# 2023 Year-End Tax Seminar

November 16, 2023

Kreischer Miller

# Today's Presenters

**Andrew Berger**
Director,
Tax Strategies

**Reed Brown**
Manager,
State and Local Tax

**Carlo Ferri**
Director,
Tax Strategies

**Tom Frascella**
Director,
State & Local Tax

**Brian Kitchen**
Director,
Tax Strategies

**Rich Nelson**
Director,
Tax Strategies

**Lisa Pileggi**
Director-in-Charge,
Tax Strategies

**Brad Runyen**
Director,
Tax Strategies

**Katrina Samarin**
Director,
Tax Strategies

**Kate Stewart**
Director,
Tax Strategies

# ESOPs as a Tax-Efficient Exit Strategy

November 16, 2023

Katrina Samarin, Director, Tax Strategies
Andrew Berger, Director, Tax Strategies

Kreischer Miller

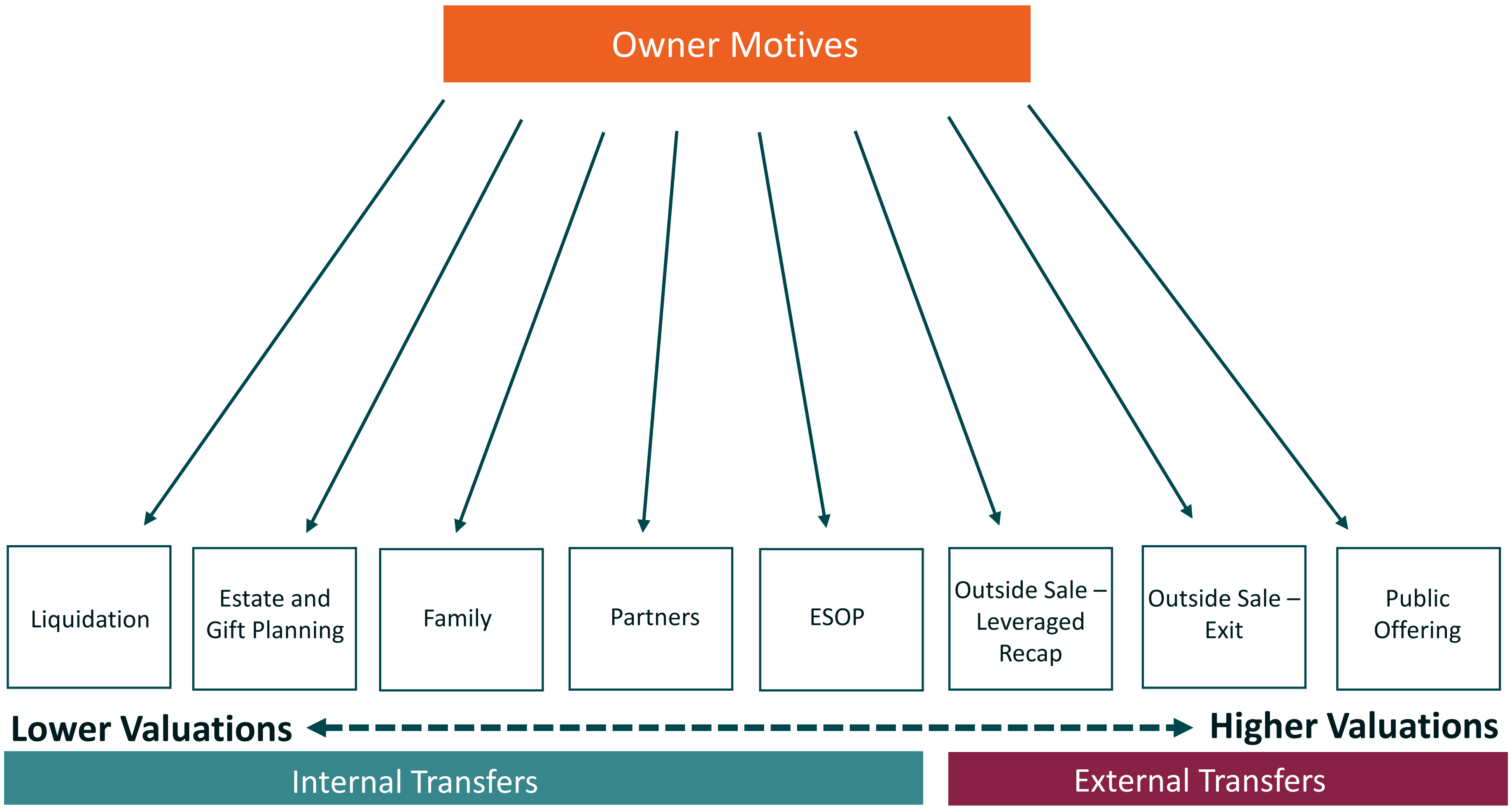
# Agenda

1. What is an ESOP?
2. ESOP Tax benefits
3. ESOP Non-tax benefits
4. Advantages and disadvantages of ESOPS
5. Key takeaways

# Disclaimer

This material is provided for general informational and educational purposes only and should not be construed as legal or tax advice. You should not rely on information contained in this presentation to make business or tax decisions without first consulting with your tax advisor. The information contained in this material is subject to change without notice. The presenters undertake no obligation to update this material.

# Business Transfer Spectrum



# What is an ESOP?

- ESOP is an Employee Stock Ownership Plan
- Defined contribution employee benefit plan
- Invests primarily in stock of employer
- Assets reside in an Employee Stock Ownership Trust (ESOT)
- Employees don’t actually own stock – ESOT owns actual shares and employees are beneficial owners
- Annual valuation requirement
- Tax advantages for the selling shareholder and company

# ESOP Owner Profile

- Emotional attachment to the business they built
- Family members not present or capable to take over business
- Worried about 3rd party “damage” if they sell outright
- Owner has multiple transfer motives
  - Money
  - Legacy
  - People
  - Community
  - Control / Timing
  - Tax Efficiency **[Caution]**
- Identify an ESOP as the best transfer channel based available based on the business and other available options

# ESOP Company Profile

- ESOPs are not for everyone!
- Non-cyclical slow to medium growth company
- Consistent & reasonably stable profits and cash flow
- Owners interested in remaining involved/participating in the business
- Competent executive team with potential successors identified
- Seller has long-time horizon – not seeking full up front cash payment
- Lack of strategic buyers willing to pay significant premium for the company

# Leveraged ESOP

# Tax Benefits (to Company)

- S Corporations owned by an ESOP are tax-free for federal and most state tax purposes
- Increased cash flow to make further investments in Company
- Less uncertainty in a changing or uncertain tax environment
- C Corporations can deduct dividends paid on ESOP Shares to reduce taxable income
- Companies deduct contributions to the ESOP to reduce taxable income
- Employees pay no tax on the contributions to the ESOP, only distributions from the ESOP

# Section 1042 – A Significant Tax Benefit to Selling Shareholders

- Allows a selling shareholder a deferral of the capital gains tax on the sale of their stock to an ESOP if:
    - The Company is a **C Corporation** at the time of the sale; **AND**
    - The ESOP owns at least 30% of the Company’s stock post-transaction; **AND**
    - The selling shareholders reinvest the proceeds in “Qualified Replacement Property” within 12 months following the transaction or 3 months prior
- What is Qualified Replacement Property ("QRP")?
    - Stocks and bonds of U.S. corporations, public or private, that derive no more than 25% of their gross income from passive sources
        - Floating rate notes
        - NOT mutual funds
        - NOT government bonds

# Section 1042 – A Significant Tax Benefit to Selling Shareholders (cont.)

- Advantages
  - Allows a selling shareholder to defer the gain on the sale of their company's stock
  - Assets work as a very tax efficient part of a seller's estate
  - Tax deferred assets provide a greater degree of optionality
- Disadvantages
  - The entity CANNOT be an S Corporation (100% tax free). Instead, the company needs to operate as a C Corporation for 5 years before electing S status
  - Selling shareholder cannot receive an allocation of shares and patriciate in the ESOP
  - Seller is may be limited on the stocks that they can invest in
  - Transaction creates some additional administrative costs
- Note, some of the disadvantages listed above may be mitigated through the use of a floating rate note
- The Secure Act 2.0 expanded the use of section 1042. Effective for transactions occurring after December 31, 2027, **S Corporation** shareholders who sell their stock to an ESOP will be able to defer 10% of the gain

# Benefits to the Shareholder

- A significant amount of flexibility with timing/control
- May provide an opportunity to defer tax on the sale of their company (NOT ALWAYS!)
- Opportunity to monetize and diversify assets
- Receive shares back via the annual share allocation and is typically the highest compensated individual
- Opportunity to achieve closer to strategic value if sold in tranches
- Don't have to worry about what happens to the company and its employees after it’s sold
- Don’t have to worry about cultural clash
- Don’t have to worry about vision being misaligned
- Provides you the opportunity to preserve corporate legacy

# Benefits to the Company

- National Center for Employee Ownership ("NCEO") tracks benefits of ESOPS and published various findings:
  - Better corporate performance – ESOP companies grew 2.5% per year faster in sales, employment and productivity after their ESOP was setup vs. expectations pre-ESOP
  - Longer business life and less likely to lay people off in a recession – ESOP companies were only half as likely as non-ESOP firms to go bankrupt or close
- During the COVID-19 Pandemic, a Rutgers study found that ESOP companies were 3-4x likely to retain staff
- Company can increase cash flow due to tax-free status
- Significant recruitment and retention tool

