Form **4562**

Department of the Treasury
Internal Revenue Service

Depreciation and Amortization
(Including Information on Listed Property)
Attach to your tax return.
Go to *www.irs.gov/Form4562* for instructions and the latest information.

OMB No. 1545-0172
2025
Attachment Sequence No. **179**

Name(s) shown on return	Business or activity to which this form relates	Identifying number

Part I **Election To Expense Certain Property Under Section 179**
Note: If you have any listed property, complete Part V before you complete Part I.

1	Maximum amount (see instructions)	1	
2	Total cost of section 179 property placed in service (see instructions)	2	
3	Threshold cost of section 179 property before reduction in limitation (see instructions)	3	
4	Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	

Federal Tax Update – Individual & Business Current Developments

i Residential rental property			27.5 yrs.	MM	S/L	
			27.5 yrs.	MM	S/L	
j Nonresidential real property			39 yrs.	MM	S/L	
				MM	S/L	
Section C—Assets Placed in Service During 2025 Tax Year Using the Alternative Depreciation System						
20a Class life					S/L	
b 12-year			12 yrs.		S/L	
c 30-year			30 yrs.	MM	S/L	
d 40-year			40 yrs.	MM	S/L	
e 50-year			50 yrs.	MM	S/L	

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 12906N Form **4562** (2025) Created 5/13/25

Federal Tax Update – Individual & Business Current Developments

Learning Objectives

Once participants have completed this session, they should be able to:

- Understand the major Federal income tax laws impacting individuals, C and S corporations, partnerships, LLCs and LLPs
- Identify and comprehend any newly enacted legislation, changes and IRS guidance affecting individual and business income tax returns

NOTE – Click here for Federal Tax Update – Individual & Business Current Developments (i.e., FTCD) course description and learning objectives.

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Chapter Index

Federal Tax Update – Individual Current Developments .... Chapter 1

Federal Tax Update – Business Current Developments .... Chapter 2

Summary Tables & Recent Legislation............ Chapter 3

Appendix TF – Tax Forms .... Appendix TF

NOTE – To download a copy of **Pat Garverick's Quick Reference Chart (QRC)** click here **or** go to www.TheTaxU.com, under the Links & Downloads tab, go to Participant Downloads section (gray area), click on + to the right of the Class Files, click on QRC to open PDF, print and/or save PDF file to computer. To see if you have the most up to date QRC, look at the date on the cover page.

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Federal Tax Update – Individual Current Developments

Table of Contents

Filing Status & Exemptions **4**
Background & Repeal of Exemptions 4
Exemptions for Dependents (§152) 5
Release of Claim by Custodial Parent (§1.152-4) 6

Gross Income & Exclusions **9**
Gross Income Defined & Exclusions 9
IRS extends relief to provides drought-stricken farmers, ranchers more time to replace livestock (Notice 2025-52) 11
Virtual Currency & Digital Assets 13
Damages Paid Were Not for Physical Injury (§104(a)(2)) 17

Trade or Business (Sole Proprietor) Issues **18**
IRC §162 Background & Rental Properties 18
Home Office Deduction (§280A(c)) 21
Deductible Transportation Expenses (Rev. Rul. 99-7) 23
Hobby Loss Rules (§183(c)) 24

Schedule E – Rentals & Passive Activities **25**
Material Participation 25
Real Estate Professionals (REP) Exception to PAL Rules (§469(c)(7) & §1.469-9)) 27
REP IRS Guidance & Cases 30

Individual Retirement Accounts (IRAs) Issues **32**
SEP Contribution & Deduction Limits 32
SIMPLE IRA Plan Contribution & Deduction Limits 34
10% Additional Tax & Exceptions to Early Distributions from Qualified Retirement Plans (§72(t)) 40
Excise Tax on Certain Accumulations in Qualified Retirement Accounts 42
Required Distributions Background (§401(a)(9)) 43
RMD for IRA Beneficiaries Summary Chart – Death After 2019 45
RMD Final Regulations Issued 46

Deductions & Adjustments **47**
Basic Standard Deduction (§63(c)(2) & (7)) 47
Additional Standard Deductions 47
Standard Deduction for Dependents (§63(c)(5)) 48
Overall Limitation on Itemized Deductions (§68) 49
Medical & Dental Expenses (§213(a)) 50
Table – Summary of Deductible & Non-Deductible Medical & Dental Expenses 51
Deductible Taxes & SALT Limitations 52
Home Mortgage Interest (§163(h)) 55
Premiums for Mortgage Insurance (PMI) 59
Charitable Contributions (§170) - Deduction Allowance & AGI Limitations 60
Casualty & Loss Limitations for Individuals 65
Miscellaneous Itemized Deductions NOT Subject to the 2% of AGI Limitation 68
Self Employed Health Insurance Deduction (§162(l)) 71
Health Savings Accounts (HSAs) 73

One Big Beautiful Bill Temporary Adjustments **77**
Deduction for Seniors (2025-2028) 77
Deduction for Qualified Tips (No Tax On Tips) (2025-2028) 78
No Tax on Overtime (2025-2028) 80
Qualified Passenger Vehicle Loan Interest (2025-2028) 81

Individual Taxes **83**
Individual, Estates & Trust Income Tax Rates (§1) 83
Long-Term Capital Gain (LTCG) & Qualified Dividend Rates 84
28% LTCG Rate – Collectibles & §1202 Gains 84
25% LTCG Rate – Unrecaptured §1250 Gain 87
20%, 15 or 0% LTCG Rate – All Other LTCGs & Qualified Dividends 87
Kiddie Tax 88
Alternative Minimum Tax (AMT) – Modifications (2018-2025) 90
Self-Employment Tax (Schedule SE) 92
Additional 0.9% H.I. Tax on Employee Portion High-Income Taxpayers 93
Net Investment Income Tax (§1411) 95
Calculation of Net Investment Income in Special Situations (§1.1411-4(g)) 97
Household Employment Taxes (Schedule H) 99
Installment Payment of Tax on Gain from Sale of Qualified Farmland to Qualified Farmers (§1062) 101

Individual Credits **102**
Child & Dependent Care Expenses Credit (§21) 102
American Opportunity vs. Lifetime Learning Credit Chart 105
Child Tax Credit (CTC) & Other Dependents Credit (ODC) (§24) 106
Premium Assistance Tax Credit (§36B) 108

Foreign Account Compliance **115**
Report of Foreign Bank & Financial Accounts (FBAR) 115
Disclosure of Information with Respect to Foreign Financial Assets (§6038D) 117
Form 8938 & FBAR Comparison Charts 121

Miscellaneous Topics **125**
Charitable Conservation Easement & Listed Transactions 125
Chevron Case Overturned (Loper Bright Enterprises) 127
Regulations Post Loper Bright Enterprises 129

Filing Status & Exemptions

Background & Repeal of Exemptions

Exemptions (§151)

There are two types of exemption deductions:

1. personal exemptions AND
2. exemptions for dependents.

NOTE – While each exemption is worth the same amount, different rules apply to each type.

For each exemption the taxpayer is allowed an additional deduction of:

Year	Exemption
2017	$4,050
Post 2017	$0

Phase-Out of Exemptions (Pre-2018)

The amount a taxpayer claimed as a deduction for exemptions is phased out once their adjusted gross income (AGI) exceeds certain levels based on the taxpayer's filing status. Taxpayers must reduce the dollar amount of their exemptions by 2% for each $2,500, or part of $2,500 ($1,250 if married filing separately) that their AGI exceeds the amount shown below for their filing status. If their AGI exceeds the amount shown by more than $122,500 ($61,250 if married filing separately) the amount of the deduction for exemptions is reduced to zero.

Filing Status	2017 Exemption Phase-Out Range	
	Beginning AGI	**Ending AGI**
Single	$261,500	$384,000
Married Filing Jointly	$313,800	$436,300
Married Filing Separately	$156,900	$218,150
Head of Household	$287,650	$410,150

Exemption Eliminated after 2017 (§151(d)(5))

UPDATE – The OBBB permanently eliminates the personal exemption deduction for most taxpayers. However, it introduces a new temporary deduction specifically for seniors.

In the case of a taxable year beginning after December 31, 2017, the term "exemption amount" means zero.

NOTE - §151(d)(5)(B) states: "For purposes of any other provision of this title, the reduction of the exemption amount to zero shall not be taken into account in determining whether a deduction is allowed or allowable, or whether a taxpayer is entitled to a deduction, under this section."

Exemptions for Dependents (§152)

Dependent Defined

Under IRC §152, a taxpayer is allowed one exemption for each person that they can claim as a dependent. A taxpayer can claim an exemption for a dependent even if the taxpayer's dependent files a return. The term "dependent" means:

1. a qualifying child OR
2. a qualifying relative.

Tests To Be a Qualifying Child (§152(c))	Tests To Be a Qualifying Relative (§152(d))
1. The child must be your son, daughter, stepchild, foster child, brother, sister, half brother, half sister, stepbrother, stepsister, or a descendant of any of them.	1. The person cannot be your qualifying child or the qualifying child of any other taxpayer.
2. The child must be (a) under age 19 at the end of the year, (b) under age 24 at the end of the year and a full-time student, or (c) any age if permanently and totally disabled.	2. The person either (a) must be related to you in one of the ways listed under *Relatives who do not have to live with you*, or (b) must live with you all year as a member of your household[2] (and your relationship must not violate local law).
3. The child must have lived with you for more than half of the year.[2]	3. The person's gross income for the year must be less than exemption amount (i.e., **$5,100 for 2025**).[3]
4. The child must not have provided more than half of his or her own support for the year.	4. You must provide more than half of the person's total support for the year.[4]
5. The child is not filing a joint return for the year (unless that return is filed only as a claim for refund). **NOTE -** If the child meets the rules to be a qualifying child of more than one person, only one person is entitled to claim the child as a qualifying child.	

[1] There is an exception for certain adopted children.
[2] There are exceptions for temporary absences, children who were born or died during the year, children of divorced or separated parents, and kidnapped children.
[3] There is an exception if the person is disabled and has income from a sheltered workshop.
[4] There are exceptions for multiple support agreements, children of divorced or separated parents, and kidnapped children. See regulation §1.152-4.

Qualifying Child of More than One Person (§152(c)(4))

There are three special rules relating to 2 or more persons who can claim the same qualifying child:

1. **General rule -** if an individual may be claimed as a qualifying child by 2 or more taxpayers for a taxable year beginning in the same calendar year, such individual shall be treated as the qualifying child of the taxpayer who is:
    a. a parent of the individual
    OR
    b. if no parent "may" claim the child, the taxpayer with the highest adjusted gross income for such taxable year.

2. **More than 1 parent claiming qualifying child -** If the parents claiming any qualifying child do not file a joint return together, such child shall be treated as the qualifying child of:
    a. the parent with whom the child resided for the longest period of time during the taxable year, OR
    b. if the child resides with both parents for the same amount of time during such taxable year, the parent with the highest adjusted gross income.

3. **No parent claiming qualifying child -** If the parents of an individual "may" claim such individual as a qualifying child but no parent so claims the individual, such individual may be claimed as the qualifying child of another taxpayer but only if the adjusted gross income of such taxpayer is higher than the highest adjusted gross income of any parent of the individual.

Release of Claim by Custodial Parent (§1.152-4)

EFFECTIVE DATE – The §1.152-4 regulations apply to taxable years beginning after July 2, 2008.

Release of Claim by Custodial Parent (§1.152-4(b))

In general, a child is treated as the qualifying child or qualifying relative of the noncustodial parent if the following two requirements are met:

Requirement #1 - Support, Custody & Parental Status

The requirements of this paragraph are met if:

1. the parents of the child provide over one-half of the child's support for the calendar year,
2. the child is in the custody of one or both parents for more than one-half of the calendar year AND
3. the parents:
    a. Are divorced or legally separated under a decree of divorce or separate maintenance;
    b. Are separated under a written separation agreement; OR
    c. Live apart at all times during the last 6 months of the calendar year whether or not they are or were married.

