BY RICH SHAVELL

Two 2019 Tax Laws Impact Multiple Years

When preparing their 2019 tax returns, construction companies and their shareholders should consider the impact of the *Taxpayer Certainty and Disaster Tax Relief Act of 2019* (Disaster Act) and the *Setting Every Community Up for Retirement Enhancement Act of 2019* (SECURE Act), which are both part of the *Further Consolidated Appropriations Act of 2020* (H.R. 1865, P.L. 116-94).[1]

Disaster Act

Signed into law on December 20, 2019[2] and often referred to as the "extenders bill," the Disaster Act extends over 30 code provisions that expired (or were set to expire) through 2020. Let's look at a few that could impact the commercial contractor and construction company shareholder-owners.

Tax Credits for Construction Businesses

It is important to recognize that credits are a direct reduction against the tax liability, whereas deductions are an offset against the taxable income that is multiplied by the applicable tax rates. A credit is therefore worth *more* in tax savings than a deduction, even after adding back the wages (or other expense) deduction.

Empowerment Zones

Businesses located or operating within an empowerment zone and that also have W-2 employees living within an empowerment zone are eligible for specific tax incentives, including:

- A credit of 20% of the first $15,000 of qualified wages;[3]
- Special §179 expensing rules whereby an extra $35,000 of expensing is permitted along with an increase to the phase-out computation;[4] and
- Capital gain deferrals on the sale of qualified assets that are sold and replaced.[5]

The empowerment zone designations originally expired at the end of 2017 but have been extended through December 31, 2020 under the Disaster Act.[6] The key here is for the contractor to identify both the jobs located in a federal empowerment zone and which employees also reside within an empowerment zone.[7] The first $15,000[8] of qualified wages for zone residents who also work on jobs within a zone are then multiplied by 20% to determine the tax credit. As with many labor-based credits, the contractor adds back the wage deduction in exchange for the credit.

Work Opportunity Tax Credit

For several decades, the Work Opportunity Tax Credit program provided incentives for businesses and contractors to hire individuals who may face difficulty gaining employment. Hiring (and timely documenting) these new employees' circumstances permits a general business credit that is extended by the Disaster Act through 2020.[9]

Generally, the 10 targeted groups for new hires are:

1) Qualified IV-A recipients (Temporary Assistance for Needy Families (TANF))
2) Qualified veterans
3) Qualified ex-felons
4) Designated community residents
5) Vocational rehabilitation referrals
6) Qualified summer youth employees
7) Qualified nutrition assistance program benefits recipients
8) Qualified SSI recipients
9) Long-term family assistance recipients
10) Qualified long-term unemployment recipients

For example, consider one new employee, a vocational rehabilitation referral, who is earning $50,000 annually. In this instance, the contractor would claim a credit for $2,400, which is 40% multiplied by the first $6,000 of qualified wages. There is paperwork that must be timely filed to qualify and certify the new hires and, for several of these categories, there are specific rules, increased rates, and qualified wages thresholds.

New Markets Tax Credit

Under the new markets tax credit, a percentage of the capital invested in a qualified community development entity results in a credit. A qualified community development entity is defined as a for-profit or non-profit entity that loans or invests substantially all of its capital in qualified businesses operating in low-income communities.

The Disaster Act adds $5 billion to the new markets tax credit allocation for 2020[10] and also extends the carry-over period for unused new markets tax credits through 2025.[11] This, along with several other changes discussed later, is a potential indirect benefit to the construction industry since the credit could lead to more construction business thanks to the increased investment in property.

Employer Tax Credit for Paid Family & Medical Leave

The Disaster Act extends the credit through 2020,[12] enabling employers to take a general business credit based on the wages paid to qualifying employees for family and medical leave. The credit varies from 12.5-25% of eligible wages with a maximum of 12 weeks each tax year for each qualifying employee.

At press time, Congress passed new laws including the *Families First Coronavirus Response Act* (H.R. 6201) and the *Coronavirus Aid, Relief, and Economic Security Act* (CARES Act) (H.R. 748), which impacts this and several other provisions. As always, before implementing any tax provisions and strategies discussed herein, you should review these laws with your tax advisor. (Visit *cafe.cfma.org/covid-19-resources* for more information and resources that can help your company address the impact of COVID-19.)

