

TAX CHANGES FOR 2025



BUSINESSES: IMPORTANT TAX CHANGES IN 2025

As the year draws to a close, it's important that we meet to discuss any year-end strategies that might help lower your business's taxable income for 2025.

New and Expanded Tax Breaks

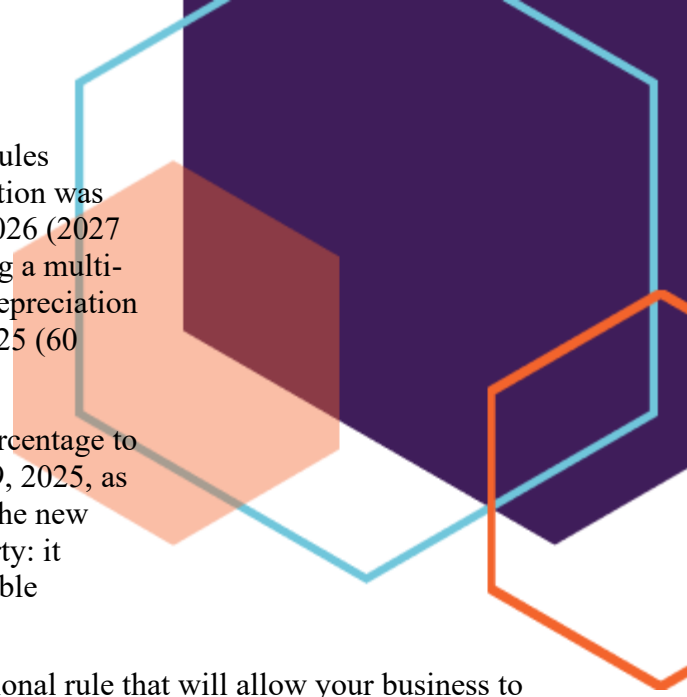
Section 179 Expensing Limit Doubled. Section 179 expensing got a big boost from the OBBBA, which more than doubles the dollar limit on the deduction from \$1.22 million to \$2.5 million. The deduction limit is reduced on a dollar-for-dollar basis (i.e. phased out) by any amount by which the cost of Section 179 property placed in service during the year exceeds a threshold amount as follows:

| For Tax Years Beginning in | Deduction Limit | Phaseout Threshold |
|-------------------------------|-----------------|--------------------|
| 2026 | \$2,560,000 | \$4,090,000 |
| 2025 | \$2,500,000 | \$4,000,000 |
| 2024 | \$1,220,000 | \$3,050,000 |

Passenger automobiles subject to the "luxury car" depreciation limitation are eligible for Section 179 expensing only to the extent of certain dollar limitations (\$12,200 for 2025). For sport utility vehicles above the 6,000 pound weight rating and not more than the 14,000 pound weight rating, which are not subject to the luxury car limitation, the maximum cost that may be expensed for 2025 under Section 179 is \$31,300.

Planning Opportunity: If your Section 179 expensing was constrained by the \$1.22 million limit in 2024, it's going to be a lot less constrained in 2025, assuming the phaseout doesn't come into play. Keep in mind that one of the big advantages of Section 179 expensing (as compared to bonus depreciation) is that it allows you to pick and choose which individual assets you expense and even what portion of the cost of each asset you expense, making it a very precise and flexible tax planning tool.

Tax Guru's tax planning checklist of additional action items may help you save tax dollars.



100 Percent Bonus Depreciation Made Permanent. Under rules enacted by the Tax Cuts and Jobs Act (TCJA), bonus depreciation was scheduled to be repealed for property placed in service after 2026 (2027 for longer production period property and aircraft), culminating a multi-year phaseout of the deduction. Under these rules, the bonus depreciation percentage was 40 percent for property placed in service in 2025 (60 percent for longer production period property and aircraft).

The OBBBA permanently increases the bonus depreciation percentage to 100 percent for all qualified property acquired after January 19, 2025, as well as for specified plants planted or grafted after that date. The new law made only one change to the definition of qualified property: it added qualified sound recording productions to the list of eligible property.

Planning Opportunity: The OBBBA provides a transitional rule that will allow your business to elect to apply a 40 percent bonus depreciation percentage (60 percent for longer production period property and aircraft) in the first tax year ending after January 19, 2025. Although it's usually advantageous to apply the maximum bonus depreciation percentage allowed, there are situations where choosing a lower percentage can make sense (for example, to avoid creating a net operating loss).

