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A background image showing a business meeting. Two people are seated at a table, looking at documents. A laptop is visible in the foreground. The image is overlaid with a blue semi-transparent rectangle containing the title and presenter information.

Essential Year-End Tax Planning for Businesses

Presented by:
Brian J. Potter, CPA, CDA
Anthony P. Pokrentowski, CPA

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Brian J. Potter, CPA, CDA
Tax Partner
bpotter@dmcpas.com



Anthony Pokrentowski, CPA
Tax Senior Manager
apokrentowski@dmcpas.com

DM Financial Plaza, 221 S. Warren St.
Syracuse, New York 13202
315-472-9127 | www.dmcpas.com

... Year-End Tax Planning Process

We provide year-end tax planning services for the majority of our business clients

The earlier the process is started, the more control a company can have over tax implications

Information needed:

- Year-to-date internal financial statements
- Internal projections for year-end
- Current Year Fixed Asset acquisitions
- Information on any extraordinary items throughout the year or expected toward year-end
- Future year projections or expectations

... Year-End Tax Planning Process (cont'd)

Our Steps:

- Review the internal financial statements
- Adjust for projected income for the remainder of the year
- Adjust for any projected book adjustments (depreciation, gain or loss, inventory, etc.)
- Calculate/project all book/tax adjustments to get to projected taxable income for the year
- Run projections through shareholders/partners (if an S-Corp or Partnership) to calculate estimated tax for the year based on “As Is” projection
- Meet and discuss the “As Is” projection and opportunities/strategies to lower tax burden at year end
- Finalize year-end planning based on meeting and strategies to enact and provide a final analysis showing projected taxable income/tax if nothing is done vs if year-end strategies are followed

... Year-End Tax Planning Process (cont'd)

Why is year-end tax planning important?

- Can help to control tax burden on a company/owners if there is a very profitable year
 - If we see financials for the first time in February/March, it's generally too late to implement significant strategies to impact taxable income/tax
- Prepare company/owners with income tax cash flow requirements for the April 15th due date
- Provides companies with a specific plan/strategy to follow for the year-end

Tax Strategies & Topics

... #1 – H.R. 7024 - Tax Relief for American Families and Workers Act of 2024

- The Tax Relief for American Families and Workers Act of 2024 (H.R. 7024) was touted as a bipartisan tax bill aimed at helping American families and businesses in the United States;
- First announced by the House Ways and Means Committee on January 16, 2024, the bill was quickly passed by the House on January 31, 2024, by a vote of 357 to 70
- Fast forward to August 1, 2024, after several months of delays and political negotiations, the Senate failed to pass the American Families and Worker's Act of 2024 by 12 votes;
- Had it passed, the bill would have, among other things;
 - Increased the Child Tax Credit;
 - Reinstated the immediate expensing of domestic qualified research expenses;

#1 – H.R. 7024 - Tax Relief for American Families and Workers Act of 2024 (cont'd)

- Reinstate 100% bonus depreciation;
- Reinstate the larger business interest expense deduction; and
- Significantly increased Employee Retention Credit (ERC) penalties and retroactively imposed a January 31, 2024, cutoff date for new ERC claims;

It is highly unlikely that there will be a significant tax legislation passed until after November 2024 election.

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174

- The Tax Cuts and Jobs Act (TCJA), signed into law on December 22, 2017, introduced significant changes to corporate and individual tax laws.
- Among these changes was a delayed provision, effective for tax years beginning after December 31, 2021, where businesses were now required to **capitalize** and **amortize** R&D costs, as opposed to being able to deduct these costs directly as in previous years.