Energy Deductions & Credits for Businesses

Energy-Efficient Commercial Buildings Deduction

Energy-efficient improvements to commercial buildings that meet specified energy thresholds result in a deduction under §179D. There's up to $1.80 deduction per square foot available for qualified construction property, and a partial $0.60 deduction per square foot applies when the entire building does not achieve the requisite energy standards. This generally includes interior lighting systems, HVAC, and the building envelope. The Disaster Act extends these deductions to property placed in service before January 1, 2021.[13]

There is an opportunity for contractors to obtain the §179D deduction for projects with governmental agencies. The jurisdictions do not have the need for tax deductions and can specify the designer entitled to the deduction.[14]

An impediment is that the jurisdiction, or its agency, generally supplies an allocation letter confirming which contractor-designers or specified subcontractors are entitled to the deduction for one of the systems for the entire project. Time and effort may need to be spent educating representatives of the jurisdiction for this deduction.

Like many of these "extenders," the §179D deduction expired at the end of 2017. With the retroactive extension of the credit through 2020, property owners and contractors have a refund opportunity for tax year 2018.

Energy-Efficient Homes Credit

The Disaster Act extends the credit for new energy-efficient homes acquired before January 1, 2021.[15] For the construction or manufacture of a new energy-efficient home that meets qualifying energy criteria, the eligible contractor may claim a tax credit of $1,000 to $2,000.

Depreciation

There are several provisions that enhance depreciation deductions. As mentioned previously, the economic concept for the construction industry is that the increased depreciation incentive could lead to more construction business because the entities capable of deducting the accelerated depreciation will invest in more property. For those provisions that expired at the end of 2017, there may be a refund opportunity by amending 2018 tax returns.

Motorsports Entertainment Complexes

The law provides a seven-year recovery period for motorsports entertainment complexes. For property placed into service after December 31, 2017, the Disaster Act extends the seven-year recovery period through 2020.[16]

Business Property on Reservations

Under this provision, qualified property is predominantly used for business purposes within a reservation, owned by someone unrelated to the previous owner, and unrelated to gaming practices. For property placed into service after December 31, 2017, the Disaster Act extends the use of accelerated depreciation for these properties through 2020.[17]

Expensing Rules for Certain Productions

Up to $15 million of the cost ($20 million for certain areas) of a qualifying film, television, or theatrical production can be expensed in the year the expenditure was incurred. The Disaster Act extends this deduction through 2020 for productions commencing after December 31, 2017.[18]

For Shareholders

Credit for Health Insurance Costs

The Disaster Act extends the Health Coverage Tax Credit (HCTC) through 2020.[19] This is a refundable credit (72.5% of the premiums paid) for coverage of the eligible individual and qualifying family members under qualified health insurance.[20]

Discharge of Qualified Principal Residence Indebtedness Excluded from Gross Income

During the housing crisis, Congress permitted homeowners to exclude cancellation of debt income for principal residences with caps on the amount that could be excluded. The Disaster Act retroactively extends this exclusion to discharges of indebtedness before January 1, 2021.[21] The threshold for qualified principal residence debt remains up to a $2 million limit ($1 million for married individuals filing separately).

If cancellation of debt income for your principal residence was taxed on your 2018 income tax return (which was after the exclusion expired), you can amend your 2018 return and get a refund.

Mortgage Insurance Premiums for Principal Residences

The Disaster Act extends the deduction for mortgage insurance premiums paid, which expired after 2017, through 2020.[22] There are limitations on the amounts that can be deducted, and the deduction is phased-out depending on the taxpayer's adjusted gross income.

Nonbusiness Energy Property

The Disaster Act retroactively extends, through 2020, the credit for purchases of nonbusiness energy property placed in service after January 31, 2017.[23] This credit is 10% of the cost for qualified energy improvements to the building envelope for principal residences and includes windows, doors, skylights, and roofs. Also, there is a fixed amount of $50 to $300 (with a lifetime cap of $500) for specified energy-efficient improvements (i.e., furnaces, boilers, biomass stoves, heat pumps, water heaters, central air conditioners, and circulating fans).

Qualified Fuel Cell Motor Vehicles

For purchases of new qualified fuel cell motor vehicles, a tax credit ranging from $4,000 to $40,000[24] is available depending on vehicle weight. Other fuel-efficient vehicles may qualify for credits from $1,000 to $4,000. The Disaster Act extends this credit through 2020.[25]

SECURE Act of 2019

The SECURE Act,[26] which was signed into law on December 20, 2019,[27] will impact many company-sponsored retirement plans and how contractors plan for retirement. Many of the provisions go into effect in 2020, so evaluating how these new rules will impact your tax and retirement planning situation is important.

