Small Business Tax Considerations:

Navigating the Post-Pandemic Landscape

Hosted by Rockland Trust and Ulshoeffer CPAs, PLLC

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Housekeeping

- This is a live event hosted and recorded through Zoom
- Have questions? Enter them in the Q&A tab on your screen – we will be answering questions at the end of the webinar
- Contact information for speakers will be included at the end of this webinar as well
- We will share this recorded presentation with everyone roughly two days following today's webinar

Speakers

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Agenda

1. Inflation Reduction Act ("IRA") of 2022
2. Consolidated Appropriations Act, 2023 (including the "SECURE ACT 2.0")
3. MA 63D Entity Level Tax ("ELT")
4. MA "Millionaires' Tax"

Inflation Reduction Act (IRA) of 2022: Overview

- Signed into law on August 16, 2022
- What is the IRA?
  - The IRA is aimed to reduce the budget deficit, fund the IRS, makes major investments in healthcare, domestic energy production and manufacturing, and climate change
    - e.g. new corporate AMT 15% tax for corporations over $1 billion income, $80 billion IRS funding, provisions to prescription drug policies and drug manufacturers, etc.

Today, we'll highlight the noteworthy
energy related tax credit incentives

Learn more:
[Inflation Reduction Act Summary of Energy and Climate Provisions]

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IRA of 2022: Energy Related Tax Credits

New Clean Vehicle

Formerly "new qualified plug-in electric drive motor vehicles credit"

- Applies to vehicles placed in service *after* 12/31/22 through 2032
- No limit of vehicles per manufacturer
- Worth up to $7,500 in two separate $3,750 components:
    - $3,500 met when a certain percentage of the critical minerals in the battery are extracted or processed in the U.S. or a country with a U.S. free trade agreement; and
    - $3,500 met when a certain percentage of battery is manufactured or assembled in North America
    - To avoid taxpayers being overburdened with locating technical requirements, the IRA requires sellers to provide buyers with a report detailing the vehicle's satisfaction of these requirements and the maximum available for the vehicle
- Credits will be disallowed for vehicles with MSRP exceeding $80,000 for vans, SUVs, and pickup trucks; and $55,000 for all other vehicles
    - MSRP does not include dealership markups

IRA of 2022: Energy Related Tax Credits

New Clean Vehicle, continued…

- Credits will also be disallowed for taxpayers with modified adjusted gross income ("MAGI") of more than $300,000 for taxpayers married filing jointly, $225,000 for head of household and $150,000 single taxpayers – for the tax year prior to purchase OR the tax year in which the vehicle is purchased, whichever is higher
- Starting in 2024, taxpayers will be able to claim the credit at the time they purchase the vehicle, through the dealership, thereby reducing the purchase price of the vehicle
    - If, when you file your return for that year, your MAGI exceeds the previously mentioned limits – then you are required to repay any credit received

View IRS List of Eligible Vehicles

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IRA of 2022: Energy Related Tax Credits

Used Clean Vehicle *(new)*

- Applies to vehicles placed in service after 12/31/22, through 2032
- Vehicle must be at least 2 years old and an electric vehicle
- Credit equals lesser of $4,000 or 30% of sale price; and sale price cannot exceed $25,000
- Credit will be disallowed for taxpayers with modified adjusted gross income of more than $150,000 for taxpayers married filing jointly, $112,500 for head of household and $75,000 single taxpayers
- Qualified sale transaction is between a qualified buyer and a dealer
    - If you locate an eligible vehicle from an individual, locating a qualified dealer willing to broker the transaction may prove to be a cost-effective way to ensure requirements are met
- Qualified buyer has not claimed the credit within the preceding 3 years, cannot be claimed as a dependent of another, cannot purchase for resale

IRA of 2022: Energy Related Tax Credits

Qualified Commercial Clean Vehicles Credit *(new)*

- Applies to any vehicles placed in service after Dec. 31, 2022, through 2032
- Credit per vehicle is the lesser of:
  - 15% of the vehicle's basis (30% for vehicles not powered by a gasoline or diesel engine) or,
  - the "incremental cost" of the vehicle over the cost of a comparable vehicle powered solely by a gasoline or diesel engine
- Must be made by a qualified manufacturer and as a motor vehicle per title II of the Clean Air Act
- The maximum credit per vehicle is $7,500 for vehicles with gross vehicle weight ratings of less than 14,000 pounds, or $40,000 for heavier vehicles

Learn more:
IRS FAQ on Clean Vehicle Credits for New, Previously Owned, and Commercial Clean Vehicles

IRA of 2022: Energy Related Tax Credits

Energy-Efficient Home Improvement Credit

Formerly "nonbusiness energy property credit"