NOTE – The requirements above are not met if over one-half of the support of the child is treated as having been received from a taxpayer under the multiple support agreements of §152(d)(3).

Requirement #2 - Release of Claim to Child

The requirements of this paragraph are met for a calendar year if:

1. The custodial parent signs a written declaration that the custodial parent will not claim the child as a dependent for any taxable year beginning in that calendar year and the noncustodial parent attaches the declaration to the noncustodial parent's return for the taxable year OR
2. A qualified pre-1985 instrument, as defined in §152(e)(3)(B), applicable to the taxable year beginning in that calendar year, provides that the noncustodial parent is entitled to the dependency exemption for the child and the noncustodial parent provides at least $600 for the support of the child during the calendar year.

Custody Defined (§1.152-4(c))

A child is in the custody of one or both parents for more than one-half of the calendar year if one or both parents have the right under state law to physical custody of the child for more than one-half of the calendar year.

Custodial Parent (§1.152-4(d))

General Rule

The custodial parent is the parent with whom the child resides for the greater number of nights during the calendar year, and the noncustodial parent is the parent who is not the custodial parent. A child is treated as residing with neither parent if the child is emancipated under state law. A child resides with a parent for a night if the child sleeps:

1. At the residence of that parent (whether or not the parent is present); OR
2. In the company of the parent, when the child does not sleep at a parent's residence (for example, the parent and child are on vacation together).

Night Straddling Taxable Years

A night that extends over two taxable years is allocated to the taxable year in which the night begins.

Absences

A child who does not reside with a parent for a night is treated as residing with the parent with whom the child would have resided for the night but for the absence. A child who does not reside with a parent for a night is treated as not residing with either parent for that night if it cannot be determined with which parent the child would have resided or if the child would not have resided with either parent for the night.

Special rule for equal number of nights

If a child is in the custody of one or both parents for more than one-half of the calendar year and the child resides with each parent for an equal number of nights during the calendar year, the parent with the higher adjusted gross income for the calendar year is treated as the custodial parent.

Exception for a parent who works at night

If, in a calendar year, due to a parent's nighttime work schedule, a child resides for a greater number of days but not nights with the parent who works at night, that parent is treated as the custodial parent. On a school day, the child is treated as residing at the primary residence registered with the school.

Written Declaration (§1.152-4(e))

The written declaration must be an unconditional release of the custodial parent's claim to the child as a dependent for the year or years for which the declaration is effective. A declaration is not unconditional if the custodial parent's release of the right to claim the child as a dependent requires the satisfaction of any condition, including the noncustodial parent's meeting of an obligation such as the payment of support. A written declaration must name the noncustodial parent to whom the exemption is released. A written declaration must specify the year or years for which it is effective. A written declaration that specifies all future years is treated as specifying the first taxable year after the taxable year of execution and all subsequent taxable years.

Form designated by IRS:

- A written declaration may be made on *Form 8332 - Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent*, or conforming document.
- A court order or decree or a separation agreement may not serve as a written declaration.

Attachment to return

A noncustodial parent must attach a copy of the written declaration to the parent's return for each taxable year in which the child is claimed as a dependent.

Revocation of written declaration

A parent may revoke a written declaration by providing written notice of the revocation to the other parent. The parent revoking the written declaration must make reasonable efforts to provide actual notice to the other parent. The revocation may be effective no earlier than the taxable year that begins in the first calendar year after the calendar year in which the parent revoking the written declaration provides, or makes reasonable efforts to provide, the written notice.

Form of revocation:

- A written declaration may be made on *Form 8332 - Release/Revocation of Release of Claim to Exemption for Child by Custodial Parent*, or conforming document.
- The revocation must specify the year or years for which the revocation is effective.
- A revocation that specifies all future years is treated as specifying the first taxable year after the taxable year the revocation is executed and all subsequent taxable years.

Attachment to return:

The parent revoking the written declaration must attach a copy of the revocation to the parent's return for each taxable year for which the parent claims a child as a dependent as a result of the revocation. The parent revoking the written declaration must keep a copy of the revocation and evidence of delivery of the notice to the other parent, or of the reasonable efforts to provide actual notice.

Ineffective declaration or revocation

A written declaration or revocation that fails to satisfy the above requirements has no effect.

Coordination with other sections

If §152(e) and this section apply, a child is treated as the dependent of both parents for purposes of

1. §105(b) – amounts expended for medical care,
2. §132(h)(2)(B) – fringe benefits, and
3. §213(d)(5) – medical and dental expenses.

Gross Income & Exclusions

Gross Income Defined & Exclusions

Gross Income Defined (§61)

Except as otherwise provided in the IRC, gross income means all income from whatever source derived, including (but not limited to) the following items:

- Compensation for services, including fees, commissions, fringe benefits, and similar items;
- Gross income derived from business;
- Gains derived from dealings in property;
- Interest;
- Rents;
- Royalties;
- Dividends;
- Alimony and separate maintenance payments;
- Annuities;
- Income from life insurance and endowment contracts;
- Pensions;
- Income from discharge of indebtedness;
- Distributive share of partnership gross income;
- Income in respect of a decedent; AND
- Income from an interest in an estate or trust.

NOTE – Gross income means all income from whatever source derived, unless excluded by law. Gross income includes income realized in any form, whether in money, property, or services. Income may be realized, therefore, in the form of services, meals, accommodations, stock, or other property, as well as in cash. (§1.61-1)

Service Income Defined (§1.61-2(a))

Wages, salaries, commissions paid salesmen, compensation for services on the basis of a percentage of profits, commissions on insurance premiums, tips, bonuses (including Christmas bonuses), termination or severance pay, rewards, jury fees, marriage fees and other contributions received by a clergyman for services, pay of persons in the military or naval forces of the United States, retired pay of employees, pensions, and retirement allowances are income to the recipients unless excluded by law.

Compensation Paid other than in Cash (§1.61-2(d))

Compensated With Property

If services are paid for in property, the fair market value of the property taken in payment must be included in income as compensation.

Compensated With Services

If services are paid for in exchange for other services, the fair market value of such other services taken in payment must be included in income as compensation. If the services are rendered at a stipulated price, such price will be presumed to be the fair market value of the compensation received in the absence of evidence to the contrary.

Income Excludable from Gross Income

Income items specifically excluded from gross income are listed in IRC §101 through §139. Some of the items excludable are:

1. Certain death benefits (§101)
2. Gifts and inheritances (§102)
3. Interest on State and local bonds (§103)
4. Compensation for injuries or sickness (§104)
5. Amounts received under accident and health plans (§105)
6. Contributions by employer to accident and health plans (§106)
7. Rental value of parsonages (§107)
8. Income from discharge of indebtedness (§108)
9. Improvements by lessee on lessor's property (§109)
10. Qualified lessee construction allowances for short-term leases (§110)
11. Recovery of tax benefit items (§111)
12. Certain combat zone compensation of members of the Armed Forces (§112)
13. Income of states, municipalities, etc. (§115)
14. Qualified scholarships (§117)
15. Contributions to the capital of a corporation (§118)
16. Meals or lodging furnished for the convenience of the employer (§119)
17. Amounts received under qualified group legal services plans (§120)
18. Exclusion of gain from sale of principal residence (§121)
19. Certain reduced uniformed services retirement pay (§122)
20. Amounts received under insurance contracts for certain living expenses (§123)
21. Cafeteria plans (§125)
22. Certain cost-sharing payments (§126)
23. Educational assistance programs (§127)
24. Dependent care assistance programs (§129)
25. Certain personal injury liability assignments (§130)
26. Certain foster care payments (§131)
27. Certain fringe benefits (§132)
28. Certain military benefits (§134)
29. Income from United States savings bonds used to pay higher education tuition and fees (§135)
30. Energy conservation subsidies provided by public utilities (§136)
31. Adoption assistance programs (§137)
32. Medicare Advantage MSA (§138)
33. Disaster relief payments (§139)
34. Federal subsidies for prescription drug plans (§139A)
35. Benefits provided to volunteer firefighters and emergency medical responders (§139B)
36. COBRA premium assistance (§139C)
37. Indian health care benefits (§139D)
38. Indian general welfare benefits (§139E)
39. Certain amounts received by wrongfully incarcerated individuals (§139F)

IRS extends relief to provides drought-stricken farmers, ranchers more time to replace livestock (Notice 2025-52)

Nonrecognition of Gain on Involuntary Conversion of Livestock

§1033(a) generally provides for nonrecognition of gain when property is involuntarily converted and replaced with property that is similar or related in service or use. §1033(e)(1) provides that a sale or exchange of livestock (other than poultry) held by a taxpayer for draft, breeding, or dairy purposes in excess of the number that would be sold following the taxpayer's usual business practices is treated as an involuntary conversion if the livestock is sold or exchanged solely on account of drought, flood, or other weather-related conditions.

Replacement Period

§1033(a)(2)(A) generally provides that gain from an involuntary conversion is recognized only to the extent the amount realized on the conversion exceeds the cost of replacement property purchased during the replacement period. If a sale or exchange of livestock is treated as an involuntary conversion under §1033(e)(1) and is solely on account of drought, flood, or other weather-related conditions that result in the area being designated as eligible for assistance by the federal government, §1033(e)(2)(A) provides that the replacement period ends four years after the close of the first taxable year in which any part of the gain from the conversion is realized. §1033(e)(2)(B) provides that the Secretary may extend this replacement period on a regional basis for such additional time as the Secretary determines appropriate if the weather-related conditions that resulted in the area being designated as eligible for assistance by the federal government continue for more than three years. §1033(e)(2) is effective for any taxable year with respect to which the due date (without regard to extensions) for a taxpayer's return is after December 31, 2002.

Extension of Replacement Periods (Notice 2006-82)

Notice 2006-82, provides for extensions of the replacement period under §1033(e)(2)(B). If a sale or exchange of livestock is treated as an involuntary conversion on account of drought and the taxpayer's replacement period is determined under §1033(e)(2)(A), the replacement period will be extended under §1033(e)(2)(B) and Notice 2006-82 until the end of the taxpayer's first taxable year ending after the first drought-free year for the applicable region. For this purpose, the first drought-free year for the applicable region is the first 12-month period that:

1. ends August 31;
2. ends in or after the last year of the taxpayer's four-year replacement period determined under §1033(e)(2)(A); and
3. does not include any weekly period for which exceptional, extreme, or severe drought is reported for any location in the applicable region.

NOTE – The applicable region is the county that experienced the drought conditions on account of which the livestock was sold or exchanged and all counties that are contiguous to that county. A taxpayer may determine whether exceptional, extreme, or severe drought is reported for any location in the applicable region by reference to U.S. Drought Monitor maps that are produced on a weekly basis by the National Drought Mitigation Center. U.S. Drought Monitor maps are archived at https://droughtmonitor.unl.edu/Maps/MapArchive.aspx.

In addition, Notice 2006-82 provides that the IRS will publish in September of each year a list of counties for which exceptional, extreme, or severe drought was reported during the preceding 12 months. Taxpayers may use this list instead of U.S. Drought Monitor maps to determine whether exceptional, extreme, or severe drought has been reported for any location in the applicable region.

The Appendix to this notice contains the list of counties for which exceptional, extreme, or severe drought was reported during the 12-month period ending August 31, 2024. Under Notice 2006-82, the 12-month period ended on August 31, 2024, is not a drought-free year for an applicable region that includes any county on this list. Accordingly, for a taxpayer who qualified for a four-year replacement period for livestock sold or exchanged on account of drought and whose replacement period is scheduled to expire at the end of 2024 (or, in the case of a fiscal year taxpayer, at the end of the taxable year that includes August 31, 2024), the replacement period will be extended under §1033(e)(2) and Notice 2006-82 if the applicable region includes any county on this list. This extension will continue until the end of the taxpayer's first taxable year ending after a drought-free year for the applicable region.

NOTE – More information on reporting drought sales and other farm-related tax issues can be found in *Publication 225, Farmer's Tax Guide*.

