Construction Industry Webinar

Tax Update for Construction Contractors

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Agenda

1. Key tax provisions in the Inflation Reduction Act (IRA) and other legislation
2. Look ahead at expiring tax provisions
3. Tips for year-end tax planning
4. State tax planning opportunities

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Inflation Reduction Act and Other Provisions

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IRA Overview

- The Inflation Reduction Act of 2022 was signed into law on August 16th, 2022
- Smaller in scope when compared to the Build Back Better Act
  - Focused on providing increased clean energy incentives and several revenue raisers
  - Electric vehicle credit enhancements
  - Residential home energy credit enhancements
  - Solar credit enhancements
  - IRC 179D enhancements

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Energy Efficient Commercial Buildings Deduction – Section 179D

- IRC 179D was enacted to encourage commercial building owners to install energy efficient property. Installation of energy efficient commercial building property occurs when constructing a new, or improving an existing, commercial building or government building.
- Prior to the IRA, Section 179D provided a permanent deduction of up to $1.80 per square foot for certain energy-saving commercial building property installed as part of:
    1. The interior lighting system;
    2. The heating, cooling, ventilation, or hot water system; or
    3. The building envelope

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Energy Efficient Commercial Buildings Deduction – Section 179D, *continued*

The IRA enhanced and expanded Section 179D as follows:

- A reduction in the minimum required savings in total annual energy and power costs from a 50% reduction to a 25% reduction
- Removal of the existing rules for partial certifications
- Increased deductions for meeting prevailing wage and apprenticeship requirements

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Energy Efficient Commercial Buildings Deduction – Section 179D, *continued*

Enhancements and expansions of Section 179D, continued:

- Removal of lifetime limitation. The 179D deduction can be taken every three tax years
- Expansion to permit allocations to tax-exempt entities
- Establishment of a new retrofit program as an election for a new alterative deduction for energy efficient building retrofits, taken in the qualifying final certification year

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Business Interest Deduction Limitation

- Limit on deductibility of business interest expense to 30% of adjusted taxable income
- Limitation increased to 50% –CARES Act for tax years 2019 and 2020
- In 2022, the limit will narrow again
  - Adjusted Taxable Income (ATI), from which 30% limitation is calculated, will now exclude depreciation and amortization add-back
- Any interest expense disallowed is carried forward

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Business Interest Deduction Limitation, *continued*

Description	163(J) LIMITATION CALCULATION	
	2021	2022
Taxable Income before 163(j) Limitation	300,000	300,000
Interest Expense	400,000	400,000
Depreciation Expense	500,000	-
Amortization Expense	50,000	-
Adjusted Taxable Income (ATI)	1,250,000	700,000
Interest Expense (30% Limit)	375,000	210,000
Interest Expense Carryover	25,000	190,000
Taxable Income after 163(j) Limit	325,000	490,000

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Research & Development Expenses – 2022 Tax Year & Forward

IRC Section 174 Costs

- All costs incidental to the development or improvement of a product or process
- How to quantify – not easily defined
  - Overhead allocation methodology

2022 Current Law – as modified by TCJA

- 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

Other thoughts:

- Phantom income – cash flow requirements
- Congress legislation required to delay or defer current law

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Research & Experimental Expenditures, *continued*

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

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Expiring Tax Provisions

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Bonus Depreciation

- Bonus depreciation was increased to 100% for eligible property placed in service from September 27, 2017 through December 31, 2022
- Starting in 2023, bonus depreciation will begin to phase out

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

Meals and Entertainment

Client Meals

- Meals purchased from a restaurant are temporarily 100% deductible for amounts paid after December 31, 2020 and before January 1, 2023
- Taxpayer present
- Business conducted
- Not extravagant
- No pre-packaged food

Employee Meals

- Meals provided for the convenience of the employer
- Overtime employee meals
- Meals during meetings of employees
- Temporarily 100% deductible for 2021 and 2022
- 50% deductible 2023-2025 (nondeductible after 2025)

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Meals and Entertainment, *continued*

Entertainment

- TCJA eliminated ability for a partial deduction
- Amusement, recreation
- Dues and Fees
- Food & beverage provided at such events ***unless*** it is separately stated on receipt or purchased separately