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

- The revised Section 174 rules require businesses to recover the capitalized expenditures over a five-year period, beginning in the taxable year the expenditures are paid or incurred.
- If the expenditures are attributable to foreign research, the five-year recovery period is extended to a fifteen-year period for the foreign research costs.
- Costs required to be capitalized consist of the following directly allocable expenses:
 - Labor costs related to R&D activities
 - Materials and Supplies used or consumed in R&D activities
 - Depreciation or Amortization with respect to property used in R&D activities
 - Travel expenses for the performance of R&D activities

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

Section 174 also requires certain Selling, General, and Administrative (SG&A) expenses to be allocated to R&D activities and included in the expenses required to be capitalized:

- Rent
- Utilities
- Insurance
- Taxes
- Repairs and Maintenance
- Employee Benefits
- Pension/Profit Sharing

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

- The indirect SG&A expenses are allocated to R&D activities based on a cause-and-effect relationship between the costs and the R&D activities or another relationship that reasonably relates the costs to the benefits provided to the R&D activities
- The most common allocation is based on labor:
Labor utilized in the R&D process/Total Labor
- Additional option can be based on square feet:
 - Sq. footage utilized for the R&D process/total sq. footage of the facility
- The ratio used is then multiplied by the indirect costs to calculate the total additional costs required to be capitalized and amortized

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

Example:

Company A has the following Direct R&D expenses:

- Payroll - \$100,000
- Materials & Supplies - \$50,000
- Company A has the following SG&A costs:
 - Rent - \$75,000
 - Utilities - \$20,000
 - Insurance - \$45,000
 - Payroll Taxes - \$20,000
 - Real Estate Taxes - \$30,000
 - Repairs & Maintenance - \$10,000
 - Employee Benefits - \$35,000
 - Pension/Profit Sharing - \$45,000
- Company A has total payroll of \$2,000,000

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

Example: Overhead Allocation Calculation

R&D Labor (\$100,000) / Total Labor (\$2,000,000) = .05

- Allocation:
 - Rent - \$3,750
 - Utilities - \$1,000
 - Insurance - \$2,250
 - Payroll Taxes - \$1,000
 - Real Estate Taxes - \$1,500
 - Repairs & Maintenance - \$500
 - Employee Benefits - \$1,750
 - Pension/Profit Sharing - \$2,250

Total Overhead Allocation to be included = \$14,000

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

Example: Total Capitalized Expense and Amortization

- Labor - \$100,000
 - Materials - \$50,000
 - Overhead - \$14,000
-
- Total Capitalized Costs = \$164,000
 - First Year Amortization = (\$16,400)
 - Total increase to taxable income = \$147,600

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

- Previously, a taxpayer would be allowed to expense the \$164,000 of costs and obtain a reduced R&D tax credit of approximately \$9,840 (under the alternative simplified method and assuming similar R&D costs each year). This would result in total tax savings of \$44,280 for a C Corporation (Deductions of \$164,000 x 21% tax rate plus the amount of the R&D credit).
- The same scenario above in 2024 under IRC 174 would result in tax savings of only \$13,284 (the same R&D credit of \$9,840 plus the current year amortization of \$16,400 x 21% tax rate).

... #2 – Research & Experimental Expenditures – Internal Revenue Code 174 (cont'd)

- Manufacturers have felt the largest affect of IRC 174, but this impacts any business that conducts R&D activities.
- IRC 174 is separate from IRC 41 (R&D Credit), which means businesses cannot simply ignore the R&D credit to avoid the Section 174 rules. IRC 174 is required whether an R&D credit is being claimed or not.
- There is a large upfront cost to IRC 174, but over time the effect on taxable income will even out/potentially lead to an additional deduction due to the prior year's amortization.

... #2 – Insight into Future Legislation

- Will these provisions be ratified or amended by Congress? Will there be a “small business exception?” The answer is, “maybe.”
- There is optimism that Congress will create a workaround to eliminate or significantly modify the capitalization rules in 2025, but, as of today, all we have is uncertainty.

#3 – Maximizing Tax Deductions – Qualified Business Income Deduction

- The Qualified Business Income (QBI) deduction allows eligible taxpayers to deduct up to 20% of QBI, plus 20% of qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income;
- Income earned through a C Corporation or by providing services as an employee is not eligible for the QBI deduction;
- The QBI deduction is available regardless of whether taxpayers itemize deductions on Schedule A or take the standard deduction;
- Eligible taxpayers can claim the deduction through December 31, 2025.