- Modified and extended through 2032
- Beginning in 2022, credit is increased from 10% to 30%
- No more lifetime credit limitation, rather limits the allowable credit to $1,200 per taxpayer, per year
  - Annual limits of $600 credits for residential energy property expenditures, windows, and skylights and $250 for any exterior door ($500 total for all exterior doors)
  - Notwithstanding these limitations, a $2,000 annual limit applies with respect to amounts paid or incurred for specified heat pumps, heat pump water heaters, and biomass stoves and boilers

IRA of 2022: Energy Related Tax Credits

Energy-Efficient Home Improvement Credit, continued…

- Qualified energy property made eligible for the credit cover a range of products, including:

Water heaters	Heat pumps
Central air conditioners	Hot water boilers
Biomass stoves	Oil furnaces
Air sealing materials and systems	Home energy audit costs
Electrical panels installed to enable qualified improvements (with specific efficiency requirements for each upgrade)	

- Reporting requirements are updated to mandate that manufacturers and taxpayers label and report, respectively, a product identification number associated with the property in order to access the credit – for property placed in service after 12/31/24

Learn more:
[IRS FAQ on Energy Efficient Home Improvements and Residential Clean Energy Property Tax Credits]

IRA of 2022: Energy Related Tax Credits

New Energy-Efficient Home Credit

- Extended and modified through 2032
- For **eligible contractors** of qualified new constructed/acquired energy efficient homes
- Credit increased to max $5,000, depending on which energy efficient and prevailing wage requirements are met
  - Previous max was $1,000-$2,000
- A dwelling unit qualifies for the credit **if it is certified** as a zero energy ready home under the zero energy ready home program (Dept. of Energy) and satisfies a set of requirements based on the type of home
- Effective for dwelling units acquired after 2022 and before 2033

Zero Energy Home Program Details

Learn more:
Energy Star – Federal Income Tax Credits and Incentives for Energy Efficiency

IRA of 2022: Energy Related Tax Credits

Residential Clean Energy Credit

Formerly "residential energy efficient property"

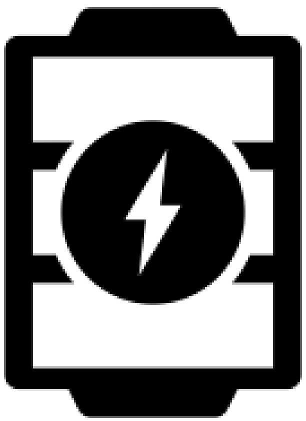
- Modified and extended through 2034, the Residential Energy Efficient Property Credit allows taxpayers to claim a credit for qualified residential energy efficient property purchases, while implementing the below phase-out:

  - through 2033, the credit is 30%
  - in 2033, the credit is 26%
  - in 2034, the credit is 22%

- Qualified property includes solar electric power, solar hot water, fuel cell, small wind energy, geothermal heat pump, and biomass fuel property

IRA of 2022: Energy Related Tax Credits

Residential Clean Energy Credit, continued…



- Battery storage with capacity of at least 3 kWh is now eligible for the credit, if installed in connection with a dwelling unit located in U.S. that is also used as a residency by the taxpayer
- The addition of qualified battery storage presents an opportunity for taxpayers to add battery storage to a previous project, incurred after 2022

Consolidated Appropriations Act, 2023

Overview

- Signed into law on 12/29/22
- This legislation is primarily a spending bill
- However, as is often the case with end of year spending bills, other items can be added, including tax provisions
- Each year, policymakers face a series of expiring tax provisions that are typically extended on a temporary basis…this year was a little different:
  - Expiring and phasing out of tax provisions ("Tax Extenders")
  - SECURE Act 2.0

Consolidated Appropriations Act, 2023

Expiring/Phasing out Tax Provisions

Research Expenditures (Section 174)

- Starting in 2022, research expenses are capitalized and amortized over five years rather than currently expensed
- With a half-year convention applying, this means that 90% of the current year research expenses will not be deducted in 2022
- There was discussion of delaying the effective date for these research expenses, but this did not end up in the Omnibus bill

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Consolidated Appropriations Act, 2023

Expiring/Phasing out Tax Provisions, continued…

Interest Expense Deduction (Section 163(j))

- As part of the TJCA, the deduction for interest expense was subject to a new limitation based on a taxpayer's Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA)
- Beginning in 2022, depreciation and amortization deductions were not added back as part of the calculation and now limits those deductions based on that taxpayer's Earnings Before Interest and Taxes (EBIT)
- This change will lower the amount of interest deducted in 2022