Company Events

- Holiday parties, picnics, team building events
- 100% deductible
- Available to all employees

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Work Opportunity Tax Credits (WOTC)

- Available through December 31, 2025
- In general, WOTC is 40% of the first-year wages of a targeted group of employees who worked 400 hours or more
  - For an employee who worked between 120 and 400 hours, credit is 25 percent of first-year wages paid
- The tax credit can range from $2,400 to $9,600 per employee depending on a worker's qualifications
- No limit applies to the number of individuals that can qualify
- Tax credit is reported on the company's federal income tax return and can be carried back one year or carried forward 20 years
- Strict compliance with reporting timeline is necessary

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Work Opportunity Tax Credits, *continued*

- Targeted Group Employees:
  - SNAP (food stamps) recipients,
  - Welfare recipients,
  - Designated community residents who are between the ages of 18 and 40 at their date of hire and reside within particular geographic areas,
  - Supplemental Security Income (SSI) or disability recipients,
  - Long-term unemployment recipients,
  - Veterans, which include a few sub-categories of qualified individuals,
  - Ex-felons,
  - Vocational rehabilitation referral employees, and
  - Summer youth employees who are between the ages of 16 and 18 at their hiring date and reside within particular geographic areas

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Income Tax Rates

- No rate increase proposals at individual level from 2022 to 2023
- Tax provisions at individual level that are scheduled to expire December 31, 2025:
  - Top tax bracket reverts to 39.6% (from current 37%)
  - The 12%, 22% and 24% individual income tax rates will increase (go back up to 2017 rates) - adjusted for inflation
  - Section 199A Qualified Business Deduction expires December 31, 2025
    - Current Top Individual Tax Rate of 37% when effectively adjusted for Section 199A 20% deduction = Effective QBI Net Top Rate of 29.6%

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2022 Federal Income Tax Rates

Tax Rate	Joint/Surviving Spouse	Single	Head of Household	Married Filing Separately
10%	$0 – $20,550	$0 – $10,275	$0 – $14,650	$0 – $10,275
12%	$20,551 – $83,550	$10,276 – $41,775	$14,651 – $55,900	$10,276 – $41,775
22%	$83,551 – $178,150	$41,776 – $89,075	$55,901 – $89,050	$41,776 – $89,075
24%	$178,151 – $340,100	$89,076 – $170,050	$89,051 – $170,050	$89,076 – $170,050
32%	$340,101 – $431,900	$170,051 – $215,950	$170,051 – $215,950	$170,051 – $215,950
35%	$431,901 – $647,850	$215,951 – $539,900	$215,951 – $539,900	$215,951 – $323,925
37%	Over $647,850	Over $539,900	Over $539,900	Over $323,925

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2023 Federal Income Tax Rates

Tax Rate	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

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Tips for Year-End Planning

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Wage Withholding/Estimates for 2022

- Consider revising your Form W-4
  - Wages/withholding considered earned evenly throughout tax year
- Adjusting your tax withholding or estimated payments to cover estimated tax liability (based on prior year or current year)
- If applicable, consult tax advisor to model out projected tax liability to ensure appropriately withheld
- 2022 Underpayment Interest Rates:
  - Q1 2022 – 3%
  - Q2 2022 – 4%
  - Q3 2022 – 5%
  - Q4 2022 – 6%

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2022 Tax Planning Strategies – Retirement and Health Savings Plans

401(k) Plans

- $20,500/year
- $27,000/year for age 50 or older with catch-up
- Maximum eligible compensation base is $305,000

IRA Contributions

- Deductible contributions up to $6,000 ($7,000 for age > 50)
- AGI max phase-outs for deductible contributions
  - Single: $78,000
  - MFJ: $129,000 if covered by workplace plan
  - MFJ: $214,000 if spouse covered by workplace plan

ROTH IRA Contributions

- $6,000 contribution ($7,000 for age > 50)
- AGI max phase-outs for contributions
  - Single: $140,000
  - MFJ: $208,000
- Back-door ROTH still viable for non-deductible contributions

FSA and HSA Contributions

- FSA Max Deferral: $2,850
- FSA Rollover to 2023: maximum of $570
- HSA Max Deferral
  - Single: $3,650
  - Family: $7,300
- HSA Catch-up contributions $1,000
- No limitation on HSA Rollover to 2023