#3 – Maximizing Tax Deductions – Qualified Business Income Deduction

Qualified Business Income Component:

- Deduction of 20% of QBI from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust, or estate.
- Subject to limitations depending on taxable income, type of business (specified service), the amount of W-2 wages paid by the qualified business, and the unadjusted basis of qualified property held by the business.
- Does not include, investment income, guaranteed payments, wage income, etc.

#3 – Maximizing Tax Deductions – Qualified Business Income Deduction

Specified Service Trade or Business (SSTB):

- Businesses performing services in the field of: health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, investing and investing management, trading, dealing in securities, and any business where the principal asset is the reputation or skill of one or more of its employees or owners.
- Need to have wages or qualified property from the business in order to qualify for the deduction.
- Deduction phases down to zero after certain income thresholds (2024 - \$383,900 Married Filing Joint / \$191,950 for other filers)

#3 – Maximizing Tax Deductions – Qualified Business Income Deduction

REIT/PTP Component:

- Deduction of 20% of the qualified REIT dividends and qualified PTP income.
- Not subject to wage or property limitations.
- Can be limited based on taxable income

#3 – Maximizing Tax Deductions – Qualified Business Income Deduction

Example:

- Taxpayer A owns an S Corporation that reports to A \$100,000 of ordinary qualified business income on A's K-1 for the year. A also received a consolidated 1099 from his broker reporting 199A REIT dividends of \$1,000.
- Assuming these two items are A's sole income, A would be allowed a QBI deduction of \$20,200 (20% of the QBI income and 20% of the 199A dividends). This lowers A's taxable income from \$101,000 to \$80,800.

#3 – Maximizing Tax Deductions – Depreciation

Section 179 Deduction

- For tax years beginning in 2024, the maximum Section 179 expense deduction is \$1,220,000;
- This limit is reduced by the amount by which the cost of Section 179 property placed in service during the tax year exceeds \$3,050,000;
- Property that qualifies:
 - Tangible property (equipment, furniture & fixtures)
 - Vehicles (limitations apply depending on type of vehicle)
 - Qualified real property (qualified improvements, roofs, HVAC, fire protection and alarm systems, and security systems)
- Limited to taxable income

#3 – Maximizing Tax Deductions – Depreciation

Bonus Depreciation

TCJA allowed for the immediate expensing of certain property, but this being slowly phased out:

- 2018-2022 = 100%
- 2023 = 80%
- 2024 = 60%
- 2025 = 40%
- 2026 = 20%
- 2027 = 0%

... #3 – Maximizing Tax Deductions – Depreciation

Bonus Depreciation

Property that qualifies:

- Property with a recovery period of 20 years or less
- This now includes qualified improvement property which was inadvertently left originally:
 - Improvements made to the interior portion of a building which is nonresidential real property if the improvements were placed in service after the date the building was first placed in service
 - Does not include: the enlargement of the building, elevator or escalators, or improvements to the internal structural framework of the building

#3 – Maximizing Tax Deductions – Depreciation

Cost Segregation Studies

- Assists Taxpayer's in allocating the purchase price of a building or total cost of improvements to lesser life assets to take advantage of accelerated depreciation if possible, rather than being all 39-year property.
- Purchase a building for \$500,000 w/out a cost seg study, Taxpayer would have a 39-year asset of \$450,000 plus a non depreciable land asset of \$50,000, providing only \$11,538 of depreciation each year.
- Purchase a building for \$500,000 and have a cost seg study performed that allows for \$100,000 of the purchase price to be allocated to 7-year property, Taxpayer would be able to take a \$100,000 section 179 deduction in year 1 and depreciate the 39-year building \$8,974 per year over 39 years.

#3 – Maximizing Tax Deductions – Cash Method

What Companies Qualify?