Virtual Currency & Digital Assets

Virtual Currency Background

Virtual currency is a digital representation of value, other than a representation of the U.S. dollar or a foreign currency ("real currency"), that functions as a unit of account, a store of value, and a medium of exchange. Some virtual currencies are convertible, which means that they have an equivalent value in real currency or act as a substitute for real currency. The IRS uses the term "virtual currency" in these FAQs to describe the various types of convertible virtual currency that are used as a medium of exchange, such as digital currency and cryptocurrency. Regardless of the label applied, if a particular asset has the characteristics of virtual currency, it will be treated as virtual currency for Federal income tax purposes.

Virtual currency is treated as property and general tax principles applicable to property transactions apply to transactions using virtual currency. See Notice 2014-21 frequently asked questions below.

Virtual Currency Frequently Asked Questions (Notice 2014-21)

NOTE – Notice 2014-21 describes how existing general tax principles apply to transactions using virtual currency. The notice provides this guidance in the form of answers to frequently asked questions.

Q&A 1 – How is virtual currency treated for federal tax purposes?
For federal tax purposes, virtual currency is treated as property. General tax principles applicable to property transactions apply to transactions using virtual currency.

Q&A 2 – Is virtual currency treated as currency for purposes of determining whether a transaction results in foreign currency gain or loss under U.S. federal tax laws?
No. Under currently applicable law, virtual currency is not treated as currency that could generate foreign currency gain or loss for U.S. federal tax purposes.

Q&A 3 – Must a taxpayer who receives virtual currency as payment for goods or services include in computing gross income the fair market value of the virtual currency?
Yes. A taxpayer who receives virtual currency as payment for goods or services must, in computing gross income, include the fair market value of the virtual currency, measured in U.S. dollars, as of the date that the virtual currency was received.

Q&A 4 – What is the basis of virtual currency received as payment for goods or services in Q&A-3?
The basis of virtual currency that a taxpayer receives as payment for goods or services in Q&A-3 is the fair market value of the virtual currency in U.S. dollars as of the date of receipt.

Q&A 5 – How is the fair market value of virtual currency determined?
For U.S. tax purposes, transactions using virtual currency must be reported in U.S. dollars. Therefore, taxpayers will be required to determine the fair market value of virtual currency in U.S. dollars as of the date of payment or receipt. If a virtual currency is listed on an exchange and the exchange rate is established by market supply and demand, the fair market value of the virtual currency is determined by converting the virtual currency into U.S. dollars (or into another real currency which in turn can be converted into U.S. dollars) at the exchange rate, in a reasonable manner that is consistently applied.

Q&A 6 – Does a taxpayer have gain or loss upon an exchange of virtual currency for other property?

Yes. If the fair market value of property received in exchange for virtual currency exceeds the taxpayer's adjusted basis of the virtual currency, the taxpayer has taxable gain. The taxpayer has a loss if the fair market value of the property received is less than the adjusted basis of the virtual currency.

Q&A 7 – What type of gain or loss does a taxpayer realize on the sale or exchange of virtual currency?

The character of the gain or loss generally depends on whether the virtual currency is a capital asset in the hands of the taxpayer. A taxpayer generally realizes capital gain or loss on the sale or exchange of virtual currency that is a capital asset in the hands of the taxpayer. For example, stocks, bonds, and other investment property are generally capital assets. A taxpayer generally realizes ordinary gain or loss on the sale or exchange of virtual currency that is not a capital asset in the hands of the taxpayer. Inventory and other property held mainly for sale to customers in a trade or business are examples of property that is not a capital asset.

Q-8: Does a taxpayer who "mines" virtual currency (for example, uses computer resources to validate Bitcoin transactions and maintain the public Bitcoin transaction ledger) realize gross income upon receipt of the virtual currency resulting from those activities?

Yes, when a taxpayer successfully "mines" virtual currency, the fair market value of the virtual currency as of the date of receipt is includible in gross income.

Q&A 9 – Is an individual who "mines" virtual currency as a trade or business subject to self-employment tax on the income derived from those activities?

If a taxpayer's "mining" of virtual currency constitutes a trade or business, and the " mining" activity is not undertaken by the taxpayer as an employee, the net earnings from self-employment (generally, gross income derived from carrying on a trade or business less allowable deductions) resulting from those activities constitute self-employment income and are subject to the self-employment tax.

Q&A 10 – Does virtual currency received by an independent contractor for performing services constitute self-employment income?

Yes. Generally, self-employment income includes all gross income derived by an individual from any trade or business carried on by the individual as other than an employee. Consequently, the fair market value of virtual currency received for services performed as an independent contractor, measured in U.S. dollars as of the date of receipt, constitutes self-employment income and is subject to the self-employment tax.

Q&A 11 – Does virtual currency paid by an employer as remuneration for services constitute wages for employment tax purposes?

Yes. Generally, the medium in which remuneration for services is paid is immaterial to the determination of whether the remuneration constitutes wages for employment tax purposes. Consequently, the fair market value of virtual currency paid as wages is subject to federal income tax withholding, Federal Insurance Contributions Act (FICA) tax, and Federal Unemployment Tax Act (FUTA) tax and must be reported on Form W-2, Wage and Tax Statement.

Q&A 12 –Is a payment made using virtual currency subject to information reporting?
A payment made using virtual currency is subject to information reporting to the same extent as any other payment made in property. For example, a person who in the course of a trade or business makes a payment of fixed and determinable income using virtual currency with a value of $600 or more to a U.S. non-exempt recipient in a taxable year is required to report the payment to the IRS and to the payee. Examples of payments of fixed and determinable income include rent, salaries, wages, premiums, annuities, and compensation.

Q&A 13 – Is a person who in the course of a trade or business makes a payment using virtual currency worth $600 or more to an independent contractor for performing services required to file an information return with the IRS?
Generally, a person who in the course of a trade or business makes a payment of $600 or more in a taxable year to an independent contractor for the performance of services is required to report that payment to the IRS and to the payee on Form 1099-MISC, Miscellaneous Income. Payments of virtual currency required to be reported on Form 1099-MISC should be reported using the fair market value of the virtual currency in U.S. dollars as of the date of payment. The payment recipient may have income even if the recipient does not receive a Form 1099-MISC.

Q&A 14 – Are payments made using virtual currency subject to backup withholding?
Payments made using virtual currency are subject to backup withholding to the same extent as other payments made in property. Therefore, payors making reportable payments using virtual currency must solicit a taxpayer identification number (TIN) from the payee.

NOTE – The payor must backup withhold from the payment if a TIN is not obtained prior to payment or if the payor receives notification from the IRS that backup withholding is required.

Q&A 15 – Are there IRS information reporting requirements for a person who settles payments made in virtual currency on behalf of merchants that accept virtual currency from their customers?
Yes, if certain requirements are met. In general, a third party that contracts with a substantial number of unrelated merchants to settle payments between the merchants and their customers is a third party settlement organization (TPSO). A TPSO is required to report payments made to a merchant on a Form 1099-K, Payment Card and Third Party Network Transactions, if, for the calendar year, both (1) the number of transactions settled for the merchant exceeds 200, and (2) the gross amount of payments made to the merchant exceeds $20,000. When completing Boxes 1, 3, and 5a-1 on the Form 1099-K, transactions where the TPSO settles payments made with virtual currency are aggregated with transactions where the TPSO settles payments made with real currency to determine the total amounts to be reported in those boxes. When determining whether the transactions are reportable, the value of the virtual currency is the fair market value of the virtual currency in U.S. dollars on the date of payment.

Q&A 16 – Will taxpayers be subject to penalties for having treated a virtual currency transaction in a manner that is inconsistent with this notice prior to March 25, 2014?
Taxpayers may be subject to penalties for failure to comply with tax laws. For example, underpayments attributable to virtual currency transactions may be subject to penalties, such as accuracy-related penalties under §6662. In addition, failure to timely or correctly report virtual currency transactions when required to do so may be subject to information reporting penalties under §6721 and §6722. However, penalty relief may be available to taxpayers and persons required to file an information return who are able to establish that the underpayment or failure to properly file information returns is due to reasonable cause.

IRS Website

Digital Assets Defined

Digital assets are broadly defined as any digital representation of value which is recorded on a cryptographically secured distributed ledger or any similar technology as specified by the Secretary. Digital assets are any digital representation of value that may function as a medium of exchange, a unit of account, and/or a store of value. Digital assets may include (but not limited to):

1. Convertible virtual currency and cryptocurrency
2. Stablecoins such as Tether and USD Coin (USDC)
3. Non-fungible tokens (NFTs)

- Digital assets are not real currency (also known as "fiat") because they are not the coin and paper money of the United States or a foreign country and are not digitally issued by a government's central bank.
- A digital asset that has an equivalent value in real currency, or acts as a substitute for real currency, has been referred to as convertible virtual currency.
- A cryptocurrency is an example of a convertible virtual currency that can be used as payment for goods and services, digitally traded between users, and exchanged for or into real currencies or digital assets.

Tax Consequences

Transactions involving a digital asset are generally required to be reported on a tax return. Taxable income, gain or loss may result from transactions including, but not limited to:

- Sale of a digital asset for fiat
- Exchange of a digital asset for property, goods, or services
- Exchange or trade of one digital asset for another digital asset
- Receipt of a digital asset as payment for goods or services
- Receipt of a new digital asset as a result of a hard fork
- Receipt of a new digital asset as a result of mining or staking activities
- Receipt of a digital asset as a result of an airdrop
- Any other disposition of a financial interest in a digital asset

NOTE - The transfer of property, including a digital asset, as a bona fide gift, requires the filing of Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return if the fair market value of the property, at the time of the transfer, exceeds the donor's annual gift exclusion amount available at the time of the transfer.

Additional Guidance

- Virtual Currency IRS FAQs
- Cryptocurrency hard forks & airdrops - Rev. Rul. 2019-24
- Charitable contributions of cryptocurrency require appraisal – CCA 202302012
- No Loss Deduction for Crypto's Substantial Decline in Value – CCA 202302011
- Sale and Other Dispositions of Assets – Publication 544

Final Regulations Issued (REG-122793-19)

Treasury and IRS issued final regulations on reporting by brokers on dispositions of digital assets for customers in certain sale or exchange transactions. This reporting is required to be made on the a Form 1099-DA beginning with transactions on or after January 1, 2025.

NOTE – Additional links to regulations, notices and procedures can be found at the IRS website.

Damages Paid Were Not for Physical Injury (§104(a)(2))

NOTE - The Tax Court case Estate of Finnegan v. Commissioner (T.C. Memo 2024-42) addresses the tax treatment of settlement proceeds received by the estate of Roman J. Finnegan. The central issue was whether these proceeds should be excluded from gross income under §104(a)(2).

Background

IRC 104(a)(2) states: *Except in the case of amounts attributable to (and not in excess of) deductions allowed under §213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness*

Key Facts

- The case arose from a $25 million settlement following the death of a child, the subsequent investigation and charges against the parents, and the removal of two siblings from the family home.
- The family brought constitutional claims under the First, Fourth, Sixth, and Fourteenth Amendments.
- After an IRS examination of the parents' 2017 tax return, the IRS advised that all the settlement proceeds were fully taxable.
- The taxpayers argued for exclusion under §104(a)(2) due to post-traumatic stress disorder (PTSD), claiming the damages were for personal physical injuries or sickness.

Court's Analysis & Rulings

Nature of Settlement Proceeds & Characterization of Claims

- The court examined whether the settlement proceeds were excludable under §104(a)(2). For damages to be excludable, they must be received on account of personal physical injuries or physical sickness.
- The court determined that the primary cause of action was the violation of civil rights, not personal physical injuries or physical sickness.
- The court noted that the settlement agreement, complaint, proposed voir dire questions, plaintiffs' preliminary statement, jury instructions, and jury verdict did not mention PTSD or physical injury or sickness.
- The court emphasized that the expert observations of PTSD were made after the settlement and thus did not establish the necessary causal link under §104(a)(2).
- The court found that the settlement primarily compensated for civil rights violations rather than for any physical injuries or sickness.
- The complaint and other legal documents did not sufficiently demonstrate that the settlement was for physical injuries or physical sickness. The mention of PTSD in the proceedings was minimal and not the basis of the settlement.