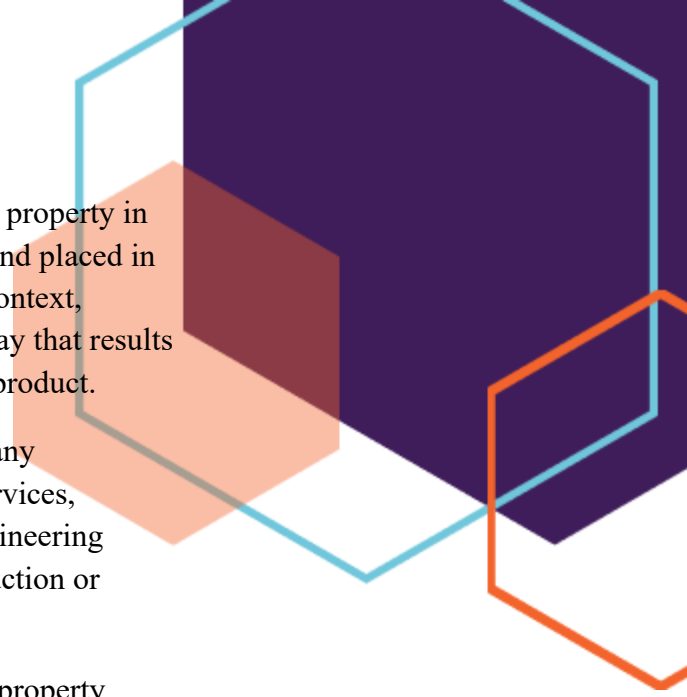
Full Expensing of Domestic Software Development and R&E Expenditures. Reversing TCJA rules that had been in effect since 2022, the OBBBA restores full expensing for domestic software development and research or experimental expenditures ("R&E expenditures"). It leaves in place the rules requiring that foreign software development and R&E expenditures be capitalized and amortized over 15 years.

The OBBBA also provides a rule that allows "small" businesses with annual gross receipts of \$31 million or less to apply the new expensing rules retroactively to tax years beginning after December 31, 2021 by filing amended returns (or, under certain conditions, an original return). In addition, any business (small or large) can write off unamortized domestic software development and R&E expenditures that were capitalized under TCJA ratably over a one- or a two-year period beginning with the business's first tax year beginning after December 31, 2024.

Businesses will continue to have the option of capitalizing domestic software development and R&E expenditures and amortizing them over a period of at least 60 months.

Planning Opportunity: If your business capitalized domestic software development or R&E expenditures for tax years after December 31, 2021, the options for writing them off on an accelerated basis (or filing amended returns) create some fantastic tax planning opportunities. We should discuss them at your earliest convenience.

Special Depreciation Allowance for Qualified Production Property. The OBBBA designates a new category of property referred to as "qualified production property" and allows businesses an additional first-year depreciation deduction equal to 100 percent of the adjusted basis of such property.



Qualified production property is essentially nonresidential real property in the United States (or any possession) used for manufacturing and placed in service after July 4, 2025 and before January 1, 2031. In this context, "manufacturing" means producing or refining a product in a way that results in a substantial transformation of the property comprising the product.

Qualified production property *does not include* the portion of any nonresidential real property used for offices, administrative services, lodging, parking, sales activities, software development or engineering activities, or other functions unrelated to manufacturing, production or refining of tangible personal property.

Recapture Rules. If the use of the qualified production property changes during the 10-year period after the property is placed in service, recapture rules generally apply.

Return to EBITDA for Limit on Business Interest Deduction. For tax years beginning after December 31, 2024, the OBBBA increases the cap on the deductibility of business interest expense by providing that "adjusted taxable income" is determined without taking into account deductions for depreciation, amortization or depletion. As a result, "adjusted taxable income" corresponds with the financial accounting concept of earnings before interest, taxes, depreciation and amortization (EBITDA). This restores a rule that was in effect from 2018-2022.

The OBBBA also changes the rules for coordinating the cap on business interest expenses with the rules for interest capitalization. The new rules require that the business interest limitation be calculated prior to the application of any interest capitalization provision, and that capitalized interest be given priority in utilizing the cap.