- Qualified Personal Service Corporation
 - Substantially all activities of the corporation involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting
 - All stock of the corporation is held directly by employees (active or retired) performing services for such corporation
- Small Business
 - Average annual gross receipts for the 3 taxable year period ending with the taxable year which precedes the current taxable year do not exceed \$30 million

... #3 – Maximizing Tax Deductions – Cash Method

When to Consider a Change

If a Company is on the accrual basis of accounting for tax purposes, but would otherwise qualify for the cash basis method, an analysis should be performed each year (usually as part of year-end tax planning) on the potential benefit to switching to the cash method

#3 – Maximizing Tax Deductions – Cash Method

Example #1

Company A had the following Balance Sheet for 12/31/22 and 12/31/23:

	<u>2022</u>	<u>2023</u>
A/R	100,000	200,000
Prepaid Expenses	10,000	20,000
A/P	75,000	70,000
Accrued Expenses	20,000	30,000

#3 – Maximizing Tax Deductions – Cash Method

Example #1

Upon performing an Accrual to Cash analysis, the Taxpayer would receive the following benefit:

Section 481(a) Adjustment –	(\$15,000)
Accrual to Cash Adjustment –	<u>(\$105,000)</u>
Total Decrease to Taxable Income –	(\$120,000)

#3 – Maximizing Tax Deductions – Cash Method

Example #2

Company A had the following Balance Sheet for 12/31/22 and 12/31/23:

	<u>2022</u>	<u>2023</u>
A/R	200,000	100,000
Prepaid Expenses	20,000	10,000
A/P	70,000	100,000
Accrued Expenses	30,000	20,000

#3 – Maximizing Tax Deductions – Cash Method

Example #2

Upon performing an Accrual to Cash analysis, the Taxpayer would receive the following benefit:

Section 481(a) Adjustment –	(\$120,000)
Accrual to Cash Adjustment –	<u>\$130,000</u>
Total Increase to Taxable Income –	\$10,000

... #3 – Maximizing Tax Deductions – Cash Method

How to Elect?

- Filing Form 3115 with the current year tax return requesting an automatic change of accounting method from accrual to cash

#3 – Maximizing Tax Deductions – Prepaid Expenses

Cash Basis Taxpayers

- Under the cash method of accounting, amounts representing allowable deductions shall, as a general rule, be taken into account for the taxable year in which paid.
- Expenses cannot have a benefit extending past one year.
- Examples: prepaid insurance, prepaid real estate taxes, prepaid maintenance contracts, prepaid professional fees, etc.
- Cash basis Taxpayer's should closely monitor cash toward year end and can help lower tax bill by prepaying expenses if cash is available

#3 – Maximizing Tax Deductions – Prepaid Expenses

Accrual Basis Taxpayers

- Under the accrual method of accounting, the “all events test” must be met in order to take a deduction:
 - All events have occurred that establish the fact of the liability
 - The amount of the liability can be determined with reasonable accuracy
 - Economic performance has occurred
- Payment is considered economic performance for a few items:
 - Insurance contracts
 - Warranty contracts
 - Real estate taxes
 - Worker’s compensation

... #3 – Maximizing Tax Deductions – Profit Sharing

- Profit sharing contributions for a tax year are tax deductible for that tax year as long as the amount is paid by the due date of Taxpayer's return (including extensions).
- If a taxpayer does not have the cash on hand to satisfy the profit-sharing contribution by the time the Taxpayer's return is due in March or April, the Taxpayer, can elect to extend the return and as long as the payment is made by the extended due date in September or October, a deduction is allowed.

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit

What is the R&D Tax Credit?

- The R&D Tax Credit is a government incentive designed to reward companies for investing in innovation;
- The credit was born in 1981 and became a permanent part of the Federal tax code in 2015 due to its success in stimulating job creation and helping to grow the U.S. as an economic leader; and
- The rules for the R&D tax credit can be found in Internal Revenue Code (IRC) Section 41 and related regulations. The credit applies to any taxpayer that incurs expenses for performing Qualified Research Activities (QRAs).

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

What are the Benefits of the R&D Tax Credit?

Some of the potential benefits to realizing the R&D tax credit include:

- Up to 12-16 cents of R&D tax credit for every qualified dollar spent;
- Dollar-for-dollar reduction in federal and (some- not NY) state income tax liability
- Reduction of effective tax rate
- Improved cash flow; and
- Credit carried forward up to 20 years

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

What Companies Qualify?