Taxability of Settlement Proceeds

- Since the settlement was for civil rights violations and not personal physical injuries or physical sickness, the proceeds were deemed taxable.
- The court concluded that the settlement proceeds must be included in the estate's gross income.

Trade or Business (Sole Proprietor) Issues

IRC §162 Background & Rental Properties

Trade or Business Expenses (§162(a))

NOTE – Deductions are a matter of legislative grace and are allowable only as specifically provided by statute. See INDOPCO, Inc. v. Commissioner (Supreme Court - 1992).

IRC 162(a) states: There shall be allowed as a deduction all the **ordinary and necessary** expenses paid or incurred during the taxable year **in carrying on any trade or business**, including:

1. A reasonable allowance for salaries or other compensation for personal services actually rendered;
2. Traveling expenses (including amounts expended for meals and lodging **other than amounts which are lavish or extravagant** under the circumstances) while away from home in the pursuit of a trade or business; and
3. Rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

NOTE – An **ordinary expense** is one that is **common and accepted** in the taxpayer's field of business, trade, or profession. A **necessary expense** is one that is **helpful and appropriate**, although not necessarily required, for the taxpayer's business. The determination of **lavish and extravagant** are based on facts and circumstances and require the use of professional judgment on the part of the taxpayer and tax professional.

Trade or Business Defined

IRC §162 allows deductions for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business. **IRC §212** allows deductions for individuals for all the ordinary and necessary expenses paid or incurred during the taxable year for the production of income or the management or maintenance of property held for the production of income. **IRC §262(a)** disallows deductions for personal, living, or family expenses.

NOTE – Neither the Code nor the Regulations define what constitutes a trade or business under IRC §162. In **Higgins (Supreme Court - 1941),** the Supreme Court stated that the determination of whether the activities of a taxpayer are carrying on a trade or business requires an examination of the facts in each case.

In Groetzinger (Supreme Court – 1987), the Supreme Court stated: "Of course, not every income-producing and profit-making endeavor constitutes a trade or business. The income tax law, almost from the beginning, has distinguished between a business or trade, on the one hand, and "transactions entered into for profit but not connected with ... business or trade," on the other. Congress "distinguished the broad range of income or profit producing activities from those satisfying the narrow category of trade or business. We accept the fact that to be engaged in a trade or business, the taxpayer must be involved in the activity with continuity and regularity and that the taxpayer's primary purpose for engaging in the activity must be for income or profit. A sporadic activity, a hobby, or an amusement diversion does not qualify." But the court provided no additional guidance.

NOTE – The Supreme Court held that an individual who earns his living by gambling is engaged in a trade or business if he wagers with regularity, consistency and intent to make a profit. The court refuted the contention that the offering of goods or services to others is necessary to qualify as a trade or business.

Summary or characteristics to be a §162 trade or business

Because there is no statutory or regulatory definition of a §162 trade or business, courts have established elements to determine the existence of a trade or business. The courts have developed two definitional requirements:

1. **Profit motive** – this requires the taxpayer to enter into and carry on the activity with a good faith intention to make a profit or with the belief that a profit can be made from the activity and
2. **Sufficient taxpayer involvement in relation to the scope of the activities** – must be considerable, regular, and continuous.

Does Rental Real Estate Qualify as a IRC §162 Trade or Business?

Since there is no definition of a §162 trade or business under the code or regulations you have to look at case law. In general, a taxpayer is considered to be engaged in the trade or business of renting real property if several properties are rented. The business and management activities must be **considerable, continuous and regular**. Rental and management activities of an outside property management company are attributed to the taxpayer. If only a few properties are rented then determination as to whether or not the real estate qualifies as a “trade or business” becomes much more difficult. Some courts have taken the position that even limited rental activities are sufficient to constitute a trade or business while other courts have required a greater level of activity on the part of the taxpayer.

NOTE – Property subject to a net lease under the case law (and IRS's ruling stance) apparently will be considered a capital asset in almost all situations and not a IRC §162 trade or business.

Why is this Important?

Non-passive IRC §162 trade or business income will escape the 3.8% net investment income tax under §1411. Thus, rentals can escape the 3.8% if:

1. The income is non-passive because either:
    a. the taxpayer is a real estate profession (REP) (under §469(c)(7)) and they materially participate in the rental real estate activities or
    b. under the rental income is recharacterized as non-passive income under §469 and the regulations.

    and
2. The rentals activity falls under §162 trade or businesses (not §212) unless they meet a safe harbor rule under the §1411 regulations.

Other Issues – Form 1099-Misc

If your rental is a §162 trade or business, then you are required to issued Form 1099-Misc to anyone (with limited exceptions) you pay $600 or more during the year. Failure to report can result in two separate penalties 1) §6721 – failure to timely file information returns with the IRS, and 2) §6722 – failure to timely furnish the payee with the information return.

NOTE - That is why they ask the following questions at the top of the Form Schedule E:

Question A: “Did you make any payments that would require you to file Form(s) 1099?”

Question B: “If yes, did you or will you file all required Forms 1099?”

Form or Schedule to report IRC §162 Trade or Businesses			
Type of Trade or Business	**Income**	**Expenses**	**Social Security & Medicare Tax**
Self-employed individual (not engaged in farming)	Schedule C	Schedule C	Net Income on Schedule S/E
Self-employed individual engaged in farming	Schedule F	Schedule F	Net Income on Schedule S/E
Common law employee	Form 1040 – Sch. 1	Non-deductible after 2017. Were limited to 2% of AGI before 2018.	FICA Withheld on gross W-2 income
Statutory Employee (Form W-2 box 13 will be checked)	Schedule C	Schedule C	FICA Withheld on gross W-2 income
S Corporation shareholder receiving Schedule K-1	W-2 Income on Form 1040 – Sch. 1 & Trade or Business income on Schedule E – page 2	Unreimbursed expenses are non-deductible after 2017. Business interest may be deductible on Schedule E - page 2	FICA Withheld on gross W-2 income
Partnership partner receiving Schedule K-1	Guaranteed payments and Trade or Business income on Schedule E – page 2	Unreimbursed expenses on Schedule E – page 2	Net Income on Schedule S/E
Rental Real Estate* (under §162 or §212)	Schedule E – page 1 (hotel or real estate dealer on Schedule C*)	Schedule E – page 1	N/A
Rental of personal property	Schedule C	Schedule C	Net Income on Schedule S/E

***NOTE -** Rental real estate income and expenses are generally reported on Schedule E. Real estate dealers engaged in the business of selling real estate to customers with the purposes of making a profit or owners of a hotel, motel, etc., who provides services for guests, report the rental income and expenses on Schedule C. Services are considered rendered to the occupant if they are primarily for his convenience and are other than those usually or customarily rendered in connection with the rental of rooms or other space for occupancy only. The supplying of maid service, for example, constitutes such service; whereas the furnishing of heat and light, the cleaning of public entrances, exits, stairways and lobbies, the collection of trash, and so forth, are not considered as services rendered to the occupant. See §1.1402(a)-4(c)(2).

Home Office Deduction (§280A(c))

Qualifying for a Deduction

Expenses related to the business use of the home are deductible by the taxpayer to the extent such item is allocable to a portion of the dwelling unit which is **exclusively used on a regular basis**:

- as the principal place of business for any trade or business of the taxpayer,
- as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business,

  OR
- in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business.

NOTE 1 – In the case of an employee, the preceding sentence shall apply only if the exclusive use is for the convenience of their employer.

NOTE 2 – Under 1 above, the term "principal place of business" includes a place of business which is used by the taxpayer for the administrative or management activities of any trade or business of the taxpayer if there is no other fixed location of such trade or business where the taxpayer conducts substantial administrative or management activities of such trade or business.

Exclusive Use

To qualify under the exclusive use test, the taxpayer must use a specific area of their home only for the trade or business. The area used for business can be a room or other separately identifiable space. The space does not need to be marked off by a permanent partition. The taxpayer does not meet the requirements of the exclusive use test if the taxpayer uses the area in question both for business and for personal purposes.

EXAMPLE – Dennis is an attorney and uses the den in his home to write legal briefs and prepare clients' tax returns. Dennis's family also uses the den for recreation. The den is not used exclusively in his law practice, so he cannot claim a business deduction for its use.

Exceptions to Exclusive Use

The taxpayer does not have to meet the exclusive use test if either of the following applies.

1. the taxpayer uses of the home for the storage of inventory or product samples
2. the taxpayer uses part of the home as a daycare facility

Storage of Inventory or Product Samples

If the taxpayer uses part of their home for storage of inventory or product samples, the taxpayer can claim expenses for the business use of their home without meeting the exclusive use test. However, the taxpayer must meet all the following tests:

1. the taxpayer sells products at wholesale or retail as their trade or business
2. the taxpayer keeps the inventory or product samples in the home for use in the trade or business
1. the taxpayer's home is the only fixed location of the trade or business
2. the taxpayer uses the storage space on a regular basis
3. the space that the taxpayer uses is an identifiably separate space suitable for storage

EXAMPLE – Andrew's home is the only fixed location of his business of selling mechanics' tools at retail. Andrew regularly uses half of his basement for storage of inventory and product samples. Andrew sometimes uses the area for personal purposes. The expenses for the storage space are deductible even though Andrew does not use this part of his basement exclusively for business.

Regular Use

To qualify under the regular use test, the taxpayer must use a specific area of the home for business on a continuing basis. The taxpayer does not meet the test if the business use of the area is only occasional or incidental, even if the taxpayer does not use that area for any other purpose.

Additional Tests for Employee Use

If the taxpayer is an employee and they use a part of their home for business, the taxpayer may qualify for a deduction for its business use. The taxpayer must meet the tests discussed above PLUS:

1. the business use of the home must be for the convenience of the employer and
2. the taxpayer must not rent any part of the home to the employer and use the rented portion to perform services as an employee

Comparison of the Home Office Deduction Methods	
Simplified Option (Rev. Proc. 2013-13)	**Regular Method**
Deduction for home office use of a portion of a residence allowed only if that portion is **exclusively** used on a **regular basis** for business purposes	Same
Allowable square footage of home use for business (not to exceed 300 square feet)	Percentage of home used for business
Standard $5 per square foot used to determine home business deduction	Actual expenses determined and records maintained
Home-related itemized deductions claimed in full on Schedule A	Home-related itemized deductions apportioned between Schedule A and business schedule (Sch. C or Sch. F)
No depreciation deduction	Depreciation deduction for portion of home used for business
No recapture of depreciation upon sale of home	Recapture of depreciation on gain upon sale of home
Deduction cannot exceed gross income from business use of home less business expenses	Same
Amount in excess of gross income limitation may **not** be carried over	Amount in excess of gross income limitation may be carried over
Loss carryover from use of regular method in prior year may **not** be claimed	Loss carryover from use of regular method in prior year may be claimed if gross income test is met in current year

- Taxpayers can choose to use either method for any taxable year.
- The method chosen must be made on a timely filed, original Federal income tax return.
- Once the method has been chosen for a taxable year it cannot be changed for that same year.
- If the simplified method is used for any year and the regular method for any subsequent year, the depreciation deduction for the subsequent year must be calculated using the appropriate optional depreciation table. This is true regardless of whether an optional depreciation table was used for the first year the property was used in business.

Deductible Transportation Expenses (Rev. Rul. 99-7)

General Rule
In general, daily transportation expenses incurred in going between a taxpayer's residence and a work location are nondeductible commuting expenses.