# Benefits to the Employee

- Provides the employee base with direct ownership in the company to align their interest with the company's success
- Better pay and benefits – NCEO found that employee-owners earned 5 – 12% more than median wages compared to employees in similar non-ESOP companies, 2.5 times more in retirement savings and 20% more in financial assets overall
- Provide greater opportunity for young workers – a recent survey that compared people ages 28 to 35 with ESOP benefits to their peers without found that those ESOP employees enjoyed 92% higher median household wealth, 33% higher income from wages and 53% longer median job tenure
- Provides significant tax savings to the employee via tax deferred compensation
- Fosters a more productive and connected work environment

# Ongoing Administration of an ESOP Owned Company

- How are shares generally allocated to employee accounts?
- How do employees receive payout? (retirement, separation, etc.)
- Employees need to be trained to think like owners and be engaged in the decision making and management process
- The company will need to manage the ESOP and the "sea of advisors" that results from the transaction
- Ongoing communication and promotion of the ESOP is necessary

# Is an ESOP a Good Fit for Your Company?

- Can reasonably anticipate cash flows and revenues
- Company should be in business for several years
- EBIDTA target greater than $1M
- Have greater then 25 employees
- Has to be a C or S Corp
- Sufficient collateral for debt
- Strong successor management team

# Advantages of an ESOP

| Seller | Company | Employees |
| --- | --- | --- |
| • Receive fair market value<br>• Flexible exit strategy<br>• Beneficial tax treatment<br>• Preserve legacy of company | • Tax advantaged financing<br>• Potential for tax free corporate profits<br>• Potential to enhance employee morale, increase productivity and reduce turnover | • Non-contributory retirement account<br>• Incentive for employees<br>• Ability to impact value of company and therefore, value of accounts |

# Disadvantages of an ESOP

**Seller**

- Seller gets price closer to a financial buyer rather than a strategic buyer
- Seller typically does not fully cash out
- Requires active role in training employees to be owners

**Company**

- Complexity
- Financial leverage is usually high
- Repurchase obligation
- Highly regulated
- Ongoing administration
- Employee group may lack buy-in

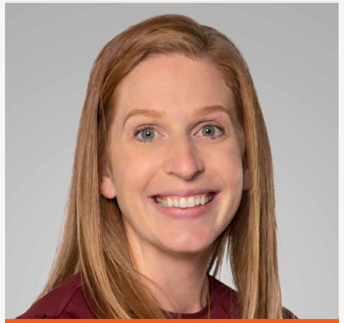
**Employees**

- Non-diversified retirement plan risk
- May not have 100% liquidity upon exit
- Employee base may not see the value that they're receiving

# 3 Key Takeaways

- Is your company and owner a good fit?
- There are significant tax advantages unique to ESOPs
- Ongoing operations and administration

# Contact the Presenter




## Katrina R. Samarin, CPA, MT

DIRECTOR, TAX STRATEGIES

ksamarin@kmco.com


Katrina is a Director in Kreischer Miller's Tax Strategies group. Katrina serves as a proactive and responsive tax advisor to her clients' needs including tax compliance, tax planning, and tax research for corporations, partnerships, trusts, and high-net-worth individuals. She is forward-looking to keep her clients compliant and well informed on the changing tax landscape.

Katrina works with a broad range of privately-held businesses including those in the manufacturing, distribution, real estate, and service industries.

# Contact the Presenter


## Andrew R. Berger, CPA

DIRECTOR, TAX STRATEGIES

aberger@kmco.com


Andrew is a Director in Kreischer Miller's Tax Strategies group. Andrew provides a variety of practical tax strategies & services including tax compliance, tax planning and tax research for corporations, multi-state companies, partnerships, trusts and high-net-worth individuals.

Andrew has a diversified range of experience providing tax services to companies in the real estate, distribution, manufacturing and professional services industries.

# Congressional and IRS Update

November 16, 2023

Richard Nelson, Director, Tax Strategies

Kreischer Miller

# Agenda

1. Congressional Update
2. Internal Revenue Service Update

# Disclaimer

This material is provided for general informational and educational purposes only and should not be construed as legal or tax advice. You should not rely on information contained in this presentation to make business or tax decisions without first consulting with your tax advisor. The information contained in this material is subject to change without notice. The presenters undertake no obligation to update this material.

# Congressional Tax Update

It's November 16th –

Where are we?

Is tax even on their minds?

# Congressional Tax Update

## Government Priorities Remaining for 2023

| Legislative Action | Deadline |
| --- | --- |
| Government Funding (appropriations) | November 17, 2023 |
| FAA reauthorization | December 31, 2023 |
| Medicare physician payments | December 31, 2023 |

# Congressional Tax Update

Tax doesn’t appear to be a priority. At best a second-tier priority.

Let's reflect on 2022.

Is 2023 different?

# 2022

- Businesses were concerned with three major issues:
  1) The capitalization of Research and Development expenses
  2) The exclusion of depreciation and amortization as an add back to income in calculating the limitation
  3) The winding down of bonus depreciation
- We were all optimistic
- The Republicans and the Democrats all agreed they wanted to eliminate these provisions retroactively
- Apparent holdup – Democrats looking for an increase in the child tax credit and the earned income tax credit

# 2023

- Everything is the same as 2022 except there was a Republican proposal in June.
- Three bills rolled into the American Families and Jobs Act.

# American Families and Jobs Act

- Retroactively restore 100% expensing for investments in equipment
- Retroactively restore the 100% expensing of research and development (R&D) costs
- Retroactively restore the addbacks for the limitation on interest expense (Section 163(j))
- All three would be extended through the end of 2025
- Other Provisions:
    1) Increase the standard deduction for individuals through 2025
    2) Permanently increase the Section 179 expensing

# American Families and Jobs Act

- To raise additional revenue, the bill would cut back on the Inflation Reduction Act's green energy credits, including repeal or modification of the clean energy production credit, the clean electricity investment credit, the previously owned clean vehicles credit, the clean vehicle credit, and the qualified commercial clean vehicle credit the standard deduction for individuals through 2025.

# Chances of Being Enacted

What’s missing?

- No increase to the Child Tax Credit
- No increase to the Earned Income Tax Credit

Eliminate?

- Energy Credits

# Is There Hope?

# IRS Update

- First wave of hiring focused on taxpayer service positions to help improve phone and in-person assistance.
- The next wave of hiring will help the IRS add key talent like tax accountants to help reverse a decade-long decline of audits for the wealthy as well as complex partnerships and corporations.
- Focus will be on higher-income and complex tax areas like partnerships, not average taxpayers making less than $400,000.

# IRS Update

- The Internal Revenue Service announced the opening of more than 3,700 positions nationwide in more than 250 locations.
- Effort to expand tax enforcement involving areas of concern with high-income earners, partnerships, large corporations and promoters.
- The hiring will be for higher-graded revenue agents, which are specialized technical positions that generally focus on audits.
- Interested in individuals in the financial services industry – such as tax accountants, forensic accountants' auditors, controllers and treasurers.
- This is an exciting time to be at the IRS," said IRS Human Capital Officer Traci DiMartini. "The IRS provides a competitive financial package for people with expertise in this high-demand area. For people with accounting and financial backgrounds, we encourage them to take a close look at the benefits of working for the IRS and serving our nation."

# IRS Update

- The IRS began focusing on examinations of the largest and most complex partnership returns through its Large Partnership Compliance pilot program launched in 2021.
- They plan to expand the program to additional large partnerships, using AI to select returns for examination.
- On September 8th, the IRS stated that it plans, by the end of the month, to have opened examinations of 75 of the largest partnership in the U.S. in a cross section of industries – including hedge funds, real estate investment partnerships, publicly traded partnerships, and large law firms.

# IRS Update

- New Centralized Partnership Audit Rules enacted in 2015.
- Increased focus on partnership compliance including Schedules K-1, K-2 and K-3.
- IRS has identified ongoing discrepancies in balance sheets of partnerships with over $10 million in assets. Discrepancies in balances between the end of one year and the beginning of the next year – many in the millions of dollars, without any required attached statement explaining the discrepancy.

# IRS Update

- Using its new resources, the IRS plans to mail out compliance letters to around 500 partnerships starting in early October. Depending on the partnerships' responses, the IRS might take additional action, including potential examination.
- What can you do?

# Employee Retention Credit

Credit for Wages paid in 2020 and 2021

Qualifying Tests:

- Quantitative based upon a significant decline in gross receipts.
  - In 2020 50% reduction in revenue compared to same quarter in 2019.
  - In 2021 20% reduction in revenue compared to same quarter in 2019

or

- Sustained a full or partial suspension of operations due to a governmental ordered shutdown.

# Employee Retention Credit

- Urge people to review guidelines before trying to claim the credit.
- Credit promoters on the radio and online continue to push ineligible people to file.
- The IRS has been issuing warnings about aggressive ERC scams since last year, and it made the agency's list this year of the Dirty Dozen tax scams that people should watch out for.

# Employee Retention Credit

- Previously extended the statute of limitations from three years to five years.
- Announced an immediate moratorium through at least the end of the year on processing new claims for the pandemic-era relief program.
- On July 26, the agency announced it was shifting its focus to review these claims for compliance concerns, including intensifying audit work and criminal investigations on promoters and businesses filing dubious claims.
- On September 14th the IRS announced that hundreds of criminal cases are being worked, and thousands of ERC claims have been referred for audit.

# Employee Retention Credit

IRS issued guidance on withdrawing a claim

Different steps depending on where you are in the process:

- You haven’t received a refund and haven’t been notified your claim is under audit.
- You haven’t received a refund and you’ve been notified your claim is under audit.
- You received a refund check but haven’t cashed or deposited it.
- Still working on guidance if you cashed the check but want to return it.

# Employee Retention Credit

The credit is a good thing if you qualify. There is still time to apply for the credit.

- For 2020 can file amended payroll tax returns until April 15, 2024
- For 2021 can file amended payroll tax returns until April 15, 2025

Important: if you amend your payroll tax returns, you must go back and amend your business return and your personal return if a pass-through entity. Your payroll deduction is reduced by the amount of the credit thereby increasing your taxable income.