To qualify for the credit, the Company must meet the following four-part test:

- 1) Elimination of Uncertainty** - The activity is performed to eliminate technical uncertainty about the development or improvement of a product or process, which includes computer software, techniques, formulas and inventions; and
- 2) Process of Experimentation** - The activities include some process of experimentation undertaken to eliminate or resolve a technical uncertainty. This process involves an evaluation of alternative solutions or approaches and is performed through modeling, simulation, systematic trial and error or other methods.

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

What Companies Qualify? (cont'd)

3) Technological in Nature - The process of experimentation relies on the hard sciences, such as engineering, physics, chemistry, biology or computer science; and

4) Permitted Purpose - The purpose of the activity is to create a new or improved product or process (computer software included) that results in increased performance, function, reliability or quality.

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

What are Some Qualifying Activities?

- Developing new or improved products, processes or techniques;
- Developing prototypes or models;
- Development of unique assembly or construction methods and processes

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

What are Some Excluded Activities?

- Research conducted outside the U.S.;
- Adaptation or duplication of existing business components;
- Market research, testing or development (including advertising or promotions);
- Routine data collection;
- Routine or ordinary testing or inspection for quality control;
- Surveys, studies, activity relating to management function, market research or routine testing/quality control;
- Research related to social sciences, arts or humanities; and
- Research funded by any grant, contract or otherwise by another person (or governmental entity).

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

What Expenses Can be Claimed (Qualified Research Expenses)?

- Wages paid to employees working on qualified activities such as engineering, design and/or design/build projects (100% of costs incurred);
- Raw materials and supplies used and consumed in the R&D process (100% of costs incurred);
- Contract research expenses paid to a third party for performing QRAs on behalf of the taxpayer, regardless of the success of the research, allowed at 65% of the actual cost incurred; and
- Basic research payments made to qualified non-profit organizations and institutions. Basic research refers to fundamental research that focuses on evaluating theories and hypotheses, regardless of an application. Basic research payments are included at 75% of the actual expense.

... #4 – Maximizing Tax Credits - Research and Development (R&D) Tax Credit – (cont'd)

2024 & Future Considerations

- IRC 174 required capitalization.
- Newly revised drafts of the R&D tax credit form for 2024 require additional qualitative and quantitative information regarding the company itself and each business component generating the credit to be disclosed. Some questions asked may lead to increased scrutiny and/or audit exposure from the IRS.
- Much of the newly required information should already be contemporaneously documented by businesses.

... #4 – Take Advantage of the Federal Work Opportunity Tax Credit (WOTC)

What is the Work Opportunity Tax Credit?

- The Work Opportunity Tax Credit (WOTC) is a Federal tax credit available to employers who invest in American job seekers who have consistently faced barriers to employment;
- The Consolidated Appropriations Act (CAA) of 2021 extended the WOTC until December 31, 2025; and
- The WOTC is one of the most overlooked credit by businesses.

... #4 – Take Advantage of the Federal Work Opportunity Tax Credit (WOTC) – (cont'd)

How is the WOTC Computed?

- A credit for employers who hire and pay wages to individuals who are certified by a local agency as being a member of one of 10 targeted groups, in their first year or second year of employment, after performing at least 120 hours of service;
- The credit is equal to 40% of up to \$6,000 of qualified wages (\$2,400) or 25% of up to \$6,000 (\$1,500) for individuals who perform fewer than 400 hours but at least 120 hours;
 - For certain qualified veterans, up to \$24,000 in wages may be used (\$9,600 maximum credit); and
 - Wages for the WOTC can't be used to figure other Federal tax credits (i.e., R&D).

... #4 – Take Advantage of the Federal Work Opportunity Tax Credit (WOTC) – (cont'd)

Who Meets the Definition of a Member of a “Targeted Group”?

- Qualified IV-A recipient (Temporary Assistance for Needy Families (TANF));
- Qualified veteran;
- Ex-felon;
- Designated community resident (empowerment zone or renewal county);
- Vocational rehabilitation referral;
- Summer youth employee;
- SNAP recipient (formally the Food Stamps Program);
- SSI recipient;
- Long-term family assistance recipient; and
- Qualified long-term unemployment recipient.