While not all of the changes to the law are favorable, they may provide some tax savings opportunities. Let's look at a few of the provisions that could impact the construction company and its owners.

For the Shareholder

Maximum Age for IRA Contributions Repealed

Starting in 2020, working individuals, regardless of age, can make contributions to a traditional IRA if the individual has compensation (earned income from wages or self-employment).[28] Before 2020, traditional IRA contributions were not permitted after an individual reached age 70-and-a-half.

Age for Required Minimum Distribution Elevated

Before 2020, IRA owners and retirement plan participants were required to begin taking their required minimum distributions (RMDs) by April 1 of the year following the year they reached 70-and-a-half years old. After December 31, 2019, required distributions for those individuals who were 70-and-a-half years old increased to age 72.[29]

As noted previously, recent legislation affects some of these provisions and, in this case, RMDs are waived and not required during 2020.[30]

Elimination of Most "Stretch" IRAs

Before 2020, when plan participants or IRA owners died, their beneficiaries were permitted to stretch out the time they had to take distributions from inherited IRAs and pay the corresponding tax. This was done by using the beneficiary's life expectancy and is known as a "stretch" IRA.

Beginning in 2020 (later for some participants in collectively bargained plans and governmental plans), certain beneficiaries can no longer employ this "stretching" strategy.[31]

Distributions to most non-spouse beneficiaries are generally now required to be distributed within the 10 years following the death. In turn, this accelerates the time the corresponding tax must be paid.

There are exceptions to the new 10-year rule for:

- The surviving spouse;
- A child of the plan participant or IRA owner who has not reached majority;
- A chronically ill individual; and
- Any other individual who is not more than 10 years younger than the deceased plan participant or IRA owner.[32]

The beneficiaries who qualify under one of these exceptions continue to take their distributions over their life expectancy, which is the same as the rules before 2020.

IRC §529 Education Savings Plans Expanded

A §529 education savings plan (tax-exempt tuition plan) is a program established and maintained by a state or one or more eligible public or private educational institutions. Anyone can make nondeductible cash contributions to a §529 plan for a designated beneficiary whereby the earnings accumulate tax-free. Distributions from a §529 plan are generally excludable up to the amount of the designated beneficiary's qualified higher education expenses.

Before 2019, expenses for registered apprenticeships or student loans were *not* qualified higher education expenses. Now, on a retroactive basis, the SECURE Act permits that tax-free distributions from §529 plans after December 31, 2018 can be used to pay for fees, books, supplies, and equipment required for the designated beneficiary's participation in an apprenticeship program.[33]

Moreover, tax-free distributions from §529 plans (up to $10,000) can be used to pay the principal or interest on a qualified education loan of the designated beneficiary (or a sibling of the designated beneficiary). However, you cannot deduct the interest expense, if permissible. The code prevents a potential double benefit of using tax deferred distributions from a §529 to pay student loan interest while also claiming an interest deduction.[34]

By simply establishing a separate savings account for your child's education using a designated §529 plan, the earnings (such as interest or dividends) remain in the §529 plan and are tax free if later used for qualified expenses. With this law, Congress expands the nature of the qualifying higher education expenses and now permits recharacterization of those expenses retroactively to the beginning of 2019.

For the Contractor's Sponsored Retirement Plans

Multiple Employer Plan (MEP) Rules Liberalized

A multiple employer plan (MEP) is a single plan maintained by two or more unrelated employers. Starting in 2021, the new rules reduce various barriers, increasing opportunities for small employers to band together to obtain more favorable investment results.[35] Through economies of scale, this may result in more efficient and less expensive management services.

New & Increased Small Employer Plan Credits

Starting in 2020, there is a new tax credit (up to $500 per year) for employers to defray start-up costs for new 401k and simple IRA plans if they include automatic enrollment.[36] Research indicates that automatic enrollment increases employee's participation and retirement savings likewise increase.[37] This new credit is for three years, can be claimed in addition to an existing plan start-up credit, and is available by simply adding the automatic enrollment feature to an existing plan.