In general, Section 163(j) limitation is **not subject** to businesses with average annual gross receipts of $25 million or less in the previous three years

Consolidated Appropriations Act, 2023

Expiring/Phasing out Tax Provisions, continued…

Meals and Entertainment Expensing

- The TCJA limited businesses to only deducting, in general, 50% of business meals (and eliminated the deduction for entertainment expenses)
- The Consolidated Appropriations Act of 2021 (which contained several provisions to help businesses impacted by COVID-19) temporarily allowed 100% deductibility of business meals at restaurants for 2021 and 2022, although entertainment expenses remain nondeductible
- Beginning January 1, 2023, meal and entertainment deductions will revert to tax rules under TCJA
    - i.e. generally 50% deduction for business meals and entertainment expenses remain nondeductible

Consolidated Appropriations Act, 2023

Expiring/Phasing out Tax Provisions, continued…

Bonus Depreciation (Section 168(k))

- Another feature in the TCJA involved the “100% bonus depreciation”, bonus depreciation was scheduled to drop to 80% for additions placed in service **after December 31, 2022**
- In 2023, companies will only be able to deduct 80% of their investments in qualifying short-lived assets immediately, with the remaining 20% spread across the asset’s life
- Continued phase-out:
  - 2024 dropped to 60%
  - 2025 drops to 40%
  - 2026 phases out completely
- Section 179 expensing still available, however, consideration of tax bracket management is still an important planning opportunity

Example: Tax Bracket Management

Tax Rate	For Single Filers	For Married Individuals Filing Joint Returns	For Heads of Households
10%	$0 to $10,275	$0 to $20,550	$0 to $14,650
12%	$10,275 to $41,775	$20,550 to $83,550	$14,650 to $55,900
22%	$41,775 to $89,075	$83,550 to $178,150	$55,900 to $89,050
24%	$89,075 to $170,050	$178,150 to $340,100	$89,050 to $170,050
32%	$170,050 to $215,950	$340,100 to $431,900	$170,050 to $215,950
35%	$215,950 to $539,900	$431,900 to $647,850	$215,950 to $539,900
37%	$539,900 or more	$647,850 or more	$539,900 or more

Example: Tax Bracket Management

Fully Expense in Year 1						
	Year 1	Year 2	Year 3	Year 4	Year 5	**TOTAL**
Net Income	500,000	500,000	500,000	500,000	500,000	**2,500,000**
Depreciation	(500,000)	-	-	-	-	**(500,000)**
Net Taxable Income	-	500,000	500,000	500,000	500,000	**2,000,000**
Top Bracket	0%	35%	35%	35%	35%	
Fed Tax Liability	-	122,507	122,507	122,507	122,507	**490,028**

Expense in Year(s) 1-5						
	Year 1	Year 2	Year 3	Year 4	Year 5	**TOTAL**
Net Income	500,000	500,000	500,000	500,000	500,000	**2,500,000**
Depreciation	(100,000)	(100,000)	(100,000)	(100,000)	(100,000)	**(500,000)**
Net Taxable Income	400,000	400,000	400,000	400,000	400,000	**2,000,000**
Top Bracket	32%	32%	32%	32%	32%	
Fed Tax Liability	88,463	88,463	88,463	88,463	88,463	**442,315**

*Mindful of other provisions subject to AGI or TI thresholds and availability of other deductions and/or credit.

Consolidated Appropriations Act, 2023

SECURE Act 2.0

- The **Setting Every Community Up for Retirement Enhancement (*SECURE*) Act 2.0** builds on the SECURE Act, which was approved by Congress in 2019
- This is a broad-ranging bill designed to give savers more access and flexibility in retirement savings

Review the SECURE Act 2.0 section-by-section

Consolidated Appropriations Act, 2023

SECURE Act 2.0, continued…

Section 102: Modification of credit for small employer pension plan startup costs

- Under the original SECURE Act, employers could get a tax credit for up to 50% of their 401k plan startup costs
- Now, starting in 2023, businesses with up to 50 employees can receive a credit of **100% for administrative expenses**, up to an **annual cap of $5,000**, for the first 3 years of a plan
- There's also an additional tax credit for employers with up to 100 employees based on a percentage of the amount employers contribute, up to a per-employee cap of $1,000

Consolidated Appropriations Act, 2023

SECURE Act 2.0, continued…

Section 110: Treatment of student loan payments as elective deferrals for the purposes of matching contributions

- This section allows employees to receive matching contributions by reason of repaying their student loans
- It permits an employer to make matching contributions under a 401(k) plan, 403(b) plan, or SIMPLE IRA with respect to "qualified student loan payments"
- *"You pay your student debt, and we'll contribute to your 401(k)"*
- **Section 110** is effective for contributions made for plan years beginning after Dec. 31, 2023

