2020 Year-End Tax Planning for Businesses

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CPAs and Advisors

ACCELERATE YOUR PERFORMANCE

Tax Relief Strategies for Resilience

As the world continues to contend with the COVID-19 pandemic and its economic fallout, businesses are doing all they can to mitigate risks and plan for a recovery that's anything but certain.

The path forward will likely not be linear. Different regions, industries and business segments may be in different stages of recovery simultaneously.

The tax function plays a critical role in navigating recovery and positioning businesses to emerge from this crisis more resilient than before. Effective tax strategy can preserve liquidity, lower costs and work in tandem with overall business strategy.

Read on to explore the tax relief tactics that can help take your business from reacting to the day-to-day challenges to taking advantage of those incentives that are available to help move your business forward.

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Finding Relief:
Tax Strategies to Generate Immediate Cash Flow

During “the dip” immediately following a crisis, businesses of all sizes are in triage mode, taking immediate action to both protect their employees and keep the lights on. Achieving these goals requires agility, strategy and resilience, as well as liquidity.

During these challenging times, companies must have access to cash to help offset unforeseen costs, whether for buying personal protective equipment (PPE) for on-site employees or investing in the technology needed to keep a remote workforce safely and efficiently connected.

The tax function can be instrumental to identify and execute cash flow opportunities and to maintain the levels of liquidity needed to navigate the uncertainty that lies ahead. In the short term, tax professionals should look to “low-hanging fruit” to generate benefits as quickly as possible.

While not exhaustive, here are several tax strategies to consider:

1. Debt and losses optimization

- File net operating loss (NOL) carryback and alternative minimum tax (AMT) credit refund claims to reduce tax payments and obtain immediate refunds for taxes paid in prior years.
- File Form 1138 to relieve 2019 tax payments due with the 2019 returns for corporations expecting a 2020 loss that could be carried back to the earlier year.
- Analyze the tax impact of income resulting from the cancellation of debt in the course of a debt restructuring for possible exceptions due to insolvency or bankruptcy. Alternatively, if the income is taxable, consider possible strategies to generate capital gain vs ordinary income during a debt workout transaction.
- Consider claiming losses related to worthless, damaged or abandoned property to generate ordinary losses under for specific assets, for insolvent investments in subsidiaries that are at least 80% owned (under Section 165(g)(3)) and for certain insolvent investment entities taxed as partnerships. Certain losses attributable to COVID-19 may be eligible for an election under Section 165(i) to be claimed on the preceding tax year’s return, possibly reducing income and tax in the earlier year, or creating an NOL that provides an additional year of carryback potential in which to receive a refund.
- Decrease estimated tax payments based on lower 2020 income projections, if over-payments are anticipated.
- Consider filing accounting method changes to accelerate deductions and defer income recognition with the goal of increasing a loss in 2020 for expanded loss carryback rules under the CARES Act. Common method changes include deferral of advance payments, accelerating the deduction of certain prepaid expenses to the year of payment under the 12-month rule, deducting software development costs in the year incurred and applying the recurring item exception for property taxes, state taxes, rebates, allowances and payroll taxes.

2. Contingent fee tax projects

- Explore projects like sales or use tax recovery services and income tax return reviews, which can recover previously paid state and local taxes (or even VAT outside the United States, if applicable).

- Consider IRS Account and Interest Recovery Services (AIRS SM) projects to identify IRS errors in processing and posting payments and to recover misapplied payments and interest.

3. International tax savings

- Review U.S. customs and duties for relaxed tariffs on some products and watch for extensions to pay duties, taxes and fees.

- Mobilize cash from foreign operations while considering repatriation costs (e.g., previously taxed earnings and profits and basis amounts, withholding taxes, local reserve restrictions, Sections 956 and 245A).

4. Making the most of legislation

- Understand how the CARES Act can provide relief to employers:
  - Defer payment of the employer's share of Social Security taxes (i.e., 6.2% of payroll; deferral of Medicare taxes is not allowed). Deferral is allowed only until the earlier of (1) Dec. 31, 2020, or (2) the date the employer's Paycheck Protection Program (PPP) loan is forgiven. Half of the deferred deposit must be repaid by Dec. 31, 2021, and the other half must be repaid by Dec. 31, 2022. The deposit deferral is not subject to interest or penalties if the deferred amounts are timely repaid.

5. Take advantage of any remaining corporate AMT credit

- This should be fully refundable beginning in 2019, with earlier elective application in 2018.

6. Secure a quick tax refund in 90 days by using Form 1139 to file for a five-year NOL carryback for losses generated in 2018 through 2020

- Taxable income for a year can be fully offset due to a temporary suspension of the 80% income limitation.