... #4 – Federal Work Opportunity Tax Credit (WOTC) – Steps for Employers

What Are the Steps to Claim the WOTC?

1. All new hires should fill out IRS Form 8850, *Pre-Screening Notice and Certification Request for the Work Opportunity Credit*, page 1, on or before the day the job offer is made;
2. The employer should subsequently fill out page 2 of the form and submit it to the State Workforce Agency (SWA) for the state in which the company is operating. This must be done within 28 days after the eligible worker begins work. See the following link for contacts:
<https://www.dol.gov/agencies/eta/wotc/contact/state-workforce-agencies>;
3. Once certified by the SWA, the employee is considered a **qualified** employee;
4. At year-end, determine the wages of the qualified employees and the number of hours worked for the year; and
5. IRS Form 5884, *Work Opportunity Credit*, should be completed and filed out with the tax return. (Note: The deduction for wages must be reduced by the amount of the credit and recorded as a permanent book-tax difference on IRS Schedule M-1 or IRS Schedule M-3).

... #4 – Federal Work Opportunity Tax Credit (WOTC) – Example

- For the current year, the company hired the following qualified and certified employees:

- Susan –

Qualified Veteran with service-connected disability and unemployed for at least six months in the prior one-year period

\$27,000 & 1,800 hours

Susan

Jim

Dave

	Wages	Hours	Eligible Credit Wages
Susan	27,000	1,800	24,000
Jim	25,000	1,600	6,000
Dave	3,000	200	3,000
	<u>55,000</u>		<u>33,000</u>

- Jim –

Qualified veteran unemployed for at least four weeks, but less than six months in the prior one-year period

\$25,000 & 1,600 hours

25% Category

40% Category

	Eligible Credit Wages	%	Credit Amount
25% Category	3,000	25%	750
40% Category	30,000	40%	12,000
	<u>33,000</u>		<u>12,750</u>

- Dave –

SNAP Recipient

\$3,000 & 200 hours

Total Credit

... #4 – Empowerment Zone Credit

- The Empowerment Zone Employment Credit is a federal tax incentive designed to encourage businesses to operate in economically distressed areas and to hire residents of these areas;
- Businesses can receive a wage credit up to \$3,000 per year for each qualified zone employee;
- The credit is calculated as 20% of the first \$15,000 in wages to each eligible employee each year;
- Full-time & Part-time employees can qualify for the credit.

#4 - Eligibility Requirements – Empowerment Zone Credit

- **Location:** The business must be located within a designated Empowerment Zone. These zones are designated by the Departments of Housing and Urban Development (HUD) and Agriculture (USDA) and include both urban and rural areas.
- **Employee Residence:** The employees for whom the credit is claimed must also reside within the Empowerment Zone.
- **Employment Duration:** Employees must work at least 90 days to be eligible for the credit. The 90-day requirement does not need to be met by the end of the calendar year, it only needs to be met before the credit is claimed on the employer's original or amended return (Wages to employees that are hired in December can still qualify). There are exceptions to this requirement, such as if the employee is terminated due to misconduct or becomes disabled.

... #5 – Take Advantage of the New York State (and other states) Pass-Through Entity Tax Programs (PTET)

- On August 25, 2021, the New York State Department of Taxation and Finance released guidance (Technical Memorandum, TSB-M-21(1)C, (1)I) addressing a recently enacted optional pass-through entity tax (PTET) that partnerships and New York S corporations may elect to pay for tax years beginning on or after January 1, 2021; and
- Entities that elect to be subject to the PTET will pay a graduated tax of up to 10.9% on NYS taxable income at the entity level, while individual partners, members and shareholders will receive a refundable tax credit equal to the pro-rata share of taxes paid by the electing entity.