Excess Business Losses Under Section 461(l)

- Created under the TCJA for years 2018 – 2025
- CARES Act – delayed implementation until 2021
- Inflation Reduction Act - extended through 2028
- An excess business loss is the amount by which the total deductions attributable to all your trades or businesses exceed your total gross income and gains attributable to those trades or businesses (adjusted for cost of living)
- For taxable years beginning in 2022, the threshold amounts are $270,000 ($540,000 MFJ)
- Any excess losses are treated as NOL carryover to the following year

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Net Operating Losses (NOLs)

- TCJA modified the treatment of NOLs
- Deduction is limited to 80% of taxable income
- Carryforward indefinitely
- Carrybacks no longer allowed
- CARES Act
  - Allowed 5 year carryback in 2018, 2019, 2020

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Looking Forward

- Social Security cost of living increase 8.7% in 2023 – consideration to tax bracket planning
- Planning for 2022 and 2023 currently set to follow normal planning approach:
  - Defer income and accelerate deductions
  - Manage income tax brackets
  - Maximize retirement contributions where possible
  - Consider state tax planning opportunities (529 plans, etc.)
- The focus of Congress for lame duck session and Q1 2023 is unknown, but flexibility in planning will continue to be a must!

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2023 Retirement and Medical Savings Plans

401(k) Plans

- $22,500/year
- $30,000/year for age 50 or older with catch-up
- Maximum eligible compensation base is $330,000

IRA Contributions

- Deductible contributions up to $6,500 ($7,500 for age > 50)
- AGI max phase-outs for deductible contributions
  - Single: $83,000
  - MFJ: $136,000 if covered by workplace plan
  - MFJ: $228,000 if spouse covered by workplace plan

ROTH IRA Contributions

- $6,500 contribution ($7,500 for age > 50)
- AGI max phase-outs for contributions
  - Single: $153,000
  - MFJ: $228,000
- Back-door ROTH still viable for non-deductible contributions

FSA and HSA Contributions

- FSA Max Deferral: $3,050
- FSA Rollover to 2024: maximum of $610
- HSA Max Deferral
  - Single: $3,850
  - Family: $7,750
  - HSA Catch-up contributions $1,000

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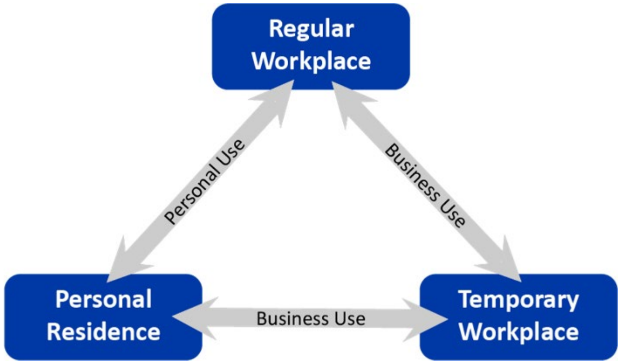
Mobile Workforce – Travel Expenses

1. Regular Workplace

- Someone who performs work at that same workplace for at least a year
- Traveling to and from your personal residence to your regular workplace is considered commuting and any reimbursement would be considered taxable compensation to that employee

2. Temporary Workplace

- Contractor on assignment for one year or less or employee with regular workplace who travels to temporary locations from time-to-time



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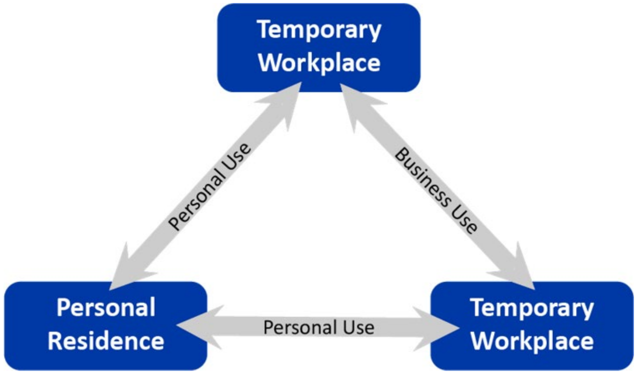
Mobile Workforce – Travel Expenses, *continued*