Transportation Between Residence & Temporary Work Location
A taxpayer may deduct daily transportation expenses incurred in going between the taxpayer's residence and a temporary work location **outside the metropolitan area** where the taxpayer lives and normally works. However, unless one of the following exceptions below applies, daily transportation expenses incurred in going between the taxpayer's residence and a temporary work location **within that metropolitan area** are nondeductible commuting expenses.

Taxpayer has One or More Regular Work Locations
If a taxpayer has one or more regular work locations away from the taxpayer's residence, the taxpayer may deduct daily transportation expenses incurred in going between the taxpayer's residence and a temporary work location in the same trade or business, regardless of the distance.

NOTE - The Service will continue not to follow the Walker decision.

Taxpayer's Residence is the Principal Place of Business
If a taxpayer's residence is the taxpayer's principal place of business, the taxpayer may deduct daily transportation expenses incurred in going between the residence and another work location in the same trade or business, regardless of whether the other work location is regular or temporary and regardless of the distance.

Temporary Work Location Defined

Realistic Expectation of 1 Year or Less
If employment at a work location is realistically expected to last (and does in fact last) for 1 year or less, the employment is temporary in the absence of facts and circumstances indicating otherwise.

Realistic Expectation of More than 1 Year
If employment at a work location is realistically expected to last for more than 1 year or there is no realistic expectation that the employment will last for 1 year or less, the employment is not temporary, regardless of whether it actually exceeds 1 year.

Realistic Expectation for 1 Year or Less Changes to More than 1 Year
If employment at a work location initially is realistically expected to last for 1 year or less, but at some later date the employment is realistically expected to exceed 1 year, that employment will be treated as temporary (in the absence of facts and circumstances indicating otherwise) until the date that the taxpayer's realistic expectation changes, and will be treated as not temporary after that date.

Lee Baker Case– TC Memo 2014-122
The Tax Court (TC) allowed a self-employed truck driver to provide estimates of those expenses with no documentation under the Cohan rule. Baker lost all of his records relating to his truck operation when he lost his home in bankruptcy. The TC found that Baker credibly testified about his business and the truck expenses were not subject to the heightened substantiation requirements of §274(d)(4). The TC did however reduce the actual deduction from the amounts estimated by Baker.

Hobby Loss Rules (§183(c))

Background Activity Not Engaged in for Profit (§183(c))

The term "activity not engaged in for profit" means any activity other than one with respect to which deductions are allowable for the taxable year under §162 or §212(1) or (2). If an activity is not "engaged in for profit," the expenses that the taxpayer can deduct on their tax return are limited to income from that activity. No losses from this activity can be used to offset income from another activity. An activity is considered "engaged in for profit" it is of the kind that would:

- support a deduction for a business expense, or
- for an expense for the production of collection of income; or
- the management, conservation, or maintenance of income-producing property.

Relevant Factors (§1.183-2(b))

Whether or not an activity is presumed to be operated for profit requires an analysis of the facts and circumstances of each case. Deciding whether a taxpayer operates an activity with an actual and honest profit motive typically involves applying the nine non-exclusive factors contained in Treas. Reg. §1.183-2(b). Those factors are:

1. the manner in which the taxpayer carried on the activity,
2. the expertise of the taxpayer or his or her advisers,
3. the time and effort expended by the taxpayer in carrying on the activity,
4. the expectation that the assets used in the activity may appreciate in value,
5. the success of the taxpayer in carrying on other similar or dissimilar activities,
6. the taxpayer's history of income or loss with respect to the activity,
7. the amount of occasional profits, if any, which are earned,
8. the financial status of the taxpayer, and
9. elements of personal pleasure or recreation.

NOTE – No single factor controls, other factors may be considered, and the mere fact that the number of factors indicating the lack of a profit objective exceeds the number indicating the presence of a profit objective (or vice versa) is not conclusive.

Horse Breeding Was Not for Profit (Donoghue, TC Memo 2019-71)

Facts

The Donoghues started a thoroughbred horse breeding activity in 1985. The horses were owned by the Donoghues but boarded at farms and stables owned by other people. Mr. Donoghue was employed full time as a programmer and Mrs. Donoghue was disabled and received disability benefits. The Donoghues owned 6 horses from 1985 through 2012. The last year any horse was raced was in 2008. During the audit years 2010-2012, the Donaghues did not breed, race, or sell any of their horses. From 1985 through 2012, their horse breeding activity reported income of $36,691 and expenses of $1,008,303 (i.e., total losses of $974,612) and never had a profitable year.

Tax court ruled in favor of the IRS

The Tax Court (TC) examined the nine factors above and determined that eight of them were in favor of the IRS. The court stated that fact that a taxpayer engaged in similar activities (factor 5) and converted them to profitable enterprises may indicate that the taxpayer engaged in the present activity for profit, even though it is presently unprofitable. Thus, the TC ruled in favor of the IRS and the Donaghues had to pay back taxes and accuracy related penalties under §6662(a).

Schedule E – Rentals & Passive Activities

Material Participation

7 Material Participation Tests (§1.469-5T(a))

If the shareholder does not materially participate in the activity, a trade or business activity of the corporation is a passive activity for the shareholder. Each shareholder must determine if they materially participated in an activity. The taxpayer materially participated in a trade or business activity for a tax year if they satisfy **any** of the following tests:

1. the taxpayer participated in the activity for **more than 500 hours,**
2. the taxpayer's participation was **substantially all the participation in the activity** of all individuals for the tax year, including the participation of individuals who did not own any interest in the activity,
3. the taxpayer participated in the activity for **more than 100 hours during the tax year**, and the taxpayer participated **at least as much as any other individua**l (including individuals who did not own any interest in the activity) for the year,
4. the activity is a **significant participation activity**, and the taxpayer participated in all significant participation activities for more than 500 hours,

NOTE – A significant participation activity is any trade or business activity in which the taxpayer participated for more than 100 hours during the year and in which the taxpayer did not materially participate under any of the material participation tests, other than this test.

5. The taxpayer materially participated in the activity for **any 5 of the 10 immediately preceding tax years** (whether or not consecutive),
6. The activity is a **personal service activity in which the taxpayer materially participated for any 3 preceding tax years** (whether or not consecutive), or

NOTE – An activity is a personal service activity if it involves the performance of personal services in the fields of health (including veterinary services), law, engineering, architecture, accounting, actuarial science, performing arts, consulting, or any other trade or business in which capital is not a material income-producing factor.

7. based on all the **facts and circumstances**, the taxpayer participated in the activity on a regular, continuous, and substantial basis during the year.

Spouse's Participation

The taxpayer's participation in an activity includes the spouse's participation. This applies even if the spouse:

1. did not own any interest in the activity AND
2. the taxpayer and spouse do not file a joint return for the year.

Limited Partners

If the taxpayer owned an activity as a limited partner, the taxpayer generally is not treated as materially participating in the activity.

NOTE – The taxpayer is treated as materially participating in the activity if they met test 1, 5, or 6 under the material participation tests discussed above.

Not Treated as Limited Partner

The taxpayer is not treated as a limited partner, however, if the taxpayer also was a general partner in the partnership at all times during the partnership's tax year ending with or within the tax year (or, if shorter, during that part of the partnership's tax year in which the taxpayer directly or indirectly owned their limited partner interest).

NOTE – On November 28, 2011, the IRS issued Prop. Reg. 1.469-5(e) below. This section applies to taxable years beginning on or after the date of publication of the Treasury decision adopting these rules as a final regulation in the Federal Register.

Treatment of limited partners (Prop. Reg. §1.469-5(e))

General Rule

Except as otherwise provided in this paragraph (e), an individual shall not be treated as materially participating in any activity in which the individual owns an interest in a limited partnership as a limited partner (as defined in paragraph (e)(3)(i) of this section) for purposes of applying section 469 and the regulations thereunder to:

1. The individual's share of any income, gain, loss, deduction, or credit from such activity that is attributable to an interest in a limited partnership as a limited partner; and
2. Any gain or loss from such activity recognized upon a sale or exchange of such an interest.

Exceptions

The prior paragraph shall not apply to an individual's share of income, gain, loss, deduction, and credit for a taxable year from any activity in which the individual would be treated as materially participating for the taxable year under paragraphs (a)(1), (a)(5), or (a)(6) of §1.469-5T if the individual did not own an interest in a limited partnership as a limited partner (as defined in paragraph (e)(3)(i) of this section) for such taxable year.

Interest in a limited partnership as a limited partner

General Rule

Except as provided in the paragraph below, for purposes of §469(h)(2) and this paragraph (e), an interest in an entity shall be treated as an interest in a limited partnership as a limited partner if:

1. The entity in which such interest is held is classified as a partnership for Federal income tax purposes under §301.7701-3; and
2. The holder of such interest does not have rights to manage the entity at all times during the entity's taxable year under the law of the jurisdiction in which the entity is organized and under the governing agreement.

Individual holding an interest other than an interest in a limited partnership as a limited partner

An individual shall not be treated as holding an interest in a limited partnership as a limited partner for the individual's taxable year if such individual also holds an interest in the partnership that is not an interest in a limited partnership as a limited partner (as defined in paragraph (e)(3)(i) of this section), such as a state-law general partnership interest, at all times during the entity's taxable year ending with or within the individual's taxable year (or the portion of the entity's taxable year during which the individual (directly or indirectly) owns such interest in a limited partnership as a limited partner).

Real Estate Professionals (REP) Exception to PAL Rules (§469(c)(7) & §1.469-9))

Background

In general, all rental activities (except those meeting the exception for real estate professionals) are passive activities. Deductions for losses from passive activities are limited. The taxpayer generally cannot offset income, other than passive income, with losses from passive activities. Nor can the taxpayer offset taxes on income, other than passive income, with credits resulting from passive activities. Any excess loss or credit is carried forward to the next tax year.

NOTE – Rental activities in which the taxpayer materially participated during the year are not passive activities if, for that year, the taxpayer was a real estate professional because the taxpayer met the requirements.

Real Estate Professional Defined (i.e., Qualifying Taxpayer) (§469(c)(7)(B))

The taxpayer (or spouse) qualify as a real estate professional for the tax year if they meet both of the following requirements:

1. **more than one-half of the personal services** performed in trades or businesses by the taxpayer during such taxable year are performed in **real property trades or businesses** in which the taxpayer **materially participates**

   AND

2. such taxpayer performs **more than 750 hours** of services during the taxable year in **real property trades or businesses** in which the taxpayer **materially participates**.

Special Rules to Remember:

- In the case of a joint return, the requirements above are satisfied if and only if either spouse separately satisfies such requirements.
- Personal services means any work performed by an individual in connection with a trade or business. However, personal services do not include any work performed by an individual in the individual's capacity as an investor as described in §1.469-5T(f)(2)(ii).
- Do not count personal services that were performed as an employee in real property trades or businesses unless the taxpayer (or spouse) was a 5% owner of their employer. The taxpayer (or spouse) is a 5% owner if they own more than 5% of the employer's outstanding stock or capital or profits interest.
- The taxpayer can count their spouse's participation in an activity in determining if the taxpayer materially participated.
- Material participation has the same meaning as under §1.469-5T.

Real Property Trades or Businesses Defined (§469(c)(7)(C))

The term "real property trade or business" means any:

1. real property development,
2. redevelopment,
3. construction,
4. reconstruction,
5. acquisition,
6. conversion,
7. rental,
8. operation,
9. management,
10. leasing OR
11. brokerage trade or business.

NOTE – A taxpayer must materially participate in a real property trade or business in order for the personal services provided by the taxpayer in that real property trade or business to count towards more than 50% and more than 750 hours test. (§1.469-9(c)(3)).

Real Estate Professionals - Real Property Brokers (CCA 201504010)

The IRS Office of Chief Counsel concluded:

1. A real estate agent who brings together buyers and sellers of real property may be engaged in a real property brokerage trade or business under §469(c)(7)(C).
2. A mortgage broker who is a broker of financial instruments is not in a real property brokerage trade or business within the meaning of §469(c)(7)(C).