Consolidated Appropriations Act, 2023

SECURE Act 2.0, continued…

Section 116: Allows additional non-elective contributions to SIMPLE plan

- **Current law** requires employers with SIMPLE plans to make employer contributions to employees of either 2% of compensation or 3% of employee elective deferral contributions
- **Section 116** permits an employer to make additional contributions to each employee of the plan in a uniform manner, provided that the contribution may not exceed the lesser of up to 10% of compensation or $5,000 (indexed)
- **Section 116** is effective for taxable years beginning after December 31, 2023

Consolidated Appropriations Act, 2023

SECURE Act 2.0, continued…

Section 121: Starter 401(k) plans offered for employers without a retirement plan

- **Permits** an employer that does not sponsor a retirement plan to offer a starter 401(k) plan (or safe harbor 403(b) plan)
- A starter 401(k) plan (or safe harbor 403(b) plan) would generally require that all employees be default enrolled in the plan at a 3% to 15% of compensation deferral rate
- The limit on annual deferrals would be the same as the IRA contribution limit, which for 2022 is $6,000 with an additional $1,000 in catch-up contributions beginning at age 50
- **Section 121** is effective for plan years beginning after December 31, 2023

Consolidated Appropriations Act, 2023

SECURE Act 2.0, continued…

Section 601: SIMPLE and SEP Roth IRAs

- Generally, all plans that allow pre-tax employee contributions are permitted to accept Roth contributions with one exception – SIMPLE IRAs
- 401(k), 403(b), and governmental 457(b) plans are allowed to accept Roth employee contributions
- **Section 601** allows SIMPLE IRAs to accept Roth employee contributions
- In addition, under current law, simplified employee pension plans (SEPs) can only accept employer money and not on a Roth basis
- **Section 601** allows employers to offer employees the ability to treat SEP contributions as Roth (in whole or in part)
- Amounts deferred into Roth SIMPLE IRAs or deposited by employers into SEP Roth IRAs will be taxable
- Effective for taxable years beginning after December 31, 2022

Consolidated Appropriations Act, 2023

SECURE Act 2.0, continued…

Section 604: **Optional** treatment of **employer** matching or non-elective contributions as **Roth contributions**

- Under current law, plan sponsors are not permitted to provide employer matching contributions in their 401(k), 403(b), and governmental 457(b) plans on a Roth basis
  - Matching contributions must be on a pre-tax basis only
- **Section 604** allows defined contribution plans to provide participants with the option of receiving matching contributions on a Roth basis, effective on the date of enactment of this Act
- Participants will be subject to income tax on such contributions

MA 63D Entity Level Tax (ELT)

- Effective for tax years beginning on or after January 1, 2021 (though was adopted September 2021)
- Allows pass-through entities, including S-Corporations, multi-member partnerships and certain trusts, to elect annually to be subject to Massachusetts pass-through entity excise tax (PTE Excise) at a rate of 5%, which is 100% deductible federally, and MA allows a refundable 90% credit of a qualified member's share

MA 63D Entity Level Tax (ELT)

Example:			No 63D ELT			Yes 63D ELT	Savings
S-Corp Tax Return (1120S) - Golden Girls S-Corporation (cash basis)							
Net income			225,000			225,000	
Less: MA 63D-ELT excise tax payment (paid in same year)			-		5%	(11,250)	
Taxable income			225,000			213,750	
Shareholder Tax Return (1040) - Dorothy & Stan Zbornak (MA resident, Married Filing Joint)							
Fed							
W-2 Wages			175,000			175,000	
Golden Girls S-Corporation pass-through income			225,000			213,750	
Adjusted gross income			400,000			388,750	
Less: Itemized deduction							
State and local taxes							
Real estate taxes	(7,000)			(7,000)			
State income taxes (paid via withholdings)	(8,750)			(8,750)			
State income taxes (paid via estimates)	(11,250)			-			
Total state and local taxes (limited $10k)	(27,000)	(10,000)		(15,750)	(10,000)		
Charitable contributions		(1,000)			(1,000)		
Mortgage interest		(16,000)			(16,000)		
Total itemized deduction		(27,000)	(27,000)		(27,000)	(27,000)	
Less: QBI deduction *		13%	(30,195)		16%	(33,495)	
Taxable income			342,805			328,255	
Tax & Tax Bracket **		**32%**	**70,161**		**24%**	**66,452**	**3,709**

* Qualified business income deduction max 20% of qualified business income; however, is subject to phaseout $340,100 to $440,100 (2022 married filing joint). Making a MA 63D ELT business expense can help lower taxable income increasing possible QBI benefit.

