**SELF-EMPLOYMENT TAX DEFERRAL FOR 2020**

Under the CARES Act, individuals who pay self-employment tax have the option to defer part their self-employment tax liability for 2020 to tax years 2021 and 2022. However, this must be carefully considered before making the election.

Background

Self-employed taxpayers (including certain partners and LLC members) must self-employment tax on their profits. This is how they qualify for Social Security and Medicare benefits. Employees ordinarily have these taxes withheld from their paychecks by their employers (7.65% is withheld from their pay and 7.65% is matched by the employer). Those who are self-employed report their self-employment income on their appropriate tax schedules (Schedules C or E) and pay approximately 15.3% self-employment tax on their earnings by filing Schedule SE.

New for 2020

The CARES Act allows taxpayers to defer the self-employment tax on profits earned between March 27, 2020 and December 31, 2020. Half of the amount deferred is payable on their 2021 return and the other half is payable on their 2022 return. Deferral is optional, meaning that the taxpayer can elect to pay all the tax on the 2020 return as usual.

Pros

Deferring the tax puts more cash in your pocket now. It will decrease your balance due. (Note that deferral is not an option if you have an overpayment on the return).

Cons

Deferring the tax increases the amount of tax you will owe in 2021 and 2022. Clients who make estimated tax payments will need to increase those payments by 1/2 of the amount deferred in 2020.

Example

Jack owns his own business and his 2020 self-employment income is $100,000. Ordinarily the annual self-employment tax due on the business profit is $14,130. Jack can elect to defer $10,770 of his 2020 self-employment tax. This would reduce his 2020 taxes overall by that amount. However, for 2021 and 2022 he would have to report half of the amount deferred in 2020 ($5,385) and increase his 2021 and 2022 quarterly estimated tax by $1,346 to account for the required repayment. Jack could also elect to not defer any of the self-employment tax and simply pay it on his 2020 return.

Is this the best move for you?

This is a personal financial decision. Please consider your current cash flow and cash reserves. Weigh that against the ability to make increased estimated tax payments for the 2021 and 2022 tax years.