3. Multiple Workplaces

- Most contracting company employees fall under this category
- Employees who are required to visit multiple work locations each day/week or do not have a regular workplace
- If the accountable plan allows for travel reimbursement, then the compensation is nontaxable to the employee and deductible to the employer



IRS Funding

- IRS's budget has been cut by 23% since 2010
- The IRA increases IRS funding by $80 billion over next 10 years
- Funding is rumored to support 87,000 new IRS employees, which will be offset by roughly 50,000 current employees set to leave IRS or retire in the next 10 years
- The Congressional Budget Office has previously estimated this increase in funding would raise $206 billion in revenue, for a net increase of roughly $126 billion
- Estimated 5,000 new hires will be geared focus towards enforcement

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State Tax Planning Opportunities

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Entity Level Taxes – States

- In response to the $10,000 Federal SALT cap, some states have enacted an optional PTE tax as a workaround
  - Allows eligible pass-through entities to deduct state taxes at the entity level for Federal tax purposes
  - Provides a credit or income exclusion to the entity owners for state income tax purposes
- Options to Consider Before Making the Election
  - Determining if the taxpayer's resident state allows a credit to be claimed for taxes paid to other states
  - Additional administrative, legal, or accounting costs

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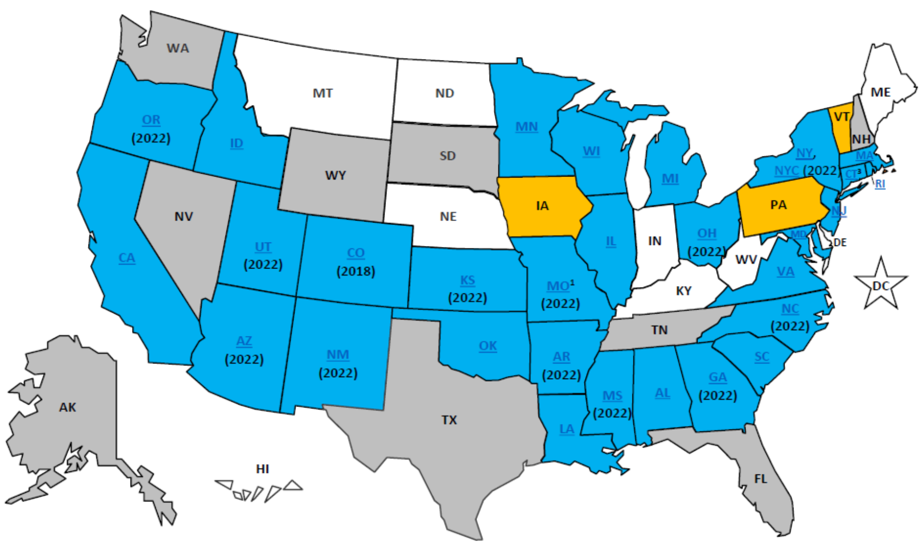
Entity Level Taxes – States

States with Enacted or Proposed Pass-Through Entity (PTE) Level Tax

As of August 31, 2022



- 29 states (& 1 locality) that enacted a PTE tax since TCJA SALT deduction limitation, effective for 2021 (or earlier) unless noted:

  AL, AR[1], AZ[1], CA, CO[2], CT[3], GA[1], ID, IL, KS[1], LA, MA, MI, MD, MN, MO[1], MS[1], NC[1], NJ, NM[1], NY, OH[1], OK, OR[1], RI, SC, UT[1], VA, WI, and NYC[1]

  [1] Effective in 2022 or later – on map (2022) or (2023)
  [2] Retroactive to 2018
  [3] Mandatory

- 3 states with proposed PTE tax bills:
  IA - HF 2087, session over, not enacted
  PA – HB 1709, in committee
  VT - H 0527 , session over, not enacted

- 9 states with no owner-level personal income tax on PTE income:

  AK, FL, NH, NV, SD, TN, TX, WA, WY

- 10 states with an owner-level personal income tax on PTE income that have not yet proposed or enacted PTE taxes:

  DE, HI, IN, KY, ME, MT, NE, ND, VT, WV

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Questions?

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