Qualified Business Income Deduction. The OBBBA permanently extends the Section 199A deduction for qualified business income that had been set to expire on December 31, 2025. For tax years beginning after 2025, the size of the fixed range of taxable income over which the wage and investment limitation and the SSTB limitation are phased in is increased from \$100,000 to \$150,000 for married individuals filing joint returns, and from \$50,000 to \$75,000 for all others.

For tax years beginning after 2025, the OBBBA also introduces a new, inflation-adjusted, minimum deduction of \$400 for taxpayers who have at least \$1,000 of QBI from one or more active trades or businesses in which the taxpayer materially participates.

Expansion of Qualified Small Business Stock Gain Exclusion. Since it was introduced in 1993, owners of Section 1202 qualified small business stock (QSBS) have been required to hold their stock for at least five years before they could exclude gain from its sale from income. Those exclusions ranged from 50 to 100 percent depending on when the stock was acquired.

The OBBBA enhances the QSBS gain exclusion by providing a tiered gain exclusion for stock acquired after July 4, 2025 as follows:

| Years stock held: | Applicable percentage: |
|-------------------|------------------------|
| 3 years | 50% |
| 4 years | 75% |
| 5 years + | 100% |

For stock acquired after July 4, 2025, the OBBBA also increases the per-issuer exclusion cap to \$15 million, and the corporate-level aggregate-asset ceiling to \$75 million. Both the \$15 million exclusion cap and the \$75 million asset ceiling are indexed for inflation beginning in 2027.

Other New and Expanded Tax Breaks. The OBBBA adds and expands several other tax breaks, including:

Expensing of Qualified Sound Recording Productions. For productions commencing in tax years ending after July 4, 2025, the special expensing rules for qualified film, television and live theatrical productions are expanded to include aggregate qualified sound recording production costs of up to \$150,000 per tax year.

Deduction for Business Meals Provided on Fishing Vessels, Etc. For amounts paid or incurred after 2025, an exception from the 50 percent limitation on the deduction for business meals applies for meals provided on fishing vessels and at certain fish processing facilities.

Qualified Opportunity Zones 2.0. The OBBBA makes the tax break for qualified opportunity zones (QOZ) permanent by instituting decennial designations of QOZs and allowing for deferrals and partial exclusions of gains rolled over into qualified opportunity funds after December 31, 2026.

Capital Gains from Sale of Farmland Property. For sales or exchanges in tax years beginning after July 4, 2025, the OBBBA allows taxes on capital gains from the sale or exchange of qualified farmland property to a qualified farmer to be paid in four equal annual installments. Forms 1099-MISC and 1099-NEC. For payments made after December 31, 2025, the threshold for reporting payments on Forms 1099-MISC and 1099-NEC by a business for services performed by independent contractors is increased from \$600 to \$2,000.

1099-K Reporting for Third Party Network Transactions. The never-implemented de minimis reporting requirement for third-party settlement organizations is repealed retroactive to its enactment as part of the American Rescue Plan of 2021.

Employer-Provided Childcare Credit. For tax years beginning after 2025, the OBBBA permanently increases the limits on the employer-provided childcare credit from \$150,000 to \$500,000 (\$600,000 for eligible small businesses) and increases the credit percentage from 25 percent to 40 percent (50 percent eligible small businesses).

Paid Family Leave and Medical Leave Credit. For tax years beginning after 2025, the OBBBA makes the paid family and medical leave credit permanent, lowers the minimum employee work requirement from 1-year to 6-months, and makes other changes that will make it practical for businesses in all fifty states to claim the credit.

Home/Residential Construction Contracts. For contracts entered into in tax years beginning after July 4, 2025, the OBBBA eliminates the four-dwelling-units-per-building limit on "home construction contracts," allowing builders to use the completed contract method for a broader range of residential construction projects.

Other Key Changes for 2025 and 2026

The One Big Beautiful Bill Act is mostly very good news for businesses. But the sweeping bill also includes several provisions that will increase the tax bills of some businesses, including the repeal of some popular tax breaks.