# IRS Dirty Dozen

**Employee Retention Credit claims**

Taxpayers should be aware of aggressive pitches from scammers who promote large refunds related to the Employee Retention Credit (ERC). The warning follows blatant attempts by promoters to con ineligible people to claim the credit. The IRS highlighted these schemes from promoters who have been blasting ads on radio and the internet touting refunds involving Employee Retention Credits. These promotions can be based on inaccurate information related to eligibility for and computation of the credit. Additionally, some of these advertisements exist solely to collect the taxpayer's personally identifiable information in exchange for false promises. The scammers then use the information to conduct identity theft.

**Phishing and smishing**

Unsolicited texts and emails from the IRS and states asking for personal and financial information that can lead to identity theft. The IRS initiates most contacts through regular mail and will never initiate contact with taxpayers by email, text or social media regarding a bill or tax refund.

# IRS Dirty Dozen

**Online account help from third-party scammers**

Swindlers pose as a "helpful" third party and offer to help create a taxpayer's IRS Online Account at IRS.gov. In reality, no help is needed. The online account provides taxpayers with valuable tax information. But third parties making these offers will try to steal a taxpayer's personal information this way. Taxpayers can and should establish their own online account through IRS.gov.

**Unscrupulous tax return preparers**

People should be careful of shady tax professionals and watch for common warning signs, including charging a fee based on the size of the refund. A major red flag or bad sign is when the tax preparer is unwilling to sign the dotted line. Avoid these "ghost" preparers, who will prepare a tax return but refuse to sign or include their IRS Preparer Tax Identification Number (PTIN) as required by law. Taxpayers should never sign a blank or incomplete return.

# IRS Dirty Dozen

**Offer in Compromise mills**

Offers in Compromise are an important program to help people who can't pay to settle their federal tax debts. But "mills" can aggressively promote Offers in Compromise in misleading ways to people who clearly don't meet the qualifications, frequently costing taxpayers thousands of dollars. A taxpayer can check their eligibility for free using the IRS Offer in Compromise Pre-Qualifier tool.

**Micro-captive insurance arrangements**

A micro-captive is an insurance company whose owners elect to be taxed on the captive's investment income only. Abusive micro-captives involve schemes that lack many of the attributes of legitimate insurance. These structures often include implausible risks, failure to match genuine business needs and, in many cases, unnecessary duplication of the taxpayer's commercial coverages.

**Syndicated conservation easements**

A conservation easement is a restriction on the use of real property. Generally, taxpayers may claim a charitable contribution deduction for the fair market value of a conservation easement transferred to a charity if the transfer meets the requirements of Internal Revenue Code 170. In abusive arrangements, which generate high fees for promoters, participants attempt to game the tax system with grossly inflated tax deductions.

# IRS Dirty Dozen

**Offshore accounts and digital assets**

The IRS continues to scrutinize attempts to hide assets in offshore accounts and accounts holding digital assets, such as cryptocurrency. The IRS continues to identify individuals who attempt to conceal income in offshore banks, brokerage accounts, digital asset accounts and nominee entities. Asset protection professionals and unscrupulous promoters continue to lure U.S. persons into placing their assets in offshore accounts and structures saying they are out of reach of the IRS. These assertions are not true. The IRS can identify and track anonymous transactions of foreign financial accounts as well as digital assets.

**Maltese individual retirement arrangements misusing treaty**

These arrangements involve U.S. citizens or residents who attempt to avoid U.S. tax by contributing to foreign individual retirement arrangements in Malta (or potentially other host countries). The participants in these transactions typically lack any local connection to the host country. By improperly asserting the foreign arrangement as a "pension fund" for U.S. tax treaty purposes, the U.S. taxpayer misconstrues the relevant treaty provisions and improperly claims an exemption from U.S. income tax on gains and earnings in and distributions from the foreign individual retirement arrangement.

# IRS Dirty Dozen

**Puerto Rican and foreign captive insurance**

U.S. business owners of closely held entities participate in a purported insurance arrangement with a Puerto Rican or other foreign corporation in which the U.S. business owner has a financial interest. The U.S. business owner (or a related entity) claims a deduction for amounts paid as premiums for "insurance coverage" provided by a fronting carrier, which reinsures the "coverage" with the Puerto Rican or other foreign corporation. Despite being labeled as insurance, these arrangements lack many of the attributes of legitimate insurance.

# IRS Dirty Dozen

Where appropriate, the IRS will challenge the purported tax benefits from these types of transactions and impose penalties. The IRS Criminal Investigation Division is always on the lookout for promoters and participants of these types of schemes. Taxpayers should think twice before including questionable arrangements like this on their tax returns. After all, taxpayers are legally responsible for what's on their return, not a promoter making promises and charging high fees. Taxpayers can help stop these arrangements by relying on reputable tax professionals they know and trust.

# Contact the Presenter


## Richard J. Nelson, CPA

DIRECTOR, TAX STRATEGIES

rnelson@kmco.com


Rich is a Director in Kreischer Miller's Tax Strategies group. He has extensive experience providing domestic and international tax strategies, planning and services to a variety of middle market companies and entrepreneurial businesses in a number of industries including manufacturing, distribution, real estate, financial, and professional services.

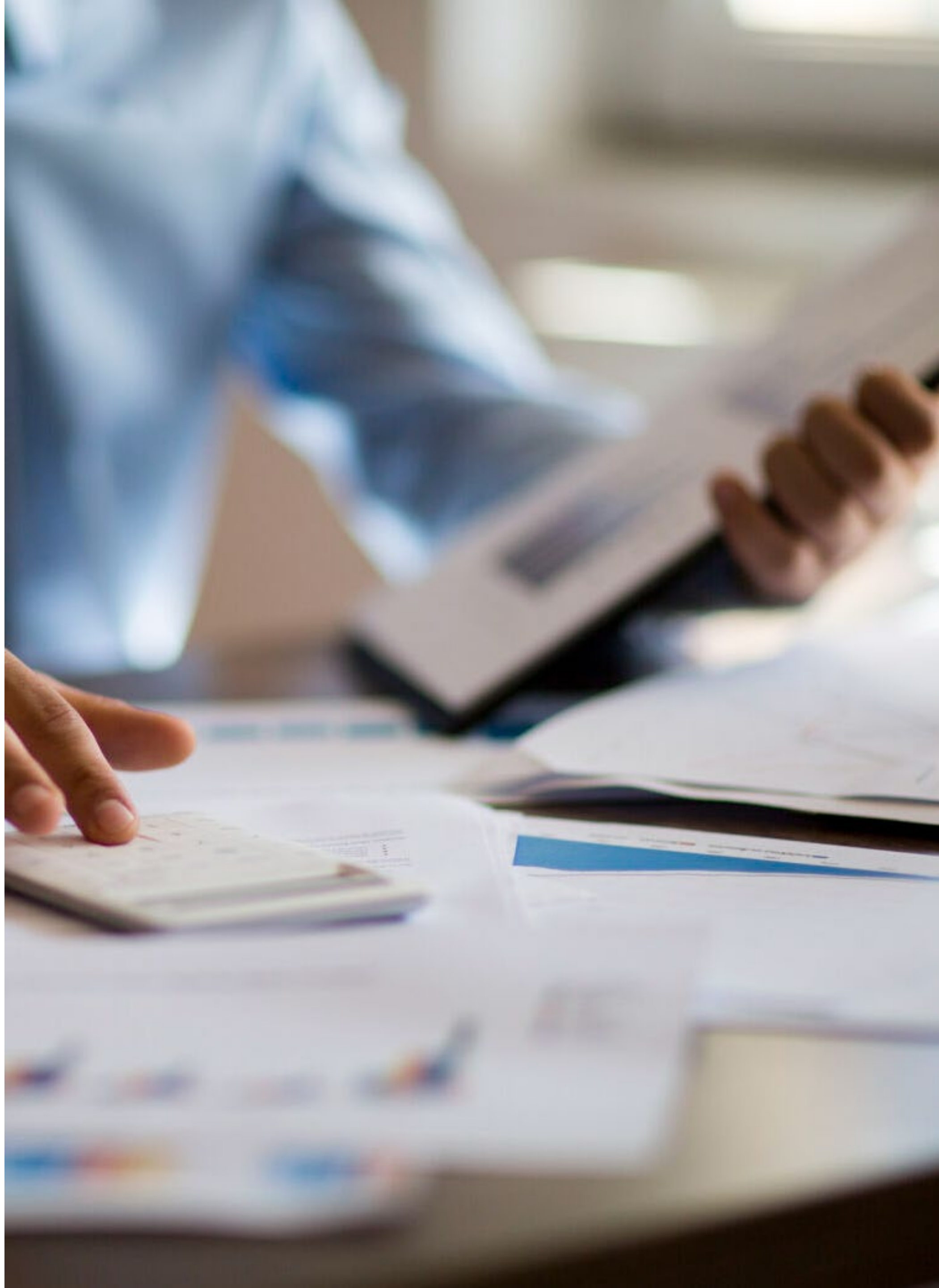
Rich has significant experience and expertise with high-net-worth individuals, investment companies and pass-through entities and has been involved in federal, state, and local tax audits, settlements, and appeals.

