extension of six months. All US persons who have a financial interest in or signature authority over at least one foreign account and the aggregate value of all accounts exceeds $10,000 at any time during the year must file a FBAR. They are filed separate from your income tax return. The willful failure to file a FBAR can carry a penalty equal to the greater of $100,000 or 50% of the highest balance in the account, for each violation.

Annual Exclusion for Gifts

With regards to gift taxes, the per-donee exclusion for gifts of present interest is $15,000, for 2020 and 2021.

Child Tax Credit

The child tax credit remains the same for 2020 at $2,000 per child and the level the credit begins to phase-out for MFJ is $400,000 and $200,000 for all others. Of this amount up to $1,400 is refundable.

Dependent Credit

Continuing for 2020, taxpayers are eligible for a non-refundable $500 credit for each dependent who is not a qualifying child under age 17. The credit begins to phase out when your income is more than $200,000 for a single taxpayer and $400,000 for a married taxpayer.

Gift Tax and Estate Tax Exemption

For 2020 gift tax and estate tax purposes, the basic exemption amount is $11,580,000 for federal taxes which will increase to $11,700,000 for 2021. The top rate remains at 40% for 2020.

Education Credits

The maximum credit allowed under the American Opportunity Credit is $2,500 per student for all taxpayers except MFS, who do not qualify for the credit. For 2020, the credit starts to phase out at $160,000 for MFJ filers and $80,000 for all other qualifying taxpayers.

The maximum credit allowed under the Lifetime Learning Credit is $2,000 per tax return for all taxpayers except MFS, who do not qualify for the credit. For 2020, the credit starts to phase out at $118,000 for MFJ filers and $59,000 for all other qualifying taxpayers.

For 2020, the above-the-line $4,000 maximum deduction for qualified tuition and related expenses for higher education continues and goes through January 1, 2021.

Solar Credits

For 2020, the federal tax credit for solar installations prior to December 31, 2020 decreases to 26%. For 2021, the federal tax credit decreases again to 22%. If you purchase or lease solar energy system equipment you are also eligible for a New York State credit equal to 25% of your qualified solar energy system equipment expenditures with a maximum amount of $5,000.

THE SETTING EVERY COMMUNITY UP FOR RETIREMENT ENHANCEMENT ("SECURE") ACT AND ITS IMPACT ON RETIREMENT PLAN PROVISIONS

The SECURE Act passed in December 2019 and includes many reforms that are designed to increase access to workplace retirement plans and expand retirement savings. The legislation includes policy changes that impact defined contribution plans, defined benefit plans, as well as individual retirement accounts and 529 plans, many of which took effect January 1, 2020. Below are some of the key changes incorporated in the SECURE Act and how they will affect both individuals, employers, and plan sponsors.

Individuals:

The age at which participants must begin taking required minimum distributions (RMDs) has been increased to 72 (previously was 70 ½). This applies to participants whom will attain age 72 after December 31, 2019.

Effective for taxable years beginning after December 31, 2019, individuals can now contribute to an IRA at any age. Previously, individuals were prohibited from contributing after age 70 1/2.

During a one-year period following the birth or adoption of a child, individuals may withdraw up to $5,000 from a retirement program, penalty free. This includes IRAs, 403(b) plans, 457 plans and 401(a) plans and is effective for plan years beginning after December 31, 2019.

Individuals who participate in 529 Plans may withdraw up to $10,000 annually, tax-free, for the repayment of student loans.

Employers and Plan Sponsors:

Small employers who start a tax-qualified retirement plan are eligible for a tax credit up to a maximum of $5,000 (previous maximum was $500) depending on the number of employees. This change is effective for employer taxable years beginning after December 31, 2019.

Small employers who create a 401(k) plan or SIMPLE IRA plan and utilize automatic participant enrollment will be eligible for an annual tax credit up to $500. This provision is effective for employer taxable years beginning after December 31, 2019.

It is important to note that employers may have to make amendments to their current plan documents to allow their plan participants to take advantage of these changes in 2020.

THE CORONAVIRUS AID, RELIEF AND ECONOMIC SECURITY (CARES) ACT

The CARES Act was passed in March 2020 and provides aid packages to families and businesses impacted by the COVID-19 pandemic. Below are some of the key changes incorporated in the CARES Act and how they will affect both individuals and employers.

Individuals:

Recovery Rebate Credit/Economic Impact Payment

The CARES Act provided an advance of the Recovery Rebate Credit in 2020 equal to $1,200 per eligible individual and $500 per eligible child subject to AGI limitations. Any amounts over the limitation were reduced by 5% of the excess.

Receipt of the advance was based on information filed with the taxpayer’s 2019 or 2018 income tax returns.

The advanced payment received by a taxpayer is not considered taxable income for 2020.

Taxpayers who received an advance payment but are not eligible for the credit based upon their 2020 income tax return, will not have to return the payment received. However, if the advanced payment received was lower than what the taxpayer was entitled to, based on their 2020 income tax filing the taxpayer will be allowed to claim the additional credit on their 2020 income tax return.

Taxpayers who received an advanced payment for a deceased individual will have to pay back that advanced payment.

Employers:

As part of the overall $5,250 cap for tax-free educational assistance programs for employees, an employer can make student loan payments on behalf of an employee in 2020.

Amounts received under the CARES Act Paycheck Protection Program (PPP) will be forgiven by the lender/SBA if expended as per provisions.