... #5 - Take Advantage of the New York State (and other states) Pass-Through Entity Tax Programs (PTET)

Tax Rate Schedule:

Tax Rate Schedule	
If the PTE taxable income is:	then the PTET due is:
\$2 million or less	6.85% of PTE taxable income.
greater than \$2 million but less than or equal to \$5 million	\$137,000 plus 9.65% of the excess of PTE taxable income greater than \$2 million.
greater than \$5 million but less than or equal to \$25 million	\$426,500 plus 10.30% of the excess of PTE taxable income greater than \$5 million.
greater than \$25 million	\$2,486,500 plus 10.90% of the excess of PTE taxable income greater than \$25 million.

... #5 - Take Advantage of the New York State (and other states) Pass-Through Entity Tax Programs (PTET)

Why would Taxpayers want to elect to pay a pass-through entity tax?

- The PTET is intended to provide a workaround to the Federal State and Local Tax (SALT) cap that was enacted with the Tax Cuts and Jobs Act (TCJA) of 2017. The TCJA limited deductions for state and local income taxes to \$10,000, thus eliminating the deduction for state income taxes for the vast majority of Taxpayers; and
- The PTET will now effectively allow pass-through entities to claim a Federal income tax deduction for state income taxes, which were previously disallowed (and limited to \$10,000 at the partner/shareholder level).

... #5 - New York State PTET – Who Qualifies?

Eligible partnership: Any partnership (including a limited liability company [LLC], treated as a partnership for Federal income tax purposes) that has a filing requirement under Tax Law §658(c)(1) and is not a publicly traded partnership. A partnership is eligible to make the election, even if it has partners that are not eligible for the PTET credit, including, but not limited to, corporate partners; and

Eligible S corporation: Any New York S corporation (including an LLC treated as an S corporation for New York and federal income tax purposes) as defined by Tax Law §208.1-A that is subject to the fixed dollar minimum tax under Tax Law §209.

... #5 - New York State PTET – Who Does Not Qualify?

C Corporations: Not eligible. Not a pass-through entity and are already allowed to deduct state income taxes at the Federal level;

Important Caveat: While Partnerships and New York S Corporations qualify to make the election, they cannot pass-through the PTET credit to certain partners/members/shareholders. These include:

- S Corporation partners of a partnership;

- C Corporation partners of a partnership; and

- Certain “non-grantor” trusts.

... #5 - New York State PTET – Making the Election

An eligible entity must elect to opt into the PTET online on an annual basis, and such election is irrevocable for the tax year it is made. The election must be made by an authorized person of the organization, which includes any member, partner, owner or other individual with authority to bind the entity and sign tax returns. CPAs are not considered an authorized person and, therefore, cannot make the election on the client's behalf; and

2025 Election and Future Years: Must be made on or before March 15, 2025.

... #5 - New York State PTET – Estimated Tax Payments and Annual Returns

2024 and Future Estimated Tax Payments: Estimated tax payments must be made on a quarterly basis (due March 15, June 15, September 15 and December 15). Each payment should be equal to 25% of the required annual payment for the taxable year, which is the lesser of: (1) 90% of the current year tax; or (2) 100% of the prior year tax;

Annual PTET Returns: Electing entities **must** file an annual PTET return on or before March 15th of the following year. There is a 6-month extension of time, if needed; and

What if my PTET computes to a loss? The electing entity is still required to file a “no balance due” PTET return.

... #5 - New York State PTET – Claiming the Credit

Eligible taxpayers must claim the PTET credit on IRS Form IT-653, *Pass-Through Entity Tax Credit*, and attach the form to the individual New York State income tax return. The PTET credit may not be claimed on group returns filed for nonresident partners (i.e., IRS Form IT-203-GR, *Group Return for Nonresident Partners*) or nonresident shareholders of S corporations (i.e., IRS Form IT-203-S, *Non-Resident and Part-Year Resident Income Tax Return*). **Taxpayers with PTET credits exceeding the tax due for the year may get the excess credit refunded.**

... #5 - NYS PTET – Example – S-Corporations

ABC Corporation has three owners

Federal Taxable income is 1.2 million

Ownership percentages are as follows:

A	40%	
B	35%	
C	25%	
Total	100%	

Step 1.	Net PTET Income		1,200,000	
Step 2.	Net PTET Income		1,200,000	
	Apportionment %		100%	
	PTET Income		1,200,000	
Step 3.	PTET Income		1,200,000	
	Tax		6.85%	
			82,200	
Step 4.		Ownership	Total Credit	Allocated Credit
	A	40%	82,200	32,880
	B	35%	82,200	28,770
	C	25%	82,200	20,550

•Note: The shareholders receive a combined Federal income tax deduction of \$82,200. Assuming they are in the 32% tax bracket, they would recognize Federal income tax savings of approximately \$26,000.