# State and Local Tax Highlights

November 16, 2023

Tom Frascella, Director, Tax Strategies, State and Local Tax Group Leader
Reed Brown, Manager, State and Local Tax

Kreischer Miller



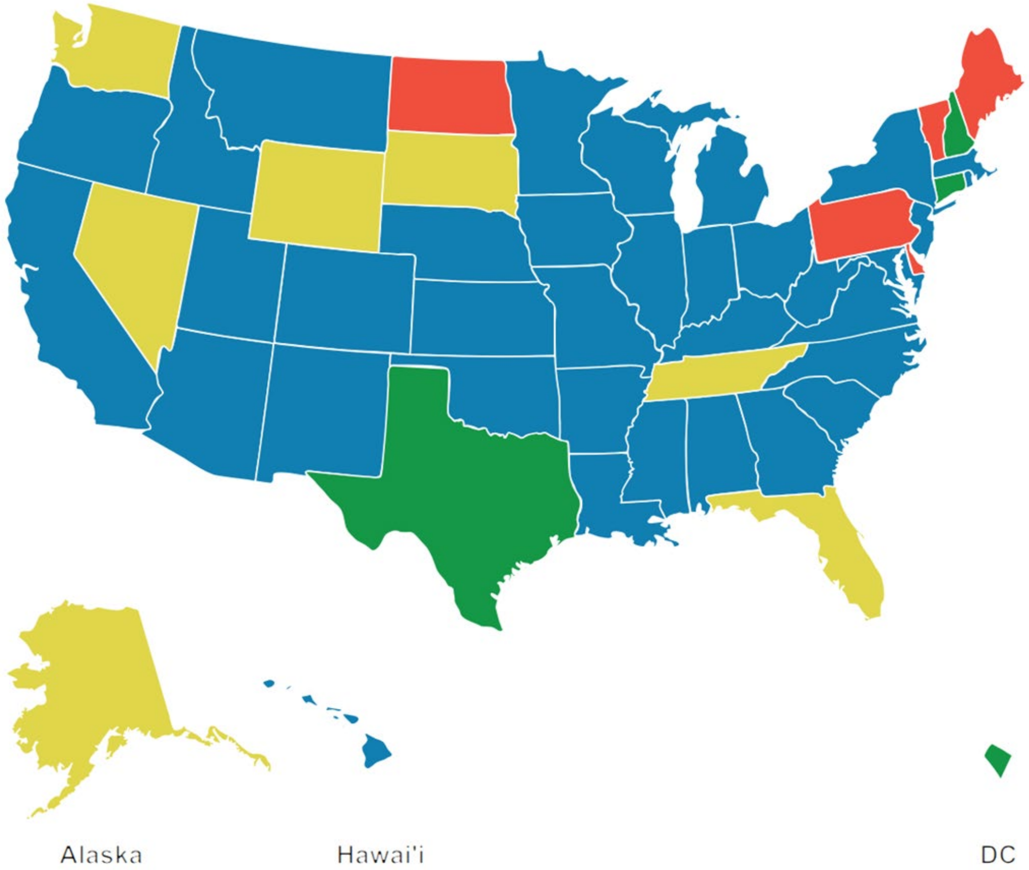
# Agenda

1. Introduction
2. State of the States – Overview of State and Local Taxes
3. Public Law 86-272 vs. Multi-State Tax Commission
4. Mergers and Acquisition Planning
5. Pennsylvania and New Jersey Budget and Tax Changes

# State of the States – Pass-Through Entity

- Tax Cuts and Jobs Act of 2017 (TCJA) changed tax landscape for owners of pass-through entities
- $10,000 cap on state and local tax deduction for individual taxpayers caused states to respond with the enactment of pass-through entity level taxes
- Shifts tax liability away from the individual to the entity
- Taxes paid under these elections are deductible at the federal level
- As of August 2023, 36 states have enacted PTE tax elections
- Are all state elections the same? Definitely not!

# State of the States – Pass-Through Entity




PTE Election allowed or elective

PTE Level Filing Mandatory

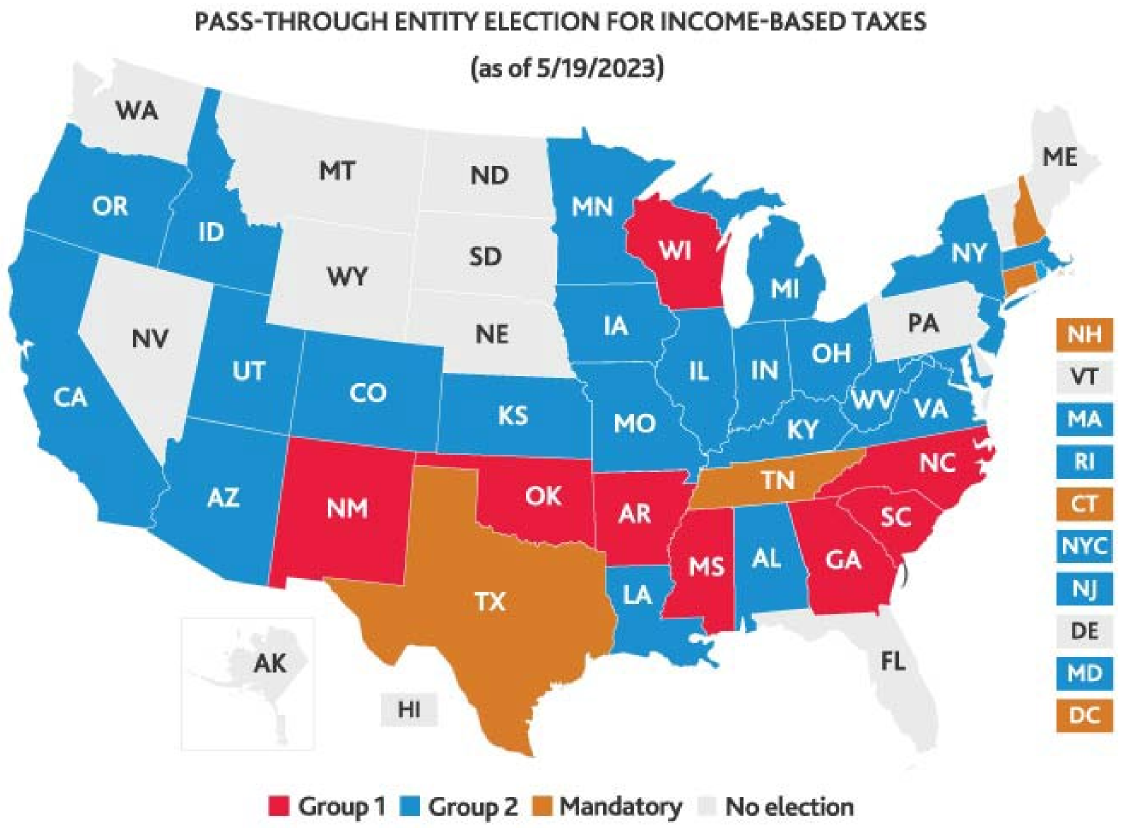
Does not impose individual income tax

PTE Election not allowed

# State of the States – Pass-Through Entity

- States have generally approached the creation of PTE tax in one of two ways:
  - Group 1: Allows members of a PTE to reduce adjusted gross income by their pro rata or distributive shares of income
  - Group 2: Allows members to take a credit to offset their taxable income but still requires members to include their distributive shares of income in their returns
- Issues and Concerns with Elections
  - Timing and due dates of elections
  - Tax rates specific to PTE election vs individual filing
  - Compliance requirements – is there still a return requirement at individual level? IT DEPENDS

# State of the States – Pass-Through Entity



# State of the States – Sales and Use Tax

- Have you heard of the Wayfair Decision?!
- Do you know what you're selling?
  - Services? Goods?
- How are you selling? Direct to customers? Through Marketplaces?
  - How are you billing?
- It Matters!
- New York Board of Tax Appeals - The Matter of Petition of Beeline.com, Inc.
  - Beeline.com charged vendors a fee for its vendor management system (VMS) that matched customers needing temporary workers with suppliers of temporary labor
  - Included in this charge were a number nontaxable services **bundled** with charges to access software-as-a-service (considered taxable in NY)
  - Primary function test, AKA "true object" test challenged
  - Devil was in the details! Customer service agreement and marketing details ultimately used to rule in favor of NY Department of Taxation and Finance

# State of the States – Sales and Use Tax

- Increase in remote seller audits
  - States have reduced personal and corporate income tax rates – where will the tax revenue come from?
  - Expanding tax base – digital goods and services are being pulled into the tax base
- Drop-shipping – the new administrative headache!
  - Have you received valid exemption certificates from your customers?
  - Are you able to provide a valid exemption certificate to your suppliers?

# State of the States – Sales and Use Tax

- Exemption Certificate Management
    - Timely acceptance?
    - Properly completed?
    - Applicable to transaction?
    - Accepted in Good Faith?

# State of the States – Sales and Use Tax

- Rhode Island Administrative Hearing Decision, Division of Taxation Example
    - Taxpayer originally charged applicable sales tax on a transaction that occurred in August 2016 and timely submitted the tax
    - Customer later provided a resale certificate in December of 2016
    - Taxpayer provided a credit to the customer and then took a credit on their sales tax return
        - Rhode Island taxation reviewed the return, and issued a notice that the taxpayer owed sales tax, interest and negligence penalties
    - Rhode Island is a Streamlined Sales and Use tax Agreement member(SSUTA) which allows 90 days from a transaction to obtain a resale certificate in order to be considered timely and valid
    - Rhode Island also has legislation that allows a taxpayer 120 days from **<u>the date of a request</u>** from the Division of Taxation to produce support for an exempt sale
    - Hearing officer denied the resale certificate accepted in December of 2016 as it was within 107 days of the 90 day window AND denied the resale certificate under the 120 day window since there was not an original request from the state!