The CARES Act provides an exception and exempts from taxation any amount forgiven under the PPP loan. Accordingly, disallowed is any expense otherwise allowed to be deducted for the amount forgiven or expected to be forgiven under the PPP loan forgiveness program.

Corporations:

The CARES Act allows the carryback of losses for 5 previous years preceding the year of loss that arose in the years ending after December 31, 2017 and before January 1, 2021.

Any net operating loss created in 2018 through 2020 can be used to offset 100% if taxable income (previously 80% imposed by the Tax Cuts and Jobs Act (“TCJA”).

The TCJA provision limiting the current deduction of net business losses has been suspended for 2018 through 2020.

For 2019 and 2020, every business is subject to a limited deduction for interest expense equal to the sum of the taxpayer’s business interest income, 50% of the adjusted taxable income of the business, and the taxpayer’s floor plan financing interest (otherwise it is 30% enacted under the TCJA). As an added benefit, taxpayers may elect to use 2019 taxable income to calculate the deductible interest in 2020.

Corporate Taxes:

Corporate tax changes that took effect for years beginning on or after January 1, 2019, continue through December 31, 2020. The following is a summary of some of the key changes that will continue:

- C-Corporations will continue to have a flat tax rate of 21% on all taxable income.
- The use of business losses of noncorporate taxpayers is restricted to $259,000 for unmarried taxpayers and $518,000 for married taxpayers.
- The deduction for employer provided meals that were previously 100% deductible under the de minimis rules are now subject to the 50% limitation.
- For 2020 there is generally no deduction allowed for amounts paid for entertainment expenses. On September 30, 2020, the IRS issued final regulations on deducting certain meal and travel expenses. The regulations make it clear that a food or beverage deduction can be available for the cost of the food or beverage consumed by the taxpayer if it is separately stated from the cost of the entertainment.
- Eligible employers are entitled to a credit for paid family and medical leave ranging from 12.5% to 25% of wages paid to qualifying employees while on family or medical leave and are being paid at least 50% of their regular wage amount. The Department of Labor implemented health emergency leave under Title I of the Family and Medical Leave Act. Employers temporarily are required to provide up to 10 weeks of paid and 2 weeks unpaid emergency family and medical leave to eligible employees for reasons related to COVID-19. The leave provision is set to expire December 31, 2020 and is effective from April 2, 2020 and December 31, 2020.
- Small and midsize employers with fewer than 500 employees are eligible for refundable tax credits that are a dollar-for- dollar reimbursement, for the cost of providing paid sick and family leave wages to their employees for leave related to COVID-19 under the Families First Coronavirus Response Act.
- The Emergency Paid Sick Leave Act entitles workers up to 80 hours of paid sick time if they are unable to work due to COVID-19 related reason.
- The alternative minimum tax no longer applies to corporations.
- There is an executive order for the optional postponement of the certain employee's share of only the Social Security portion of FICA tax on wages and compensation paid from September 1, 2020 through December 31, 2020. These deferred taxes are to be withheld from the employees' wages and remitted ratably beginning January 1, 2021 through April 30, 2021. The employer is responsible for the deferred taxes liability.
- <u>Qualified Business Income Deduction (199A Deduction):</u>
    - A special 20% deduction will apply for certain business income reported on a person's individual return. This includes income from qualified businesses.
    - This deduction is available to sole proprietors (Schedule C), real estate rental income (Schedule E), Trust and Estates, Partnerships and S-Corporations.
    - The deduction is subject to some limitation rules and in general will not be allowed for most professions or consulting businesses, unless the taxpayer's total income is under $163,300 for single and $326,600 for MFJ taxpayers.

Tax Organizer

We have included the engagement letter and tax organizer to assist you in gathering information necessary for the preparation of your 2020 tax return. We recommend that you enter all pertinent 2020 information and include with your tax information. In the interest of time savings, or personal preference, you can also mail in your completed organizer or send it electronically through the firm's secure client portal with all supporting tax documentation. Be sure to complete the section pertaining to your contact information including your email address and current phone number. For the safety and security of our client's personal information, we will be once again utilizing a client tax portal to send and receive tax information for the upcoming tax season. For those clients who do not have access to a computer, we will still accept hard copies of tax documents and provide a hard copy of your tax return.

The enclosed engagement letter should be signed by both taxpayer and spouse if filing a joint return and included with your tax information.

When you send in your tax documents, verify beforehand that you have all your IRS forms, including W-2 forms, 1099 forms and K-1 forms and any other information that has been sent to the IRS. This will eliminate assessments by the IRS after the tax returns have been filed.

We have provided a complete tax service to our clients for over eighty years. We also provide you with highly professional services at a fair and reasonable cost commensurate with the service rendered and complexity of the tax return. We are available throughout the year for any questions you may have concerning taxes or other financial matters.

Please send in all tax information by April 7th so we may complete your tax return timely. After that date, it may be necessary to file an extension. Please call our office if an extension is necessary.

We would also like to remind business owners that tax filings for Partnerships and S- corporations are due March 15, 2021. C-corporations tax filings are due April 15, 2021. Please forward all necessary information as soon as possible to assist us with filing your tax return on a timely basis.

We will commence accepting tax information starting February 1, 2021 through April 7, 2021. For your convenience we are still accepting credit card payments.

If you have any questions, feel free to contact us. You may visit our website at www.rsabrams.com for updated information on tax matters and other relevant changes. We would like to take this opportunity to thank you for your confidence in us and to wish you Happy Holidays.

Very truly yours,

R.S. Abrams + Co., LLP

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