7. Consider the employee retention credit

- This which allows for a refundable payroll tax credit for eligible employers harmed by COVID-19. The credit is equal to 50% of up to $10,000 in qualified wages per employee (i.e., a total of $5,000 per employee). Employers generally are not eligible for the Employee Retention Credit if any member of their controlled or affiliated service group obtained a PPP loan.

Regardless of which tax strategies you choose to leverage, keeping the focus on generating and retaining cash will ensure that your business is prepared to weather an extended period of disruption.

Optimizing Operations: Undercover Tax Relief Operations

During "the trough" period of economic recovery, the initial tumult of the pandemic and economic fallout has passed, but significant challenges remain. Although companies that have managed to survive up to this point will have overcome immediate safety and cash flow problems, they still face an uncertain future. No one can predict how long the downturn will last, whether the world will revert into crisis mode or whether the path towards long-term recovery has begun.

Despite the uncertainty, savvy companies can position themselves to outperform their competitors by capitalizing on market shifts and strengthening their core business models. To do so, liquidity will continue to be at a premium, but many companies at this stage should be able to spend a bit in order to reap considerable returns. The tax function is poised to help them do just that.

After taking advantage of tax solutions that are within reach, it's time to consider low-risk strategies that will plant the seed for future growth. Consider which tax strategies can help you find a competitive edge, including:

1. Uncovering missed opportunities for savings:

Look for potential projects that, though they may require an upfront investment of time and capital, have the potential to reveal significant savings opportunities.

- R&D tax credit studies: The money companies spend on technology and innovation can offset payroll and income taxes via R&D tax credits. The credits benefit a broad range of companies across industries, yet many businesses are leaving money on the table.
- Property tax assessment appeals: In the wake of the COVID-19 pandemic, some jurisdictions are reevaluating their property tax processes, for example, via disaster relief and conducting assessments at an earlier date. However, assessed property values tend to lag true market value in an economic recession. Property tax appeals can generate cash savings by challenging assessed values and reducing property tax liabilities.
- Cost segregation studies: Cost segregation studies can help owners of commercial or residential buildings increase cash flow by accelerating federal tax depreciation of construction-related assets. The extension of bonus depreciation for assets with a useful life of 20 years or less, including qualified improvement property as corrected by the CARES Act, will substantially enhance the benefit of these studies. Depending on the type of building and cost, the increased cash-flow and time-value benefits are often significant.
- State and local credits and incentives projects: By taking advantage of existing programs, as well as those implemented as a result of COVID-19, companies can qualify for state tax credits and business incentives. These programs help companies maintain payroll, manage business costs, such as utilities, and facilitate capital investment.
- Opportunity zone program: This federal program is structured to encourage investor to shift capital from existing assets to distressed, low-income areas, and in doing so, deferring and even reducing taxes. While investment in opportunity zones has slowed recently, COVID-19 and additional guidance has created renewed interest in using this program to assist with undeserved communities and to provide tax relief for investors.

Advising on business decisions: In this phase, it's likely that your C-suite is beginning to think about what's next. Tax professionals should aim to provide strategic insights into the tax implications of these critical business decisions, including supply chain shifts, transactions, restructuring and more.

2. Maintaining compliance:

If your business secured any federal funding in the early stages of the pandemic, those funds likely came with certain tax and financial reporting compliance measures attached. Work with the finance and accounting department to ensure that these benefits don't result in unexpected penalties and costs. You should also aim to secure forgiveness for any forgivable loans.

3. Continue to grow liquidity:

Cash is still key to navigating an uncertain road ahead. Continue to leverage liquidity-generating tactics, such as:

- Evaluating existing accounting methods and changing to optimal methods for accelerating deductions and deferring income recognition, thereby reducing taxable income and increasing cash flow.
- Reviewing transfer pricing strategies to identify opportunities to optimize cash flow.
- Pursuing a tax deduction through charitable donations.
- Maximizing state NOLs through elections, structural changes, inter-company transactions and triggering unrealized gains.

Businesses that effectively use tax strategies to focus on seizing the strategic opportunities they do have will be able to make the most of tough conditions and emerge as market leaders.

Moving Forward:
Adopt New Business Strategies to Re-imagine the Future

In the recovery phase, demand for goods and services has returned to pre-pandemic-recession levels. The wisest companies won't spend this time resting on their laurels but will instead use it to re-imagine their futures in a world forever changed.

Plans made prior to spring 2020 may no longer make sense in a post-COVID world. To stand apart from competitors, companies need to not only recover from COVID-19, but also integrate the lasting forces of change brought on by the pandemic to emerge more resilient and more agile than before it began.

It's time to reset vision and strategy – and tax needs to be an integral part of that process.
On the next page, review ways that tax can align with new business strategies.

1. Workforce

In this phase, businesses have likely confirmed near-term strategies around where employees will work. While these plans need to balance employee safety and operational efficiency, they also come with important tax impacts.