# State of the States – Corporate Income Tax

- Shift in reduction of corporate tax rates
    - Since 2021, 20 states have reduced their corporate income/personal income taxes
- Shifts in corporate income tax create adjustments and changes for other taxes

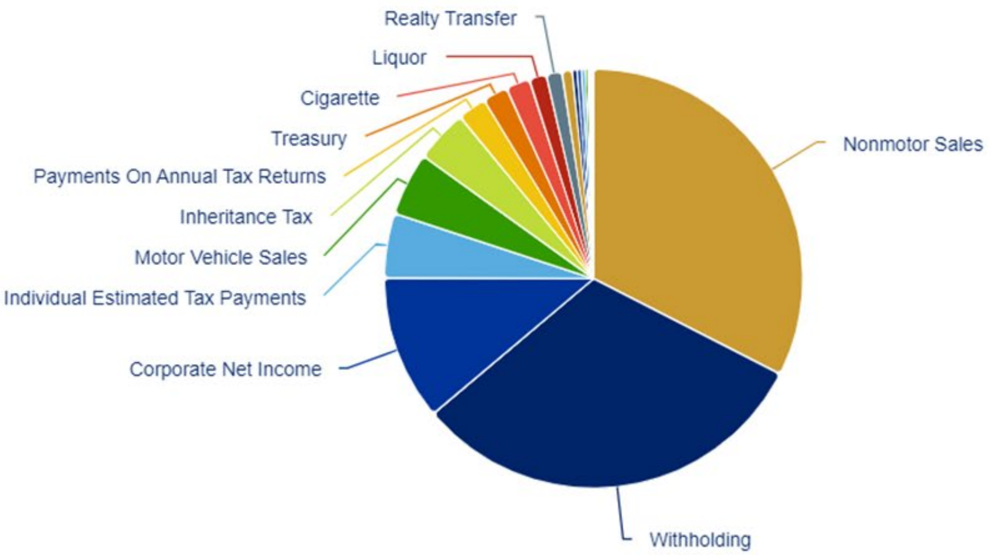
# State of the States – Budget Example

## General Fund Current Fiscal Year Enacted Budget

Total:**$13,085,469,422** | Fiscal Year:**2023**

### Collected Revenue Classifications

Click Within the Chart to Drilldown or Use Dropdown Selector




| Category Description |
|---|
| Realty Transfer |
| Gaming |
| Other Tobacco Products Tax |
| Other Miscellaneous |
| Licenses and Fees |
| Fines, Penalties and Interest Total |
| Financial Institutions |
| Gross Receipts |
| Insurance Premium |
| Malt Beverage |

| | |
|---|---|
| NonMotor Sales | 33.69% |
| Withholding | 32.69% |
| Corporate Income | 11.65% |
| Motor Vehicles | 5.149% |
| Inheritance | 4.255% |

# Income Tax Nexus and MTC Statement on P.L. 86-272

- Has protected interstate commerce from net income tax obligations in customer's states since 1959
    - ONLY APPLIES TO THE SALE OF TANGIBLE PERSONAL PROPERTY
    - However, the standard is quickly being eroded through efforts like the MTC
    - State sovereignty will quickly become the next battleground through the expansion of the Wayfair decision to other taxes
- MTC Updated Statement Issued August 2021 expanding scope of "unprotected activity"
    - Focus is on internet activities
    - Providing post sale assistance through chat or email through the website
    - Solicitation or receiving online credit card applications
    - Placing cookies used for product development/product management on electronic devices of customers
    - Allowing candidates to apply for job openings online

# Income Tax Nexus and MTC Statement on P.L. 86-272 (cont.)

- MTC Updated Statement Issued August 2021
  - Previously only considered an interpretation and “guidance” is now being introduced into tax regulations by state taxing authorities
    - CA and NJ have adopted provisions from the guidance into their updated tax regulations
    - NY and OR have noted they are working on adopting provisions but have not issued updates to date
- What does this mean for the P.L. 86-272 position and historical filings?
  - Buckle up. It is going to be a bumpy ride

# Mergers and Acquisition
# Issues and Pitfalls

- State of the economy has buyers focusing on due diligence processes and areas of potential exposure
- Federal considerations and deal structure typically take precedent and priority during the planning process
- State and local considerations often overlooked in the beginning of the process and are not considered until an issue is discovered or question is asked during due diligence
- What can be done to prevent or plan for state and local tax exposures
- Timing, Timing, Timing
    - Proactive and preemptive prevents reactive
    - State and local tax review
    - Taxability determination
    - Exemption certificate review
    - Sourcing determination

# Pennsylvania Tax Changes & Updates

**Proposed Legislation**

- Senate Bill 345
    - Proposes to accelerate the reduction of Corporate Net Income (CNI) by immediately dropping to 7.99% and then reducing it additional point every January until 4.99%
    - Original plan of reducing tax rate over nine years was passed as part of 2022-2023 budget
- Senate Bill 346
    - Proposes to gradually increase Net Operating Loss(NOL) Carryover limit from current 40% to 80% over four years
    - Brings PA in line with federal limitation and other 48 states
    - Would make PA more competitive for start ups and new businesses

# Pennsylvania Tax Changes & Updates

**Proposed Legislation**

- Senate Bill 815
    - Proposes to simplify and streamline irrevocable grantor trust process
- H.B. 1773
    - Proposes to establish a “fair share tax plan” by changing income tax system Reduces income tax on individual wages and interest to 1.9%
    - Raises tax on passive income to 12%
    - Net gains or income from disposition of property, estates, or trusts, royalties, patents, copyrights
    - Dividends, winnings from gambling and lotteries other than noncash prizes

# New Jersey Tax Changes & Updates

**Tax Changes retroactive to January 2023**

- Partnership Apportionment Change to Single Sales from 3 Factor
  - Effective for taxable years beginning on and after Jan. 1, 2023, and not withstanding other applicable sourcing provisions, a gross income taxpayer's income from a trade, business, partnership, or S Corporation is sourced consistent with the CBT rules
- BAIT Apportionment Shifts to Single Sales (Again)
  - New Jersey Division of Taxation issued guidance in October of 2023 that 2023 BAIT calculation would now follow the CBT rules
  - The NJ DOT did not have to extend the GIT legislative change to the BAIT
  - Practitioners are generally thinking that the NJ DOT didn't know why they were making this change, only that they were making it

# New Jersey Tax Changes & Updates

**Tax Changes effective for tax years after July 1, 2023**

- Adoption of bright line economic nexus standard for corporate income tax
  - $100k of sales or 200 or more separate transactions delivered to customers in state
- Adoption of updated MTC guidance on PL 86-272
- Shift from Joyce to Finnegan for Combined Reporting
  - Joyce- receipts only included in apportionment if nexus is established by individual entity
  - Finnigan- all receipts included in apportionment, regardless of nexus by entity

# New Jersey Tax – Clock is Ticking!

- ***New Jersey 2.5% corporate surtax set to sunset the end of 2023 or is it?***
  - Surtax increased tax rate on companies with net income in excess of $1 million from 9% to 11.5%
  - Surtax accounts for almost 20% of CBT revenue which totaled $5.8 Billion in FY 2022
  - End of surtax is expected to cost state $332.5 million in FY 2024 and $1 billion in FY 2025
  - Legislation has been introduced to keep the surtax dormant but available to resurrect it in the event additional revenue is needed

# Contact the Presenter


## Thomas M. Frascella

DIRECTOR, TAX STRATEGIES, STATE AND LOCAL TAX GROUP LEADER

tfrascella@kmco.com


Tom has a wide range of experience providing state and local tax strategies & services in the areas of income/franchise, sales and use, realty transfer, and unclaimed property taxes to a variety of businesses, including multi-state and multi-national businesses in the light and heavy manufacturing, distribution, life sciences, not-for-profit and professional services industries. He helps businesses address their multi-state tax needs.

As an experienced multi-state tax professional, Tom has developed a solid understanding of the issues and concerns of growing middle market companies and large publicly-traded enterprises and has been proactive in anticipating their issues and developing solutions to minimize administrative burdens and tax exposures.

# Contact the Presenter


## Reed Brown, CMI

MANAGER, STATE AND LOCAL TAX

reedbrown@kmco.com


Reed is a Manager in Kreischer Miller's State and Local Tax group. As an experienced multi-state tax professional, Reed has developed a solid understanding of state and local tax concerns and he assists businesses in anticipating issues and developing solutions to minimize administrative burdens and exposures. He has a wide range of experience providing services in the areas of multi-state income/franchise tax and sales and use tax, as well as audit defense, tax planning, and state tax controversies in the manufacturing, construction, distribution, and professional services industries.

Reed is committed to serving as an advisor to his clients, and particularly enjoys helping them understand and navigate the often complex, and at times daunting, state and local tax environment.

# Individual Tax Update

November 16, 2023

Kate Stewart, Director, Tax Strategies
Brad Runyen, Director, Tax Strategies

Kreischer Miller

# Disclaimer

This material is updated as of November 13, 2023 and is provided for general informational and educational purposes only and should not be construed as legal or tax advice. You should not rely on information contained in this presentation to make business or tax decisions without first consulting with your tax advisor. The information contained in this material is subject to change without notice. The presenters undertake no obligation to update this material.