Treatment of Rental Real Estate Activities (§1.469-9(e))

A rental real estate activity of a qualifying taxpayer (i.e., real estate professional) is a passive activity under §469 for the taxable year **unless** the taxpayer materially participates in the activity. Each interest in rental real estate of a qualifying taxpayer will be treated as a separate rental real estate activity, unless the taxpayer makes an election under §1.469-9(g) to treat all interests in rental real estate as a single rental real estate activity.

NOTE – Each separate rental real estate activity, or the single combined rental real estate activity if the taxpayer makes an election, will be an activity of the taxpayer for all purposes of §469, including the former passive activity rules under §469(f) and the disposition rules under §469(g). However, §469 will continue to be applied separately with respect to each publicly traded partnership, as required under §469(k), notwithstanding the rules of this section.

Treatment as a former passive activity

For any taxable year in which a qualifying taxpayer materially participates in a rental real estate activity, that rental real estate activity will be treated as a former passive activity under §469(f) if disallowed deductions or credits are allocated to the activity under §1.469-1(f)(4).

Grouping rental real estate activities with other activities

For purposes of this section, a qualifying taxpayer may not group a rental real estate activity with any other activity of the taxpayer.

Special rule for certain management activities

A qualifying taxpayer may participate in a rental real estate activity through participation, within the meaning of §§1.469-5(f) and 5T(f), in an activity involving the management of rental real estate (even if this management activity is conducted through a separate entity). In determining whether the taxpayer materially participates in the rental real estate activity, however, work the taxpayer performs in the management activity is taken into account only to the extent it is performed in managing the taxpayer's own rental real estate interests.

Election to Treat All Interests in Rental Real Estate as a Single Activity (§1.469-9(g))

If the taxpayer was a real estate professional and had more than one rental real estate interest during the year, the taxpayer can choose to treat all the interests as one activity. The taxpayer can make this choice for any year that the taxpayer qualifies as a real estate professional. If the taxpayer forgoes making the choice for one year, the taxpayer can still make it for a later year.
If the taxpayer makes the choice, it is binding for the tax year the taxpayer makes it and for any later year that the taxpayer is a real estate professional. This is true even if the taxpayer is not a real estate professional in any intervening year. For that year, the exception for real estate professionals will not apply in determining whether the taxpayer's activity is subject to the passive activity rules.
If there is a material change in the taxpayer's facts and circumstances, the taxpayer may revoke the election using the procedure described in (§1.469-9(g)(3) of this section.

Making the Election (§1.469-9(g)(3))

A qualifying taxpayer makes the election to treat all interests in rental real estate as a single rental real estate activity **by filing a statement with the taxpayer's original income tax return for the taxable year.** This statement must contain a declaration that the taxpayer is a qualifying taxpayer for the taxable year and is making the election pursuant to §469(c)(7)(A). The taxpayer may make this election for any taxable year in which §469(c)(7) is applicable.

Relief for Late Aggregation Election (Rev. Proc. 2011-34)

Revenue procedure 2011-34 provides guidance under §1.469-9(g) of the Income Tax Regulations allowing certain taxpayers to make late elections to treat all interests in rental real estate as a single rental real estate activity. The procedures in this revenue procedure are in lieu of the letter ruling procedure that is used to obtain relief for a late §1.469-9(g) election. User fees do not apply to corrective action under this revenue procedure.

NOTE – A taxpayer that is not eligible for relief under this revenue procedure may request relief by applying for a private letter ruling. The Service will not ordinarily issue a private letter ruling under §1.469-9(g) if the period of limitations on assessment under §6501(a) has lapsed for any taxable year that would be affected by the requested late election.

Revoking the Election (§1.469-9(g)(3))

A taxpayer may revoke the election only in the taxable year in which a material change in the taxpayer's facts and circumstances occurs or in a subsequent year in which the facts and circumstances remain materially changed from those in the taxable year for which the election was made. To revoke the election, the taxpayer must file a statement with the taxpayer's original income tax return for the year of revocation. This statement must contain a declaration that the taxpayer is revoking the election under §469(c)(7)(A) and an explanation of the nature of the material change.

REP IRS Guidance & Cases

CCA 201427016

The IRS Office of Chief Counsel concluded that whether a taxpayer is a qualifying taxpayer (REP) within the meaning of §469(c)(7)(B) and §1.469-9(b)(6) depends upon the rules for determining a taxpayer's real property trades or businesses under Reg. §1.469-9(d), and is not affected by an election to treat all rental activities as a single activity under Reg. §1.469-9(g). The §1.469-9(g) election is only relevant after the determination of whether the taxpayer is a REP.

CCA 201504010

The IRS concluded that a real estate agent who brings together buyers and sellers of real property may be engaged in a real property brokerage trade or business under §469(c)(7)(C). However, a mortgage broker who is a broker of financial instruments is not in a real property brokerage trade or business within the meaning of §469(c)(7)(C).

Taxpayer did Not Spend > 50% Time in REP (Penley TC Memo 2017-65)

The taxpayer (Penley) worked 2,194 hours in their non-real estate job and 2,520 hours on his real estate activities (i.e., 4,712 hours/366 days = 12.88 hours per day). Penley claimed to have worked on his real estate activities 10-14 hours on each Saturday and Sunday during 2012 and an additional 4-6 hours most weekdays, in addition to another full-time job. The court said that Penley greatly exaggerated the time spent on the real estate activities and did not provide a sufficient explanation to reconcile their documentary evidence.

Taxpayers failed to show they were real estate professionals (Makhlouf – TC Summary Opinion 2017-1)

The Makhloufs failed to show that they performed more than 750 hours of services during the tax year in real property trades or businesses in which they materially participated. The taxpayers records were not prepared contemporaneously, and it were implausible on its face in many respects. Most entries on the taxpayer's spreadsheet were round-number estimates, many were clearly inflated, and many were duplicative. For most entries, each of the Makhloufs supposedly devoted the exact same number of hours to the task in question. The Makhloufs allegedly attended every meeting with contractors together and spent precisely the same amount of time at each meeting. Thus, they allegedly double-teamed tasks that could easily have been performed by one person, such as supervise yard work.

REP Must Materially Participate Rentals (Gragg – CA-9 (09-08-16))

Issue

The issue on appeal is whether §469(c)(7) automatically renders a REP's rental losses nonpassive and deductible, or whether it merely removes §469(c)(2)'s per se bar on treating rental losses as passive. The Graggs advocate for the former interpretation, and the IRS argues for the latter.

Analysis & Ruling

The IRS disallowed the taxpayers rental losses because it concluded that the Graggs were required to show they materially participated in the rental properties, and had not done so. The Graggs' complaint renewed their argument that by virtue of Delores's status as a real estate professional, their rental losses were automatically nonpassive and they did not need to prove material participation. The district court ruled in favor of the government, and the Graggs timely appealed.

Thus, the 9th Circuit panel held that §469 allows real estate professionals to deduct rental losses from their taxable income, but only if they materially participate in rental activities.

Travel Time Allowed for Real Estate Professional Tests (Leyh - TC Summary 2015-27)

The Tax Court held that the taxpayer kept a contemporaneous log and accurately recorded her rental real estate activity for each day she engaged in the activity (necessary under §1.469-5T(f)(4)). The taxpayer's original log did not account for travel time from the taxpayer's home to the rental properties (approximately 45 minutes each way). When added to the total other hours she spent at her rental properties it brought the total REP hours to 846 (i.e., more than the 750 necessary hours).

S Corp Lessors Subject to PAL Self-Rental Rules (Williams, CA-5)

The 5th Circuit court of appeals affirmed the Tax Court's decision on both arguments:

1. passthrough entities are subject to §469, even though passthrough entities are not specifically included in the list of "taxpayers" to whom §469 is applicable (i.e., apply at owner level) and
2. the §1.469-2(f)(6) passive loss self-rental rule do apply to rentals by S corporations .

NOTE – The court agreed that §1.469-4(a) is a valid regulation. They stated that the S corporation is only a pass-through entity and that the shareholders are the taxpayers. Thus, the proper focus is not on a non-taxpayer S corporation, but on the actual taxpayers (i.e., shareholders).

Mortgage Broker is Not a REP (Hickam, TC Summary Opinion 2017-66)

The Tax Court agreed with the IRS that an individual who brokered real estate mortgages and other loans did not qualify as a real estate professional (REP) for purposes of the passive activity loss (PAL) rules. As a result, Hickman's rental real estate losses were limited.

IRS Website

- Passive Activity and At-Risk Rules Publication 925
- Real Estate Tax Center – click here
- Passive Activity Loss Audit Technique Guide (ATG) – click here

Individual Retirement Accounts (IRAs) Issues

SEP Contribution & Deduction Limits

Employer Annual Election to Contribute

The taxpayer does not have to make contributions every year. But if the taxpayer makes contributions, they must be:

1. based on a written allocation formula AND
2. must not discriminate in favor of highly compensated employees.

Must Contribute to All Eligible Employees

When the taxpayer makes the contribution, the taxpayer must contribute to the SEP-IRAs of all participants who actually performed personal services during the year for which the contributions are made, even employees who die or terminate employment before the contributions are made. The contributions that the company makes under a SEP are treated as if made to a qualified pension, stock bonus, profit-sharing, or annuity plan. Consequently, contributions are deductible within limits, as discussed later, and generally are not taxable to the plan participants.

UPDATE – Nontrade or Business SEP Contributions

The SECURE Act 2.0 (Section 118) permits employers of domestic employees (e.g., nannies) to provide retirement benefits for such employees under a SEP.

NOTE - This is effective for tax years beginning after December 29, 2022 (date of enactment).

Time Limit for Making Contributions

Employer contributions can be made until the due date of the employer's tax return, including extensions, regardless of when the tax return is actually filed. Thus, a SEP plan sponsor has until the due date of the year's income tax return, including extensions, to both set up and fund the SEP plan for the year.

EXAMPLE – A calendar-year corporate income tax return is due on March 15, but, with a valid extension, the corporation has until September 15 to both file its tax return and deposit employer contributions into its DC plan's trust or IRA. If contributions are not deposited timely, the employer must amend its tax return and pay any tax, interest and penalties that may apply.

Maximum Contribution

Contributions that the employer makes to a common-law employee's SEP-IRA cannot exceed the lesser of:

1. 25% of the employee's compensation, OR
2. the annual limit (adjusted for inflation):

Year	SEP Contribution Limit
2024	$69,000
2025	$70,000
2026	$72,000 (projected)

EXAMPLE – ABC Company's employee, Mary Plant, earned $21,000 for the year. The maximum contribution that ABC Company can make to Mary's SEP-IRA is $5,250 (25% x $21,000).

Annual Compensation Limit
The employer cannot consider the part of an employee's compensation over the annual compensation limit (adjusted annually for inflation):

Year	Maximum Compensation Limit
2024	$345,000
2025	$350,000
2026	$360,000 (projected)

More than One Plan
If the employer contributes to a defined contribution plan, annual additions to an account are limited to the lesser of the annual limit or 100% of the participant's compensation during the year. When the employer figures this limit, the employer must add the contributions to all defined contribution plans. Because a SEP is considered a defined contribution plan for this limit, the employer's contributions to a SEP must be added to the contributions to other defined contribution plans.

Roth SEP IRA
After 2022, employers can offer employees the ability to treat employee and employer SEP contributions as Roth IRA contributions.

NOTE – IRC 408(k)(7) states: An individual retirement plan which is designated as a Roth IRA shall not be treated as a simplified employee pension (SEP) under this subsection unless the employee elects for such plan to be so treated (at such time and in such manner as the Secretary may provide).