Excess Business Losses of Noncorporate Taxpayers. The OBBBA makes permanent the rules that disallow the deduction of "excess business losses" by noncorporate taxpayers. Excess business losses are the excess of current-year net business losses over an inflation-indexed threshold amount (see table below). The OBBBA also resets the base year for inflation indexing of the threshold from 2018 to 2025, resulting in a decrease in the threshold in 2026:

| For Tax Years Beginning In | Threshold Amount Joint Returns | Threshold Amount All Others |
|----------------------------|--------------------------------|-----------------------------|
| 2024 | \$610,000 | \$305,000 |
| 2025 | \$626,000 | \$313,000 |
| 2026 | \$512,000 | \$256,000 |

One Percent Floor on Charitable Contributions by Corporations. The OBBBA keeps in place the longstanding 10-percent limit on the deduction for corporate charitable contributions and adds a 1 percent floor. For tax years beginning after December 31, 2025, a corporate taxpayer may claim a deduction for charitable contributions only to the extent that total contributions exceed one percent of its taxable income and does not exceed 10 percent of its taxable income.

Excise Tax on Remittance Transfers. For transfers made after 2025, the OBBBA imposes a 3.5 percent excise tax on remittance transfers. The tax is paid by the sender and collected by remittance transfer providers. For purposes of the new tax, remittance transfers are cross-border transfers of cash or similar instruments between U.S. senders and recipients in foreign countries.

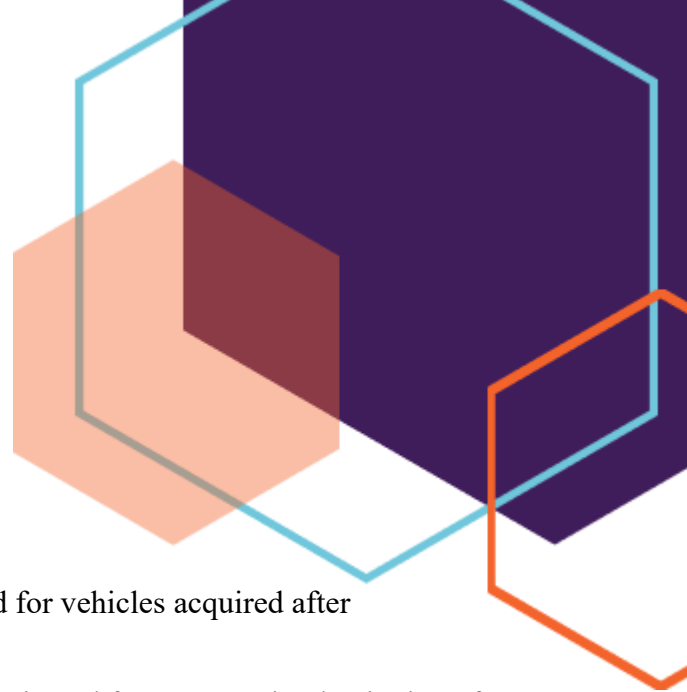
Repeal of Clean Energy Tax Breaks for Businesses. The OBBBA terminates several clean energy tax breaks for businesses enacted by the Inflation Reduction Act of 2022 by moving up their expiration dates (most were scheduled to expire at the end of 2032 or 2034):

- The qualified commercial clean vehicle credit is terminated for vehicles acquired after September 30, 2025.
- The energy efficient commercial buildings deduction is terminated for construction beginning after June 30, 2026.
- The alternative fuel vehicle refueling property credit is terminated for property placed in service after June 30, 2026.
- The clean hydrogen production credit is terminated for facilities the construction of which begins on or after January 1, 2028.
- The special five-year cost recovery period for certain energy property is terminated for construction beginning after December 31, 2024.

The OBBBA also curtailed the availability of several other clean energy credits, most notably the clean electricity production credit.

Other Year-End Tax Considerations

Rental Real Estate. If you have any rental real estate activities, it's important to determine if the activity will be considered a passive activity by the IRS. Generally, losses from passive activities are only deductible against passive activity income. However, a deduction of up to \$25,000 (\$12,500 if married filing separately) may be allowed against nonpassive income to the extent you actively participate in the rental real estate activities. This deduction is subject to a phaseout for individuals with modified adjusted gross income above \$100,000 (or \$50,000 if married filing separately). Additionally, you may be eligible for a qualified business income deduction if certain criteria are met, such as the rental activity qualifying as a Section 162 trade or business.