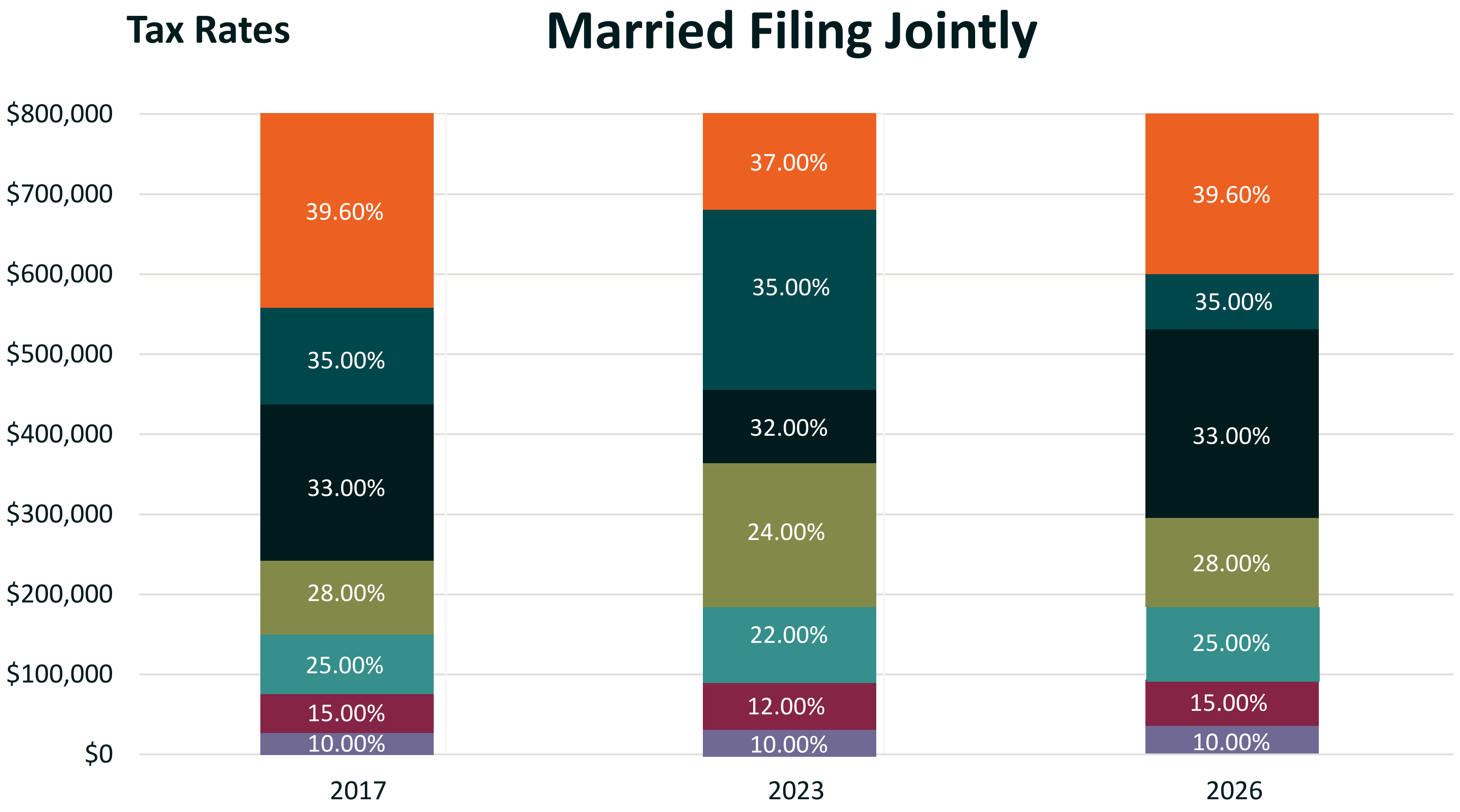
# Agenda

1. General Planning Checklist
2. TCJA Sunsets
3. Retirements Plans & Secure 2.0
4. Education Savings and Credits – Overview
5. Year-end timing items (Capital gains/losses, itemized deductions)
6. Estimated Taxes and underpayments

# 2023 Year-End Planning – Checklist

- Itemized Deduction Bunching
  - Medical expenses
  - Charitable contributions
- Gain & Loss Harvesting
  - Current rate > Future rate
- Retirement Planning
  - Funding IRAs, 401Ks, pension plans
  - Consider Roth conversion
  - Required Minimum Distributions
- Education Planning
  - 529 plans
- Charitable Planning
  - Qualified Charitable Distribution (QCD)
  - Donor Advised Fund (DAF)
  - Appreciated stock
- Estimated Taxes
  - Review payments and estimated taxable income
  - Underpayment penalty
  - Additional W-2 withholding

# Historic, Current, & Future Tax Rates




# TCJA Sunsets – December 31, 2025

| Tax Provision | Current Law | 2026 |
|---|---|---|
| Highest marginal tax bracket | 37% | 39.6% |
| Qualified Business Income "QBI" Deduction | Eligible Taxpayers receive up to 20% deduction of business income | 20% deduction eliminated |
| Alternative Minimum Tax (AMT) | Applies to relatively few taxpayers given high exemption amounts | AMT would apply to more taxpayers due to lower exemption and income phaseout amounts |
| State and Local Income Tax Deduction | Limited to $10,000 Cap | No limit |
| Limitation on Itemized Deductions "Pease Limitation" | Repealed 2018 through 2025 | Reinstated; cap on total allowable itemized deductions |
| Limitation on cash charitable contributions | Limited to 60% of AGI | Limited to 50% of AGI |
| Miscellaneous itemized deductions | Not available | Available in excess of 2% of AGI, including investment fees, un-reimbursed work-related expenses |

# Required Minimum Distributions
# RMDs

**Required Beginning Date**

IRA owners must take their first RMD by April 1 of the year after they reach age 73

| 2019 & earlier | | 2020 | | 2023 | | 2033 |
|---|---|---|---|---|---|---|
| **Age 70 1/2** | → | **Age 72** | → | **Age 73** | → | **Age 75** |

- Example: You turn 72 years old in 2023 (born in 1951)
    - First RMD will be for 2024 (the year you turn 73)
    - Can be taken as late as April 1, 2025 but then the 2nd payment must be taken by December 31, 2025.

# Inherited IRAs – Non-Spousal Beneficiaries

- Proposed regulations
    - 10-year distribution rule
- Notice Relief for failed RMDs
    - 2021, 2022, and 2023

# Inherited IRAs – Non-Spousal Beneficiaries

| Original owner began taking RMDs | Original owner did not take RMDs |
| --- | --- |
| • Annual RMDs paid to the beneficiary in years 1 – 9.<br>• Fully depleted by year 10 | • Annual<br>• Wait until year 10<br>• Skip years<br>• Fully depleted by year 10 |

# Inherited IRAs – Spousal Beneficiary

- Treated as a beneficiary of the IRA or elect to be treated as its owner
- The owner dies before required beginning date RMDs to the surviving spouse can be postponed until the later of:
    - The year following the owner's death, or
    - The year of the owner's required beginning date for RMDs

# Inherited IRAs –Spousal Beneficiary

| Original owner | Beneficiary |
| --- | --- |
| • RMDs based on the spouse's life expectancy<br>• Distributions begin when spouse reaches the required beginning date<br>• Special rules apply when more than 10 years younger than IRA owner | • When spouse is older than owner of the IRA<br>• Must take RMDs<br>• No RMD taken rolled over into own IRA |

# Charity – Qualified Charitable Distributions (QCD)

- Taxpayer must be age 70½ or older
- Distribution must be direct to charity
- Limited to $100,000
  - Spouse can make QCD from own IRA up to $100,000
- Counts towards RMD
- Distributions to donor advised funds & private foundations - **do not qualify**
- Not included in income and not an itemized charitable deduction

# Education – Savings & Credits

- **529 Savings Plans**
  - Treated as a completed gift for gift tax purposes – annual exclusion up to $17,000 per recipient in 2023
  - "Superfund" opportunity to contribute 5 years at once ($85K in 2023)
  - Investment growth in 529 Savings Plan tax free if used for qualified education purposes
  - Most states have some mechanism (subject to limitations) of deduction for 529 type contributions

# Education – Savings & Credits

- **529 Savings Plans, cont'd**
  - Distributions can be used for qualified education expenses
    - Includes trade schools
  - Up to $10K/year for K-12 education tuition
  - Secure 2.0 opened option to rollover 529 to ROTH IRA
    - Up to $35K aggregate lifetime limit
    - Restrictions based on duration of 529 plan and timing of contributions

# Education – Savings & Credits

- **Coverdell Education Savings Accounts**
  - Also treated as completed gift
  - Significant limitations that make it less attractive option
    - Max contribution of $2,000/year recipient
    - AGI Phase-out limitations (full phase out)
      - Single/other - $110K MFJ - $220K
  - Greater flexibility in how funds are invested
  - Distributions for either qualified education or withdrawal by beneficiary at age 30

# Education – Savings & Credits

- **American Opportunity Tax Credit**
  - Available for four tax years
  - Max value of $2,500 credit per year
  - AGI Phase-outs:
    - MFJ: $180K
    - Single: $90K
- **Lifetime Learning Tax Credit**
  - Nonrefundable $2K credit (unlimited number of years)
  - Also subject to AGI Phase-outs

# Capital Gains (Losses)

## Capital Gain Planning

- Maximize gains at lower current tax rates (tax bracket management and/or future rate increases)
- Immediate repurchase of assets sold to increase basis at lower tax rate (as applicable)
- Tax Savings vs. Return on Investment

## Capital Loss Planning

- Harvest loss positions – Focus on current year tax savings
- Consider digital/crypto wash losses
- Planning of short/long losses interplay for appropriate benefit

# Capital Gains (Losses)

| | SHORT TERM GAINS | LONG TERM GAINS |
|---|---|---|
| SHORT TERM LOSSES | NEUTRAL | INEFFECTIVE |
| LONG TERM LOSSES | EFFECTIVE | NEUTRAL |