** The 2022 32% tax bracket begins at $340,101 for MFJ 2022. By making a MA 63D ELT payment in this example, it also helped lower taxable income putting the taxpayer in the lower 24% tax bracket.

MA 63D Entity Level Tax (ELT)

Example:		No 63D ELT		Yes 63D ELT	Savings
Shareholder Tax Return (1040) - Dorothy & Stan Zbornak (MA resident, Married Filing Joint)					
MA					
W-2 Wages		175,000		175,000	
Golden Girls S-Corporation pass-through income		225,000		213,750	
Add: MA 63D ELT excise tax				11,250	
Total income		400,000		400,000	
Less: SS, Medicare, MA Retirement deduction - taxpayer		(2,000)		(2,000)	
Less: SS, Medicare, MA Retirement deduction - spouse		(2,000)		(2,000)	
Less: Personal exemptions		(8,800)		(8,800)	
Taxable income		387,200		387,200	
Tax	5%	19,360	5%	19,360	
MA taxes paid					
W-2 withholdings		(8,750)		(8,750)	
Estimated taxes		(11,250)		-	
Credit for 90% of MA 63D-ELT tax		-		(10,125)	
Tax Due (refund)		**(640)**		**485**	**(1,125)**
Total Savings					
Fed tax savings					3,709
MA 10% of 63D ELT tax withheld by state					(1,125)
Total savings					**2,584**

MA 63D Entity Level Tax (ELT)

CAUTION

- The law expires if the federal state and local tax ("SALT") deduction ($10k) limit expires or is repealed
  - Important to keep in mind in future federal legislation

- 63D ELT is flat 5% based on the business' taxable income; however if you're personal income tax is subject to:
  - new additional 4% MA $1 millionaire surtax tax,
  - 12% MA short term cap gains tax, or
  - have significant income other than pass-through business income
    - e.g. investment income, Schedule C income, etc.
- Consider how/when you'll pay the difference
  - e.g. quarterly estimates vs. 4/15 balance due

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MA 63D Entity Level Tax (ELT)

How do you do this?

Learn more:
[MA 63D ELT]

1. Log into the qualified pass-through entity's MA Tax Connect account, add a 63D tax account, make quarterly estimated 63D payments (for the desired tax year)
2. File (for S-Corp example) Form 355S, make an annual voluntary election to pay MA 63D ELT tax (on Schedule S), file Form 63D-ELT showing the calculation of the tax and amount paid, and report each qualified shareholder's credit on shareholder's MA SK-1
3. Then the shareholder files MA Form 1 and reports their share of the credit on Schedule CMS

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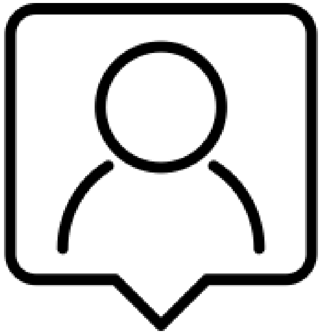
MA "Millionaires' Tax"

- Effective 1/1/23
- 4% flat rate surtax (adjusted for inflation) on portion of annual taxable income per return that exceeds $1 million
  - This is on top of the state's current 5% flat income tax (12% short term cap gains tax)



Example

✓ Massachusetts resident earns $2 million in 2023
   ➢ From ordinary income or long term capital gain

✓ Will pay 5% tax on the first million ($50,000)

✓ Will pay 9% tax (5% + 4%) on the second million ($90,000)

✓ Totaling $140,000 in tax

MA "Millionaires' Tax"

CAUTION

- The $1 million applies to "per tax return"
  - If a married couple would exceed the $1 million threshold based on their combined income but not on their separate incomes, the couple should consider filing tax returns as married filing separately to avoid the surtax
- Applies to one-time millionaires
  - A Massachusetts taxpayer may be subject to the surtax in one year but not another if they recognize a significant gain from the sale of a substantially appreciated asset such as a home or business

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MA "Millionaires' Tax"

CAUTION

- Spreading income
  - If you're selling an asset at a significant taxable gain, then consider an installment sale to spread the gain over multiple years

- Change in residency
  - Taxpayers should not do so without due diligence and reviewing all factors that determine when residency has changed, and consider future impact of tax planning
    - It has been common for states to question changes in residency where sole intent was to reduce tax liabilities
  - State budgets in crisis
    - Health care costs rising/Medicaid, state pension obligations, and shrinking tax revenue

Lean more: [Changing Your MA Residency]

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