Substantiation of Vehicle-Related Deductions. In audits, the IRS tends to focus on deductions taken for vehicle expenses. If not properly substantiated, such deductions are disallowed. Thus, if vehicles are used in any part of your business or business-related activities, your tax records with respect to each vehicle should include the following:

- the amount of each separate expense with respect to the vehicle (e.g., the cost of purchase or lease, the cost of repairs and maintenance, etc.);
- the amount of mileage for each business or investment use and the total miles for the tax period;
- the date of the expenditure; and
- the business purpose for the expenditure.

The IRS will consider the following as adequate substantiation for such expenses: (1) records such as a notebook, diary, log, statement of expense, or trip sheets; and (2) documentary evidence such as receipts, canceled checks, bills, or similar evidence.

It's important to note that records are considered adequate to substantiate the element of a vehicle expense only if they are prepared or maintained in such a manner that each recording of an element of the expense is made at or near the time the expense is incurred.

Employee Benefits. One area I would like to discuss with you are the tax and other advantages your business could reap by offering a retirement plan and/or other fringe benefits to employees. By offering such benefits, your business has a better chance of attracting and retaining talented workers which, in turn, reduces the costs of searching for and training new employees. Contributions made to retirement plans on behalf of employees are deductible and your business may be eligible for tax credits for offering retirement and other benefits.

Flexible Spending Arrangements. If you haven't already done so, you might consider the establishment of a flexible spending arrangement (FSA). An FSA allows employees to be reimbursed for medical expenses and is usually funded through voluntary salary reduction agreements with the employer. The employer has the option of making or not making contributions to the FSA. Some of the benefits of providing an FSA for employees include contributions made by the business being excluded from the employee's gross income, reimbursements to the employee are tax free if used for qualified medical expenses, the FSA can be used to pay qualified medical expenses even if the employer or employee haven't yet placed the funds in the account, and up to \$660 of funds in the FSA can be carried over to subsequent years indefinitely.

Health Savings Accounts. Another popular employee benefit your business might consider is a high deductible health plan paired with a health savings account (HSA). The benefits to your business include savings on health insurance premiums that would otherwise be paid to traditional health insurance companies and having employee wage contributions to the plan not being counted as wages and thus neither the employer nor the employee is subject to FICA taxes on the payroll contributions. As for employees, they can reap a tax deduction for funds contributed to the HSA, and there is no use-it-or-lose-it limit like there is for most flexible spending arrangements (FSAs). Thus, the funds can grow tax free and be used in retirement.

"Starter" 401(k) Plans. Businesses that do not already sponsor a retirement plan can offer a "starter" 401(k) plan. A starter 401(k) plan generally requires that all employees be default enrolled in the plan at a 3 to 15 percent of compensation deferral rate. Employer contributions are not permitted. The limit on annual deferrals is the same as the IRA contribution limit (for 2025, \$7,000 with an additional \$1,000 in catch-up contributions for employees age 50 or older).

Pass-Thru Entity Considerations. If you are operating a business through a pass-thru entity such as a partnership or S corporation, your basis in the entity must be high enough to allow for any loss deduction, if you have one for the year. In such a situation, we should consider the options available for increasing your basis in such entity.

If you are an S corporation shareholder it's important to ensure that you and other shareholders involved in running the business are paid an amount that is commensurate with the work being done. The IRS scrutinizes S corporations which distribute profits instead of paying compensation subject to employment taxes. Failing to pay arm's length salaries can lead to tax deficiencies, interest, and penalties. The key to establishing reasonable compensation is showing that the compensation paid for the type of work an owner-employee does for the S corporation is similar to what other entities would pay for similar work. An S corporation needs to adequately document the factors that support the salary an S corporation owner is being paid.

Also, because there are stringent requirements for who may be an S corporation shareholder, if the number of shareholders have changed or increased during the year, we should review the residency or citizenship status of the S corporation's shareholders and S corporation stock beneficiaries (including contingent and residuary beneficiaries).

Concluding Thoughts

As you can see, there is much to consider before we prepare your 2025 business tax return and calculate any estimated tax payments that might be due in 2025. Please call me at your convenience so we can set a time to meet and review potential strategies for reducing your business's 2025 taxable income and tax liability.

Sincerely,

Tax Guru Team