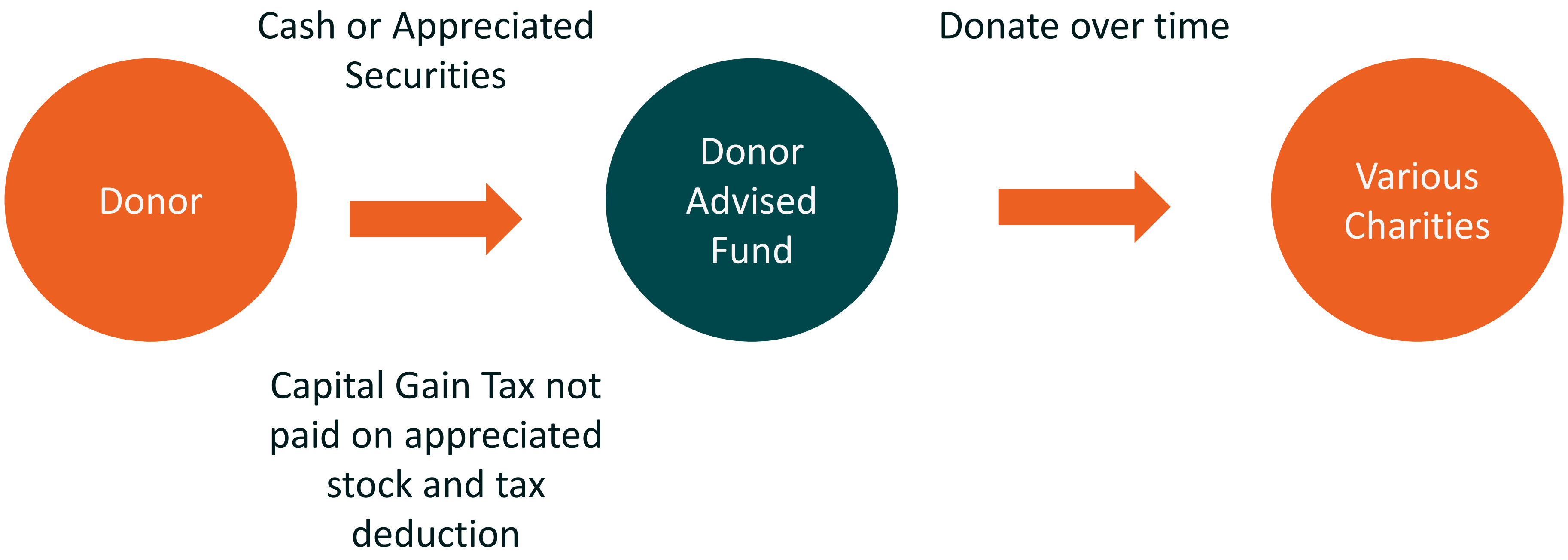
# Itemized Deductions

- **Healthcare Expenses**
  - If exceeding 7.5% of AGI, maximize (as applicable) into current year to increase benefit
  - Health insurance premiums payment timing
- **Charitable Contributions**
  - Timing of contributions based on income tax bracket (value of deduction)
  - Bunch/maximize if value in 2023 greater than 2024
  - Interplay with Qualified Charitable Distribution (not an itemized deduction)

# Charity – Donor Advised Fund (DAF)

- Fund with cash – deductible up to 60% of adjusted gross income
  - Example – AGI $500,000. Can fund DAF with $300,000
- Fund with appreciated assets – deductible up to 30% of adjusted gross income
  - Example – AGI $500,000. Can fund DAF with $150,000
- Long-term appreciated assets
  - Receive deduction for the fair market value
  - Do not have to pay capital gain or net investment income tax on the appreciation
  - Example – Basis in stock $100,000 and now worth $500,000. $400,000 gain is not taxable if move the stock to DAF

# Charity – Donor Advised Fund (DAF)



# Year-End – Considerations

- **Underpayment Interest Rates**
  - Currently 8% rate for Q4 2023
  - 7% rate for Q1- Q3 2023
  - Estimated tax remittance
    - 90% of Current Year Projected Tax
    - 100/110% of Prior Year Tax Liability
- **Adjust Year-End Bonus withholdings**
  - Withholding treated as paid evenly throughout the year

# Thanks for Playing!

# Supplement –2023 Federal Income Brackets

| Tax Rate | Married Filing Joint & Surviving Spouse | Single | Head of Household | Married Filing Separately |
|---|---|---|---|---|
| 10% | $0 – $22,000 | $0 – $11,000 | $0 – $15,700 | $0 – $11,000 |
| 12% | $22,001 – $89,450 | $11,001 – $44,725 | $15,701 – $59,850 | $11,001 – $44,725 |
| 22% | $89,451 – $190,750 | $44,726 – $95,375 | $59,851 – $95,350 | $44,726 – $95,375 |
| 24% | $190,751 – $364,200 | $95,376 – $182,100 | $95,351 – $182,100 | $95,376 – $182,100 |
| 32% | $364,201 – $462,500 | $182,101 – $231,250 | $182,101 – $231,250 | $182,101 – $231,250 |
| 35% | $462,501 – $693,750 | $231,251 – $578,125 | $231,251 – $578,100 | $231,251 – $346,875 |
| 37% | Over $693,750 | Over $578,125 | Over $578,100 | Over $346,875 |

# Supplement – 2023 Federal Long-Term Capital Gains Brackets

| Long-Term Capital Gains Tax Rate | Married Filing Joint & Surviving Spouse | Single | Head of Household | Married Filing Separately | Estates & Trusts |
|---|---|---|---|---|---|
| 0% | $0 – $89,250 | $0 – $44,625 | $0 – $59,750 | $0 – $44,625 | $0 – $3,000 |
| 15% | $89,251 – $553,850 | $44,626 – $492,300 | $59,751 – $523,050 | $44,626 – $276,900 | $3,001 – $14,650 |
| 20% | Over $553,850 | Over $492,300 | Over $523,050 | Over $276,900 | Over $14,650 |

**Planning Observation – Capital Gains are still subject to the 3.8% Net Investment Income Tax**

# Supplement – 2023 Retirement and Medical Savings Plans

| 401(k) Plans | IRA Contributions | ROTH IRA Contributions | FSA and HSA Contributions |
|---|---|---|---|
| • $22,500/year<br>• $30,000/year for age 50 or older with catch-up of $7,500<br>• Maximum eligible compensation base is $330,000 | • Deductible contributions up to $6,500 ($7,500 for age > 50)<br>• AGI max phase-outs for deductible contributions<br>  • Single: $83,000<br>  • MFJ: $136,000 if covered by workplace plan<br>  • MFJ: $228,000 if spouse covered by workplace plan | • $6,500 contribution ($7,500 for age > 50)<br>• AGI max phase-outs for contributions<br>  • Single: $153,000<br>  • MFJ: $228,000<br>• Back-door ROTH still viable for non-deductible contributions | • FSA Max Deferral: $3,050<br>• FSA Rollover to 2024: maximum of $610<br>• HSA Max Deferral<br>  • Single: $3,850<br>  • Family: $7,750<br>  • HSA Catch-up contributions $1,000<br>• Dependent Care FSA<br>    • $5,000 per yr per household |

# Supplement – 2024 Federal Income Brackets

| Tax Rate | Married Filing Joint & Surviving Spouse | Single | Head of Household | Married Filing Separately |
|---|---|---|---|---|
| 10% | $0 – $23,200 | $0 – $11,600 | $0 – $16,550 | $0 – $11,600 |
| 12% | $23,201 — $94,300 | $11,601 – $47,150 | $16,551 – $63,100 | $11,601 – $47,150 |
| 22% | $94,301 — $201,050 | $47,151 – $100,525 | $63,101 – $100,500 | $47,151 – $100,525 |
| 24% | $201,051 — $383,900 | $100,526 – $191,950 | $100,501 – $191,950 | $100,526– $191,950 |
| 32% | $383,901 — $487,450 | $191,951 – $243,725 | $191,951– $243,700 | $191,951 – $243,725 |
| 35% | $487,450 - $731,200 | $243,726 – $609,350 | $243,700 – $609,350 | $243,726 – $365,600 |
| 37% | Over $731,200 | Over $609,350 | Over $609,350 | Over $365,600 |

# Supplement – 2024 Retirement and Medical Savings Plans

| 401(k) Plans | IRA Contributions | ROTH IRA Contributions | FSA and HSA Contributions |
|---|---|---|---|
| • $23,000/year<br>• $30,500/year for age 50 or older with catch-up of $7,500<br>• Maximum eligible compensation base is not available as of 11/6/2034 | • Deductible contributions up to $6,500 ($7,500 for age > 50)<br>• AGI max phase-outs for deductible contributions<br>  • Single: $87,000<br>  • MFJ: $143,000 if covered by workplace plan<br>  • MFJ: $240,000 if spouse covered by workplace plan | • $7,000 contribution ($8,000 for age > 50)<br>• AGI max phase-outs for contributions<br>  • Single: $161,000<br>  • MFJ: $240,000<br>• Back-door ROTH still available for non-deductible contributions | • FSA Max Deferral: $3,050<br>• FSA Rollover to 2024: maximum of $610<br>• HSA Max Deferral<br>  • Single: $4,150<br>  • Family: $8,300<br>  • HSA Catch-up contributions $1,000<br>• Dependent Care FSA<br>  • $5,000 per yr per household |

# Contact the Presenter


## Bradley J. Runyen, CPA

DIRECTOR, TAX STRATEGIES

brunyen@kmco.com


Brad is a Director in Kreischer Miller's Tax Strategies group. Brad provides tax services including compliance, planning, and research for multi-state corporations, partnerships, trusts, and high-net-worth individuals. He has assisted companies with business transactions, including acquisitions, sales, and reorganization transactions.

Brad has a diversified range of experience providing services to a variety of companies in the construction, manufacturing, real estate, distribution, and service industries.

# Contact the Presenter


## Kathryn J. Stewart, CPA, MT

DIRECTOR, TAX STRATEGIES

kstewart@kmco.com


Kate is a Director in Kreischer Miller's Tax Strategies group. Kate has experience providing tax and business advisory services. She enjoys working with business owners and key personnel to assist with various tax matters including tax planning, tax compliance, cost segregation studies, research and development tax credits, business growth, and succession planning.

Kate works with an extensive range of industries, including construction, real estate, distribution, and manufacturing.