Tax Considerations:

- Assess the tax implications of your mid- to long-term workforce strategy, whether it's on-site, fully remote or a hybrid approach.
- Ensure tax compliance with state or local tax withholding for employees working remotely.
- Consider the tax implications of outsourcing any business functions.

2. Finances

As demand for products and services increases, it's likely that profits will grow as well, meaning many companies that may have been incurring losses may find themselves with taxable income again. At this point, tax strategies should focus on lowering the organization's total tax liability.

Tax Considerations:

- Optimize the use of any available credits, incentives, deductions, exemptions or other tax breaks.
- Maximize the benefit of changes to the net operating loss rules included in the CARES Act.
- Consider the foreign-derived intangible income (FDII) deduction, if applicable (i.e., companies that earn income from export activities).

3. Transactions

Many businesses may be considering strategic transactions, such as acquiring another company, merging with a peer, selling certain assets or purchasing new resources. Each of these actions can have multiple tax consequences.

Tax Considerations:

- Assess potential tax benefits or liabilities of strategic transactions before they take place as a part of the due diligence process.
- Identify loss companies and plan around utilizing losses and credits.
- Structure acquisitions and divestitures in a tax-efficient manner to increase after-tax cash flow.

4. Innovation

As companies reconfigure their businesses to adapt to COVID-19 changes that are here to stay – from greater shifts to e-commerce to outsourced back office functions to partially remote work arrangements – they should determine how to use tax strategies to offset the costs of these investments.

Tax Considerations:

- Consider using federal, state or even other countries' R&D tax credits to offset costs of new products, processes, software and other innovations.
- Explore whether previously undertaken activities may have qualified for these credits as well.

5. Regulations and Legislation

As the economy improves, regulatory oversight likely will increase as well. Non-compliance can be costly and can reverse much of the progress a business has made in its recovery. At the same time, it's likely that additional tax law changes are on the horizon, and companies will need to be able to act quickly when they appear.

Tax Considerations:

- Ensure compliance with rules around federal funding received during the pandemic.
- Monitor tax regulatory and legislative developments at all levels, especially in the area of digital taxation, post-election tax reform, and federal, state and local policy changes.
- Scenario plan to outline the potential impact of future tax legislation on the company's overall tax liabilities.

6. Transformation

Staying ahead in the "new normal" means accelerating efforts around digital transformation to build a business with agility and resilience at its core. This should always include evolving the tax function. Businesses must strive to fully integrate processes, people, technology and data to understand total tax liability and forecast how decisions and changes will impact their tax standing.

Tax Considerations:

- Collaborate with leadership and other areas of the business on a company-wide approach to digital transformation efforts.
- Establish a clear, shared vision of the future state of the tax department.
- Develop the business case for transformation efforts.

Whatever pivots your business takes once the worst has passed, tax strategy needs to be an integral part of the plan to move forward. Evolving your tax strategy alongside business strategy will help prevent unforeseen costs and maximize potential savings.

Planning for What's Next:
Be Prepared to Seize Opportunities

The reality for many is that it may take years to get the phase when a business is meeting or even exceeding market growth. During this stage, a company has fully recovered from the business challenges of the pandemic-recession and is experiencing significant growth. It's a time when many businesses will be executing the long-term plans they've crafted throughout their recovery journey. But companies should consider the tax effects of acting on these plans.

Key Tax Strategies

- Use tax transformation to maintain a broad view of your total tax liability.
- As a business executes on tax transformation plans, it should leverage automated solutions for manual and error-prone areas, including state and local sales and use taxation, value added tax, etc.
- Consider the tax benefits of outsourcing non-essential functions to third parties to lower a company's total tax liability.
- Review federal Work Opportunity Credit criteria for eligible new hires.
- Consider eligibility for paid family and medical leave. Under the new law, an eligible employer is allowed the paid family and medical leave credit, which is an amount equal to a percentage of wages paid (up to 25%) to qualifying employees during any period in which those employees are on family and medical leave due to a critical illness or the birth (or adoption or foster care) of a child.

  The applicable percentage is 12.5%, increased (but not above 25%) by 0.25 percentage points for each percentage point by which the rate of payment exceeds 50%.
- Consider alternative legal entity structures to minimize total tax liability and enterprise risk.
- Regularly monitor and assess potential regulatory and legislative changes at the federal, state and local levels, as well as in other countries, if applicable.
- Continuously iterate and adjust tax strategies to align with overall business strategies.
- Evaluate global supply chain and cross-border transactions to minimize global tax liability.

Most importantly, companies need to continue to plan for what's next. While the immediate threat of the pandemic has abated in this stage, new threats are inevitable. But alongside those threats come new opportunities for the businesses poised to seize them.