... #5 - Pass-Through Entity Tax – Other State Considerations

New York State is not the only state implementing a pass-through entity level tax to circumvent the SALT cap. There are currently 35 states that are implementing similar taxes; and

Businesses in a multi-state environment, can elect into PTET in multiple states in the same tax year, including:

... #5 - Other States Currently with PTE Taxes

- Alabama – Elective PTE Tax effective 1/1/2021
- Arizona – Elective PTE Tax effective 1/1/2022
- Arkansas – Elective PTE Tax effective 1/1/2022
- California – Elective PTE Tax effective 1/1/2021
- Colorado – Elective PTE Tax effective 1/1/2022
- Connecticut – Mandatory PTE Tax effective 1/1/2018, Elective starting 2024
- Georgia – Elective PTE Tax effective 1/1/2022
- Hawaii – Elective PTE Tax effective 1/1/2023
- Idaho – Elective PTE Tax effective 1/1/2021
- Illinois – Elective PTE Tax effective 1/1/2021
- Indiana – Elective PTE Tax effective 1/1/2022

... #5 - Other States Currently with PTE Taxes

- Iowa – Elective PTE Tax effective 1/1/2022
- Kansas – Elective PTE Tax effective 1/1/2022
- Kentucky – Elective PTE Tax effective 1/1/2022
- Louisiana – Elective PTE Tax effective 1/1/2019
- Maryland – Elective PTE Tax effective 1/1/2020
- Massachusetts – Elective PTE Tax effective 1/1/2021
- Michigan – Elective PTE Tax effective 1/1/2021
- Minnesota – Elective PTE Tax effective 1/1/2021
- Mississippi – Elective PTE Tax effective 1/1/2022
- Missouri – Elective PTE Tax effective 1/1/2022
- Montana – Elective PTE Tax effective 1/1/2023
- Nebraska – Elective PTE Tax effective 1/1/2018

... #5 - Other States Currently with PTE Taxes

- New Jersey – Elective PTE Tax effective 1/1/2020
- New Mexico – Elective PTE Tax effective 1/1/2022
- North Carolina – Elective PTE Tax effective 1/1/2022
- Ohio – Elective PTE Tax effective 1/1/2022
- Oklahoma – Elective PTE Tax effective 1/1/2019
- Oregon – Elective PTE Tax effective 1/1/2021
- Rhode Island – Elective PTE Tax effective 1/1/2019
- South Carolina – Elective PTE Tax effective 1/1/2020
- Utah – Elective PTE Tax effective 1/1/2022
- Virginia – Elective PTE Tax effective 1/1/2021
- West Virginia – Elective PTE Tax effective 1/1/2022
- Wisconsin – Elective PTE Tax effective 1/1/2019

Questions



Dannible & McKee Annual Tax & Financial Planning Conference

- **Date:** November 6, 2024, 11:30 am - 6:30 pm
- **Location:** DoubleTree by Hilton Hotel Syracuse / 6301 NY-298, East Syracuse, NY
- **Schedule:**
 - Registration and Networking: 11:30 a.m.
 - Lunch: 12:00 p.m.
 - Program: 12:30 p.m. – 5:00 p.m.
 - Cocktail Networking Reception: 5:00 p.m. – 6:30 p.m.
- **Registration:** <https://www.dmcpas.com/events/annual-tax-financial-planning-conference/>



Brian J. Potter, CPA, CDA
Tax Partner
bpotter@dmcpas.com



Anthony Pokrentowski, CPA
Senior Tax Manager
apokrentowski@dmcpas.com

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