# Business Tax Update

November 16, 2023

Carlo Ferri, Director, Tax Strategies
Brian Kitchen, Director, Tax Strategies

Kreischer Miller

# Agenda

- Tax Law Changes: Tax Depreciation, Interest Expense Limitation and Excess Business Losses
- Energy Incentives
- Research and Development Amortization
- Year-End Business Planning Check-List
- Federal Tax Compliance and Reporting Changes

# Depreciation Update

**De minimis Safe Harbor Election**

- Accounting policy - Book/Tax Conformity
- Up to $5,000 per unit of property if the business has an Applicable Financial Statement
- Up to $2,500 per unit of property if the business **does not** have an Applicable Financial Statement

**Bonus Depreciation**

- 80% with no phase-out or taxable income limitation in 2023; 60% in 2024; 40% in 2025; 20% in 2026
- Opportunity to create a business loss
- Qualified Improvement property – certain qualifying improvements to the interior portion of a non-residential building
  ***Excludes enlargements, elevators/escalators and internal structure***

**Section 179 Expense**

- Immediate write-off
- Limited to $1.16 million with $2.89 million property phase-out
- Limited to taxable income of the entity
- Enhanced property includes certain building components; ***i.e. Roof, HVAC, Fire Equipment, Security and Alarm Systems***

**Tax Deductions**

# Business Interest Limitations

- Business interest is limited to sum of 30% of adjusted taxable income
- Depreciation, amortization, and depletion is **no longer** allowed to be added back to adjusted taxable income
- Exceptions
    - Small businesses with 3 year average gross receipts under 29 million**
    - Real Property businesses***


** Related party aggregation of gross receipts apply
*** Must elect to depreciation fixed assets using ADS

# Business Loss Limitations

**Current law**

- Business loss limitation prohibits individuals, partnerships, S Corporations and trusts and estates from netting aggregate deductions allocable to trade or businesses against nonbusiness income, to the extent such business losses exceed a threshold amount. Any disallowed business loss is treated as part of the taxpayer's Net Operating Loss and carried over to the next tax year
- Threshold limit is $289,000 for 2023 ($578,000 for joint filers)
- Tax planning complexity - hierarchy of losses
- Lack of guidance issues
    - "Attributable" to Trade or Businesses
    - Sale of partnership interest or S Corporation stock

# Energy Incentives for Business Solar and Wind

| | Pre-IRA (Tax Year 2022 & Prior) | Post-IRA (Tax Year 2023 & Future) |
|---|---|---|
| Amount | Max credit of 30% of the eligible basis | Max 30% +10% add-on credits for meeting specific requirements |
| Eligible Systems | Primarily used for solar, wind, fuel cell or waste energy recovery | Expanded to include more eligible property such as biogas and microgrid controllers |
| Eligibility to Claim | Taxpayers | Now include government and tax-exempt entities through the direct payment options |
| Transfer/Selling | Prohibited | Now eligible to sell or transfer credits to qualified buyers |

# Commercial Building Energy Deduction 179D

| | Pre-IRA (Tax Year 2022 & Prior) | Post-IRA (Tax Year 2023 & Future) |
|---|---|---|
| Amount | Max $1.80 per square foot | Max $5.00 per square foot |
| Allocation for Designers | Government Building Owners | Government & Tax-Exempt Building Owners |
| Lifetime Deduction | Max $1.80 per square foot for the lifetime of the building | Deduction resets after 3 of 4 years |
| Calculation Methodology | Energy Modeling<br>Compare to a building to a baseline standard | Energy Modeling<br>Or<br>Before & After Energy Reduction |

# Research and Development

**Current law**

- Governed by IRC Section 174
- Expenses incurred WITHIN the U.S. – 5-year amortization using mid-year convention
- Expenses incurred OUTSIDE the U.S. – 15-year amortization using mid-year convention
- Expenses include specified research or experimental expenditures, including software development costs
- R&D Tax Credit still available, but does require additional analysis

# Research and Development

**The Math**

| Year | GAAP Books | Tax Return | Difference |
|---|---|---|---|
| 12/31/2022 | $ 1,000,000 | $ 100,000 | $ 900,000 |
| 12/31/2023 | | $ 200,000 | $ (200,000) |
| 12/31/2024 | | $ 200,000 | $ (200,000) |
| 12/31/2025 | | $ 200,000 | $ (200,000) |
| 12/31/2026 | | $ 200,000 | $ (200,000) |
| 12/31/2027 | | $ 100,000 | $ (100,000) |
| **Total** | $ 1,000,000 | $ 1,000,000 | $ - |

# Research and Development

**Congress Response**

- Changes part of several proposed pieces of legislation
- Nothing has passed

# Research and Development

**IRS Response**

- September 2023 – IRS and Treasury issued Notice 2023-63
- Intent to issue proposed regulations implementing Section 174 research expense capitalization
- Provides interim guidance and further clarity into the requirement for capitalization, but is in line with the TCJA guidance
- The IRS anticipates the forthcoming proposed regulations will be effective for taxable years ending after September 8, 2023 (the issuance date of Notice 2023-63). Taxpayers may, however, generally rely on the notice for taxable years beginning after December 31, 2021
- Notable clarifications:
    - Includable expenditures - Labor costs (including benefits and payroll taxes), materials and supplies, cost recovery (depreciation), patent costs, overhead and travel
    - Excludable expenditures – G&A support (HR, Accounting, Admin), interest on debt, web hosting, costs to register trademark

# Research and Development

**IRS Response**

- Notable clarifications:
    - Allocating expenditures – cause and effect approach
        - Direct SRE labor costs over total labor costs
        - Square footage of a facility dedicated to SRE activities over total square footage of the facility
    - Treatment of software development
        - Includes system software, programming software, application software, and embedded software
        - Applies only to costs for software upgrades and enhancements. It does not apply to maintenance after the software is placed in service

# Research and Development

**IRS Response**

- Notable clarifications:
    - Research funding (contract research)
        - Research provider must be at financial risk of loss under an agreement in order for capitalization
        - The right to use the SRE product is the real determinative factor in the analysis
        - IRS has requested comments

# Year-End Business Tax Planning Checklist

| **Checklist** | |
|---|---|
| Accounts Receivable Review | Income Deferral Strategies |
| Prepaid Expenses | Evaluation of Company Retirement Plan |
| Inventory Review | Timing of Payroll/Bonus payments |
| Fixed Asset Purchases | |
| Capitalization Policy | |
| Pre-payment of state entity level taxes | |
| Estimated Tax/Cash Flow Planning | |
| Accounting Methods Review | |

# Federal Tax Compliance and Other Reporting Changes

**Corporate Transparency Act (CTA)**

- The CTA is a new federal law designed to combat money laundering, tax evasion, and other illicit financial activities by requiring “reporting companies” to disclose beneficial ownership information (BOI) about their “beneficial owners” to the Financial Crimes Enforcement Network (FinCEN), a bureau of the U.S. Department of Treasury
- January 1, 2024, reporting companies newly formed or registered in the U.S. on or after that date will have 30 days to report BOI and “company applicant” information to FinCEN
- Reporting companies existing or registered in the U.S. prior to January 1, 2024, will need to report BOI (not “company applicant” information) to FinCEN by January 1, 2025

# Federal Tax Compliance and Other Reporting Changes

**Corporate Transparency Act (CTA)**

- Who must file? Every corporation, LLC or other entity created by the filing of a document with a Secretary of State or similar office under the law of a state, **unless there is an available exemption**
- What are the exemptions?
    - 23 exemptions in total
    - Exempt entities include, for example, publicly traded companies and other entities that file reports with the SEC, banks, credit unions, money services businesses, securities brokers and dealers, tax-exempt entities, insurance companies, state-licensed insurance producers, pooled investment vehicles, public utilities, and accounting firms
    - **Large operating company**: an entity that (1) employs more than 20 full-time employees in the United States, (2) has an operating presence at a physical office within the United States, and (3) has filed a federal income tax or information return in the United States for the previous year demonstrating more than $5 million in gross receipts or sales

# Federal Tax Compliance and Other Reporting Changes

**1099 Tax Reporting Changes**

- 1099-K - IRS has lowered the reporting threshold for Form 1099-K for the 2023 tax year from $20,000 and 200 transactions to $600, regardless of transaction limits
- Form 1099 series – **<u>must be filed electronically</u>** if the filer is required to file 10 or more "specified information returns" during the calendar year that includes the first day of the plan year. Non-compliance will result in penalties

# Contact the Presenter


## Carlo R. Ferri, CPA

DIRECTOR, TAX STRATEGIES

cferri@kmco.com


Carlo is a Director in Kreischer Miller's Tax Strategies group. Carlo has a wide range of experience providing tax and business advisory services to privately-held companies in various industries including manufacturing, distribution, and construction. He advises owners and key executives through the various cycles of their business related to corporate and individual tax matters (i.e., growth, maturity, exit) and represents them in front of the IRS.

Carlo is an active member of the community. In addition to participating in numerous accounting and construction industry groups, he is involved with several not-for-profit organizations.

# Contact the Presenter


## Brian D. Kitchen, CPA, MT

DIRECTOR, TAX STRATEGIES

bkitchen@kmco.com


Brian is a Director in Kreischer Miller's Tax Strategies group. He has a wide range of experience providing domestic and international tax planning and compliance services to a variety of middle market companies and entrepreneurial businesses. Brian has also assisted companies with business transactions, including mergers, acquisitions and transition planning. He has significant experience in federal, state, and local tax audits, settlements, and appeals.

Brian provides tax services to companies in the manufacturing, distribution, media, real estate, investment, financial, and professional services industries.


# About
# Kreischer Miller

Kreischer Miller is an advisory, audit and accounting, and tax firm serving the Greater Philadelphia and Lehigh Valley areas. We take an advisory approach in everything we do, working diligently to understand what your business needs to move ahead and providing the tools and guidance to help you get there.

**Learn more at** **www.kmco.com**