IRS Notice 2024-2 additional guidance

- **No requirement to offer Roth -** An employer is not required to offer a Roth contribution election.
- **Effective opportunity -** If an employer offers a Roth election, employees must have an effective opportunity (see Reg. §1.401(k)-1(e)(2)(ii)) to elect before the contribution is made that a SEP/SIMPLE contribution be treated as Roth.
- **Roth SEP employer contributions income inclusion -** Employer contributions designated as Roth SEP are includible in the employee's gross income for the taxable year in which the contribution is made to the employee's Roth IRA.
- **Designated Roth salary reductions income inclusion -** A salary-reduction contribution designated Roth (e.g., SIMPLE IRA or grandfathered SARSEP) is includible in the employee's gross income for the year the amount would otherwise have been received as wages.
- **Reporting -** Employer Roth SEP contributions must be reported on Form 1099-R for the year contributed, with the total in boxes 1 and 2a, code 2 (early distribution, exception applies) or code 7 (normal distribution) in box 7, and the IRA/SEP/SIMPLE checkbox marked.
- **Payroll treatment -**Designated Roth salary-reduction contributions (SIMPLE IRA/SARSEP) are subject to income-tax withholding, FICA, and FUTA. Employer nonelective/matching contributions (including Roth SEP employer contributions) are not wages and not subject to withholding, FICA, or FUTA.
- **Plan documents -** An employer may continue using Form 5305-SEP or an approved prototype document without amendment until the IRS issues updated forms or guidance.

SIMPLE IRA Plan Contribution & Deduction Limits

Prototype IRS Forms

The company can use Form 5304-SIMPLE or Form 5305-SIMPLE to set up a SIMPLE IRA plan. Each form is a model savings incentive match plan for employees (SIMPLE) plan document. Which form the company uses depends on whether the company selects a financial institution or the employees select the institution that will receive the contributions. If the company sets up a SIMPLE IRA plan using Form 5304-SIMPLE or Form 5305-SIMPLE, the company can use the form to satisfy other requirements, including the following:

1. meeting employer notification requirements for the SIMPLE IRA plan and
2. maintaining the SIMPLE IRA plan records and proving that the company set up a SIMPLE IRA plan for its employees.

NOTE – Page 3 of Form 5304-SIMPLE and Page 3 of Form 5305-SIMPLE contain a Model Notification to Eligible Employees that provides the necessary information to the employee.

Form 5304-SIMPLE

Use Form 5304-SIMPLE if the company allows each plan participant to select the financial institution for receiving his or her SIMPLE IRA plan contributions.

Form 5305-SIMPLE

Use Form 5305-SIMPLE if the company requires that all contributions under the SIMPLE IRA plan be deposited initially at a designated financial institution.

NOTE - Taxpayers must keep their plans up-to-date with current law. If using a prototype plan document, ensure you receive an amended plan from your financial institution. If you haven't updated your SIMPLE IRA plan, correct this mistake promptly.

Deadline for Setting up a SIMPLE IRA Plan

A company can set up a SIMPLE IRA plan effective on any date from **January 1 thru October 1 of a year**, provided that the company did NOT previously maintain a SIMPLE IRA plan.

Exception for New Company

This requirement does NOT apply if the company is a new employer that comes into existence after October 1 of the year the SIMPLE IRA plan is set up and the company set up a SIMPLE IRA plan as soon as administratively feasible after the business comes into existence.

Company had Previous SIMPLE IRA

If the company previously maintained a SIMPLE IRA plan, the company can set up a SIMPLE IRA plan effective only on January 1 of a year. A SIMPLE IRA plan CANNOT have an effective date that is before the date that the company actually adopts the plan.

Setting Up Each Employee's SIMPLE IRA

SIMPLE IRAs are the individual retirement accounts or annuities into which the contributions are deposited. A SIMPLE IRA must be set up for each eligible employee.

Deadline

A SIMPLE IRA must be set up for an employee before the first date by which a contribution is required to be deposited into the employee's IRA.

Roth SIMPLE IRA

After 2022, employers can offer employees the ability to treat employee and employer SIMPLE contributions as Roth IRA contributions.

NOTE – IRC 408(p)(12) states: An individual retirement plan which is designated as a Roth IRA shall not be treated as a simple retirement account under this subsection unless the employee elects for such plan to be so treated (at such time and in such manner as the Secretary may provide).

IRS Notice 2024-2 additional guidance

- **Roth is optional -** An employer is not required to offer a Roth contribution election.
- **Effective opportunity -** Employees must have the same effective opportunity to elect Roth treatment as they have to enter into a salary-reduction agreement under the plan (see §408(p)(5) and Notice 98-4). The Roth election must be made before the contribution is made.
- **Salary reductions income inclusion -** A Roth salary-reduction contribution is includible in the employee's gross income for the tax year in which the employee would otherwise have received the amount as wages absent the election.
- **Employer match/nonelective income inclusion -** An employer matching or nonelective contribution made to a Roth IRA under a SIMPLE is includible in the employee's gross income for the tax year the contribution is deposited to the Roth IRA (regardless of the employer's deduction year).
- **Payroll treatment -** Roth salary-reduction contributions are subject to income-tax withholding, FICA, and FUTA. Employer matching/nonelective contributions (even when designated Roth) are not wages and are not subject to withholding, FICA, or FUTA.
- **Plan documents -** An employer may continue using Form 5304-SIMPLE, Form 5305-SIMPLE, or an approved prototype without amendment until the IRS issues updated forms or further guidance.

Increased SIMPLE annual deferral limits (After 2023)

For tax years beginning after December 31, 2023, the SIMPLE annual deferral limit and the catch-up contribution at age 50 are increased by 10%, as compared to the limit that would otherwise apply in the first year this change is effective, in the case of an employer with no more than 25 employees.

NOTE - An employer with 26 to 100 employees would be permitted to provide higher deferral limits, but only if the employer either provides a 4% matching contribution or a 3% employer non-elective contribution.

IRS Notice 2024-2 additional guidance

- **Automatic application (≤25 employees) -** If the employer has no more than 25 employees who each received ≥ $5,000 in the preceding calendar year (see §408(p)(2)(E)(iv)), the increased limits apply automatically.
- **Election required (>25 employees) -** If more than 25 employees received ≥ $5,000 in the preceding year, the increased limits apply only if the employer formally elects to apply them and provides the required higher matching or nonelective contributions.
- **Two-year grace rule for the 25-employee test -** An employer that grows above 25 is still treated as having 25 employees for the two years following the last year it had ≤25, unless the increase resulted from an acquisition, disposition, or similar transaction.
- **Formal action & documentation -** Employers that must elect the increased limits must take formal written action and retain documentation in plan records. All employers

(including those for whom the limits apply automatically) must update plan terms to reflect the higher limits and notify employees (observe the plan-amendment deadlines referenced in the notice).
- **Notify vendors & keep records -** Notify the SIMPLE IRA or SIMPLE 401(k) financial institution and the payroll provider of the higher limits, and keep records of all actions taken. No IRS filing is required to make the election.
- **Timing of the election -** The election to apply the increased limits must be made before delivering the annual SIMPLE notice that offers employees the opportunity to enter into or modify salary-reduction agreements for that calendar year.
- **Duration & revocation -** An election remains in effect until revoked. To revoke, take formal written action before issuing the next annual SIMPLE notice, keep the revocation in plan records, and notify employees of the new applicable limits.

Eligible Employer
The increased limits apply to an eligible employer described in section 408(p)(2)(E)(iv) of the Code. An eligible employer is described in §408(p)(2)(E)(iv) if, during the 3-taxable year period preceding the first year that the employer maintained the SIMPLE IRA plan or SIMPLE 401(k) plan, the employer (including any member of the employer's controlled group or any predecessor of the employer or any member) has not established or maintained a qualified plan under section 401(a), a §403(a) annuity plan, or a §403(b) plan under which contributions were made or benefits were accrued for substantially the same employees as are eligible to participate in the SIMPLE IRA plan or SIMPLE 401(k) plan.

Salary Reduction
The amount the employee chooses to have the company contribute to a SIMPLE IRA on his or her behalf cannot be more than annual deferral limit below:

Tax Year	SIMPLE Plan	SIMPLE Plan Eligible Employer *
2024	$16,000	$17,600
2025	$16,500	$17,600
2026	$17,000 (projected)	$17,600 (projected)
* **NOTE –** An eligible employer is all employers that have no more than 25 employees and any employer with 26 to 100 employees that elects to increase the matching contribution to 4% (from 3%) or the non-elective contribution to 3% (from 2%).		

- These contributions must be expressed as a percentage of the employee's compensation unless the company permits the employee to express them as a specific dollar amount.
- The company cannot place restrictions on the contribution amount (such as limiting the contribution percentage), except to comply with the annual deferral limit.

WARNING – The company cannot place restrictions on the contribution amount (such as limiting the contribution percentage), except to comply with the SIMPLE deferral limits above.

If an employee is a participant in any other employer plan during the year and has elective salary reductions or deferred compensation under those plans, the salary reduction contributions under a SIMPLE IRA plan also are elective deferrals that count toward the overall annual limit **($23,500 for 2025)** on exclusion of salary reductions and other elective deferrals.

Catch-Up Contributions (Age 50 or Older)

A SIMPLE IRA plan can permit participants who are age 50 or over at the end of the calendar year to also make catch-up contributions.

> **NOTE** – Salary reduction contributions are NOT treated as catch-up contributions until they exceed the annual deferral limit (i.e., **$16,500 for 2025**).

UPDATE – Post 2024 increased catch-up contribution (ages 60 - 63)

For tax years beginning after December 31, 2024, the SIMPLE catch-up limit for participants who attain age 60, 61, 62, or 63 during the year is the greater of $5,000 or 150% of the regular 2025 catch-up amount. The annual limits adjust for inflation are:

Tax Year	Employees ages 50-59 & > 63	Eligible Employer * with employees ages 50-59 & >63	All employers with employees ages 60-63
2024	$3,500	$3,850	$3,500
2025	$3,500	$3,850	$5,250
2026	$4,000 (projected)	$4,150 (projected)	$5,250 (projected)
*** NOTE –** Employers with 25 or fewer employees, or 26–100 employees that elect to increase their SIMPLE plan contributions (4% match or 3% non-elective).			

Employer Contributions - Option 1 - Dollar-For-Dollar Match

The company is generally required to match each employee's salary reduction contributions on a dollar-for-dollar basis up to 3% of the employee's compensation. This requirement does NOT apply if the company makes a non-elective contributions.

> **EXAMPLE** – ABC Company's employee, John Rose, earned $25,000 and chose to defer 5% of his salary. The company chooses to make a 3% matching contributions for it's employees. The total contribution that the company can make for John is $2,000, figured as follows:

Salary reduction contributions ($25,000 × .05)	$1,250
Employer matching contribution ($25,000 × .03)	750
Total contributions	$2,000

Lower Percentage

If the company chooses a matching contribution less than 3%, the percentage must be at least 1%. The company must notify the employees of the lower match within a reasonable period of time before the 60-day election period (discussed earlier) for the calendar year.

> **NOTE** – The company cannot choose a percentage less than 3% for more than 2 years during the 5-year period that ends with (and includes) the year for which the choice is effective.

Treatment of student loan payments as elective deferrals for purposes of matching contributions

For contributions made for plan years beginning after December 31, 2023, the SECURE Act 2.0 (Sec. 110) 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." A qualified student loan payment is broadly defined (under §401(m)(D)(4)) as any indebtedness incurred by the employee solely to pay qualified higher education expenses of the employee. The Act permits a plan to test separately the employees who receive matching contributions on student loan repayments.

Employer Contributions - Option 2 - Non-Elective Contributions

Instead of matching contributions, the company can choose to make non-elective contributions of 2% of compensation on behalf of each eligible employee who has at least $5,000 (or some lower amount that the company selects) of compensation from the company for the year. The following rules also apply:

- If the company makes this choice, the company must make non-elective contributions whether or not the employee chooses to make salary reduction contributions.
- The maximum employee's compensation that can be taken into account to figure the employer's non-elective contribution is limited to **$350,000 in 2025**.
- If the company chooses this 2% contribution formula, the company must notify the employees within a reasonable period of time before the 60-day election period (discussed earlier) for the calendar year.