The SECURE Act increases the credit for plan start-up costs for small businesses that are setting up retirement plans.[38] The credit's flat dollar amount limit is now the greater of $500; the lesser of $250 multiplied by the number of non-highly compensated employees eligible to participate in the plan; or $5,000.[39] The maximum credit is $5,000 (minimum is $500) and applies for up to three years starting in 2020.[40]

Long-Term Employees Who Work Part-Time to Participate in 401k

Beginning in 2021, certain part-time employees will become eligible to participate in 401k plans.[41] The SECURE Act requires most employers maintaining a 401k plan to implement a dual eligibility requirement whereby an employee completes either one year of service (1,000-hour rule) or three consecutive years of service where the employee completes at least 500 hours of service per year (500-hour rule). For employees who are eligible solely because of the new 500-hour rule, the employer is permitted to exclude part-time employees from testing under the nondiscrimination, coverage, and top-heavy rules.

Deadline to Establish New Plan Extended to Following Year

The current rules require plans be adopted by certain dates before the end of the year. Starting in 2020, the SECURE Act permits employers to elect to treat newly established qualified retirement plans adopted after the close of a tax year as having been adopted on the last day of the year.[42] The deadline is the due date (including extensions) for the annual income tax return.

For a calendar year employer, this is generally September 15 of the following year, which is the extended due date when an extension is filed. The additional time adds flexibility for employers considering a plan. For some contractors, the extension enables more certainty as to where annual net income falls for the preceding tax year before establishing the plan. This also may enable employees to receive contributions for the earlier year.

New Annual Disclosures

The SECURE Act requires that plan participants' benefit statements include new planning disclosures.[43] A lifetime income disclosure is to be issued at least once during any 12-month period. The disclosure is intended to illustrate the monthly payments employees would receive if the total account balance were used to provide lifetime income streams. This includes illustrations for a qualified joint and survivor annuity for the participant and the participant's surviving spouse as well as a single life annuity. The date for starting the new disclosure requirements is not yet set.

Summary

While not heavily publicized, there are several tax opportunities in these two tax laws that should be carefully evaluated by construction company owners and their CFMs.

Elevating communication with tax preparers will be vital to ensure that refund opportunities are pursued (i.e., for 2018 tax returns that can be amended) and new prospective tax deduction/credit opportunities are considered (i.e., credits for establishing new company sponsored retirement plans). This summary does not cover all the nuances and requirements for each respective tax provision, so construction company owners and CFMs should always review the details with their tax advisors. ■

Endnotes

1. *www.congress.gov/bill/116th-congress/house-bill/1865.*
2. *www.congress.gov/bill/116th-congress/house-bill/1865.*
3. IRC §1396.
4. IRC §1397A(a).
5. IRC §1397B.
6. IRC §1391(d)(1)(A)(i).
7. IRC §1396(d)(1).
8. IRC §1396(c)(2).
9. IRC §51(c)(4).
10. IRC §45D(f)(1)(H).
11. IRC §45D(f)(3).
12. IRC §45S(i).
13. IRC §179D(h).
14. IRC §179D(d)(4); Notice 2008-40.
15. IRC §45L(g).
16. IRC §168(i)(15)(D).
17. IRC §168(j)(9).
18. IRC §181(g).
19. IRC §35(b)(1)(B).
20. IRC §35(a).
21. IRC §108(a)(1)(E).
22. IRC §163(h)(3)(E)(iv)(I).
23. IRC §25C(g)(2).
24. IRC §30B(b)(1).
25. IRC §30B(k)(1).
26. *www.congress.gov/bill/116th-congress/house-bill/1865.*
27. *www.congress.gov/bill/116th-congress/house-bill/1865.*
28. IRC §219(d)(1).
29. IRC §401(a)(9)(C)(i)(I).
30. IRC §401(a)(9)(I)(i).
31. IRC §401(a)(9)(H)(i).
32. IRC §401(a)(9)(E)(ii).
33. IRC §529(c)(8).
34. IRC §221(e)(1).
35. IRC §413(c)(1) and 413(e)(3).
36. IRC §45T.
37. *www.pewtrusts.org/en/research-and-analysis/articles/2018/08/15/automatic-enrollment-can-boost-retirement-plan-participation.*
38. IRC §45E(b)(1).
39. IRC §45E(b).
40. IRC §45E (b)(1).
41. IRC §401(k)(15).
42. IRC §401(b).
43. SECURE Act §203.

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