EXAMPLE 1 – XYZ Company's employee, Jane Wood, earned $36,000 and chose to have XYZ Company contribute 10% of her salary. The company makes a 2% non-elective contribution. Jane is under age 50. The total contribution that XYZ Company can make for Jane is $4,320, figured as follows:

Salary reduction contributions ($36,000 × 10%)	$3,600
2% non-elective contributions ($36,000 × 2%)	720
Total contributions	$4,320

EXAMPLE 2 – Using the same facts as in Example 1, above, the maximum contribution that the XYZ Company can make for Jane if she earned $75,000 and deferred $11,500 is figured as follows:

Salary reduction contributions	$11,500
2% non-elective contributions ($75,000 × .02)	1,500
Total contributions	$13,000

Additional nonelective contributions to SIMPLE plans

For tax years beginning after 2023, an employer may make a uniform nonelective contributions to each eligible employee, up to the lesser of 10% of compensation or $5,000 (indexed).

Time Limits for Contributing Funds to Employee's SIMPLE

30 Days for Salary Reduction Contributions (Notice 98-4)

The company must make the salary reduction contributions to the SIMPLE IRA **within 30 days** after the end of the month in which the amounts would otherwise have been payable to the employee in cash.

Employer Match & Non-elective Contribution by Due Date of Return

The company must make matching contributions or non-elective contributions by the due date (including extensions) for filing the company's federal income tax return for the year.

Tax Treatment of Contributions – Traditional SIMPLE

Employee Deferrals

Employees can exclude their SIMPLE IRA contributions from their gross income. SIMPLE IRA contributions are NOT subject to federal income tax withholding. However, salary reduction contributions are subject to social security, Medicare, and federal unemployment (FUTA) taxes.

Reporting on Form W-2

Do NOT include elective deferrals in the "Wages, tips, other compensation" box 1 of Form W-2. The employer must, however, include them in the "Social security wages" and "Medicare wages and tips" boxes 3 and 5. The employer must also include them in box 12 and mark the "Retirement Plan" checkbox in box 13.

Employer Contributions

Matching and non-elective contributions are not subject to FICA and FUTA taxes.

Tax Treatment of Contributions – Roth SIMPLE (Notice 2024-02)

Employee Deferrals

A salary reduction contribution made to a Roth IRA is includible in the employee's gross income for the taxable year that includes the date on which the employee would otherwise have received the salary reduction contribution as wages or salary if the employee had not elected for the amount to be contributed to the SIMPLE IRA plan.

Reporting on Form W-2

The employer must report salary reduction contributions made to a Roth IRA on Form W-2, Wage and Tax Statement, Box 12, using Code S (for a SIMPLE IRA), and include the same amount in Boxes 1, 3, and 5. Check the "Retirement plan" checkbox in box 13.

Employer Contributions

An employer matching or nonelective contribution made to a Roth IRA is includible in the employee's gross income for the taxable year that includes the date on which the contribution is made to the Roth IRA (regardless of what year the employer deducts it).

Reporting on Form 1099-R

Employer matching and nonelective contributions to a Roth SIMPLE must be reported on the Form 1099-R, for the year in which the contributions are made to the employees Roth IRA, with the total reported in boxes 1 and 2a, using code 2 (i.e., early distribution, exception applies (under age 59 ½) or code 7 (i.e., normal distribution) in box 7, and the IRA/SEP/SIMPLE checkbox in box 7 checked.

10% Additional Tax & Exceptions to Early Distributions from Qualified Retirement Plans (§72(t))

General Rule – 10% Penalty (§72(t)(1))

If any taxpayer receives any amount from a qualified retirement plan or IRA, the taxpayer's tax for the taxable year in which such amount is received shall be increased by an amount equal to 10% of the portion of such amount which is includible in gross income.

Exceptions to the 10% Penalty (§72(t)(2))

The 10% additional tax will not apply to any of the following:

1. **Age 59½ –** Distributions made on/after the date the participant attains age 59½. (Both)
2. **Death –** Paid to a beneficiary or estate after the participant's death. (Both)
3. **Disability –** The participant is disabled (as defined in §72(m)(7)). (Both)
4. **Substantially Equal Periodic Payments (SEPPs)** – Series of substantially equal periodic payments for life/life expectancy (participant alone or joint with beneficiary). (Both)
5. **Separation from service at age 55** – Distributions (not from IRAs) after separation from service in/after the year the employee turns 55. (Employer plans only)
6. **Qualified public safety employees –**Distributions (not from an IRA) to a qualified public safety employee (from a government plan) and private sector firefighters after separation from service after attainment of age 50 or 25 years of service under the plan, whichever is earlier (Employer plans only)
7. **ESOP dividends –** Dividends paid on employer securities under §404(k). (Employer plans only)
8. **IRS levy –** Distributions made to comply with a federal tax levy under §6331 on the plan. (Both)
9. **Medical expenses –** To the extent deductible under §213 (i.e., unreimbursed medical expenses exceeding the AGI threshold) for the year of the distribution. Determined without regard to whether the employee itemizes deductions for such taxable year. (Both)
10. **QDRO –** Distributions to an alternate payee under a qualified domestic relations order (within the meaning of §414(p)(1)). (Employer plans only)
11. **Health insurance premiums for the unemployed** – Payments for medical insurance while receiving unemployment compensation (timing rules apply). (IRAs only)
12. **Higher education expenses –** Qualified higher-education costs for the participant, spouse, children, or grandchildren. (IRAs only)
13. **First-time homebuyer –** Up to $10,000 lifetime for qualified first-home acquisition costs (participant or eligible family). (IRAs only)
14. **Qualified reservist distributions –** Called to active duty for >179 days (or indefinitely); special recontribution rules. (Both)
15. **Qualified birth or adoption (QBAD) –** Up to $5,000 per child; may be repaid within 3 years. (Both)
16. **Emergency personal expense distributions (after 2023) –** One distribution per year up to $1,000; repay within 3 years; no new emergency distribution permitted during the 3-year period unless repaid or new contributions ≥ amount withdrawn. (Both, plan must permit)
17. **Domestic abuse distributions (after 2023)** – Up to the lesser of $10,000 (indexed) or 50% of the vested account; repay within 3 years. (Both, plan must permit)
18. **Terminal illness** – Distributions to a participant medically certified as terminally ill (per statute/IRS guidance). (Both)

19. **Federally declared disaster distributions** – Permanent rule (for disasters on/after January 26, 2021): up to $22,000 per disaster; income spread over 3 years; recontribution permitted; related plan loan relief available. (Both)
20. **Long-term care (LTC) premium distributions (after 2025)** - Penalty-free distributions up to an annual cap (statutory; indexed) to pay specified long-term care insurance premiums; amounts are still taxable but exempt from the 10% penalty. (Both, plan/IRA must permit)

NOTE – The term "employee" includes any participant, and in the case of an individual retirement plan, the individual for whose benefit such plan was established.

SIMPLE Retirement Accounts – 25% Penalty (§72(t)(6))

In the case of any amount received from a SIMPLE retirement account during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer, the additional tax is 25% of the portion of such amount which is includible in gross income.

Summary Table - §72(t) Exceptions to the 10% Penalty	
§72(t) Exception to 10% Penalty	**Applies to IRAs and/or QRPs?**
1. Age 59½ or older	Both
2. Death (beneficiary/estate)	Both
3. Disability (§72(m)(7))	Both
4. SEPP / 72(t) periodic payments	Both
5. Separation from service at age 55 (Rule of 55)	QRPs only
6. Public safety / firefighters (age 50 or 25 yrs svc)	QRPs only
7. ESOP dividends (§404(k))	QRPs only
8. IRS levy on plan/IRA (§6331)	Both
9. Medical expenses > §213 AGI threshold	Both
10. QDRO to alternate payee (§414(p))	QRPs only
11. Health insurance for unemployed (IRAs)	IRAs only
12. Higher-education expenses (IRAs)	IRAs only
13. First-time homebuyer up to $10,000 lifetime (IRAs)	IRAs only
14. Qualified reservist called to active duty	Both
15. Birth or adoption (QBAD) up to $5,000	Both
16. Emergency personal expense distribution (after 2023)	Both
17. Domestic abuse distribution (after 2023)	Both
18. Terminal illness distribution	Both
19. Federally declared disaster distribution	Both
20. Long-term care insurance premium distribution (after 2025)	Both

Excise Tax on Certain Accumulations in Qualified Retirement Accounts

25% Excise Tax (§4974(a))

If the amount distributed to a payee under any qualified retirement plan or any eligible deferred compensation plan (as defined in §457(b)) for a calendar year is less than the required minimum distribution for that year, §4974 imposes an excise tax on the payee for the taxable year beginning with or within the calendar year during which the amount is required to be distributed.

UPDATE – For taxable years beginning after December 29, 2022, the tax shall be paid by the payee and is equal to 25% of the amount by which the required minimum distribution exceeds the actual amount distributed during the calendar year. Prior to 2023 the excise tax was 50%.

NOTE - The excise tax is reported on the Form 5329.

For purposes of §4974, the term required minimum distribution means the minimum amount required to be distributed pursuant to §§401(a)(9), 403(b)(10), 408(a)(6), 408(b)(3), or 457(d)(2), as the case may be, as determined under the regulations.

3-year statute of limitations

The SECURE Act 2.0 (Sec. 313) adds IRC §6501(l)(4) (effective 12-29-22) that provides for a 3-year statue of limitations to begin when the taxpayer files an individual tax return (Form 1040) for the year of violation rather than when the Form 5329 is filed.

Reduction of tax (10%) in certain cases (§4974(e))

The 25% excise tax will be reduced to 10% in the case of a taxpayer who:

1. receives a distribution, during the correction window, of the amount which resulted in imposition of a tax from the same plan to which such tax relates, and
2. submits a return, during the correction window, reflecting such tax (as modified by this subsection),

Correction window

The term "correction window" means the period of time beginning on the date on which the tax is imposed with respect to a shortfall of distributions from a plan, and ending on the earliest of:

1. the date of mailing a notice of deficiency with respect to the tax imposed under §6212,
2. the date on which the tax imposed by §4972(a) is assessed, or
3. the last day of the second taxable year that begins after the end of the taxable year in which the tax under §4972(a) is imposed.

Waiver of Tax in Certain Cases (§4974(d))

The Secretary may waive the tax imposed by §4974(a) for the taxable year if the taxpayer establishes to the satisfaction of the Secretary that:

1. the shortfall during any taxable year was due to reasonable error, and
2. reasonable steps are being taken to remedy the shortfall.

Required Distributions Background (§401(a)(9))

RMDs Required at RBD (§401(a)(9)(A))

A trust shall not constitute a qualified trust under unless the plan provides that the entire interest of each employee:

1. will be distributed to such employee not later than the required beginning date (RBD), or
2. will be distributed, beginning not later than the required beginning date, in accordance with regulations, over the life of such employee or over the lives of such employee and a designated beneficiary (or over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and a designated beneficiary).

NOTE - A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries will constitute a qualified trust if certain requirements are met under §401(a).

Required Beginning Date (RBD) Defined (§401(a)(9)(C)

The term "required beginning date" means April 1 of the calendar year following the later of:

1. the calendar year in which the employee **attains the applicable age**, or
2. the calendar year in which the employee retires.

NOTE – In the case of distributions from an IRA or from a qualified retirement plan to a more than 5% owner employee, the term required beginning date means April 1 of the calendar year following the calendar year in which the individual attains the applicable age.

Applicable age

- **Age 73** - In the case of an individual who attains age 72 after December 31, 2022, and age 73 before January 1, 2033, the applicable age is 73.
- **Age 75** - In the case of an individual who attains age 74 after December 31, 2032, the applicable age is 75.

NOTE – Prior to the SECURE Act the applicable age was 70 ½ and prior to the SECURE Act 2.0 the applicable age was 72.

Death of Employee After RMDs Have Started

At Least as Rapidly Rule (§401(a)(9)(B)(i))

If the RMDs of an employee have started and they die before the entire interest has been distributed, then the plan must require that any remaining balance must be distributed at least as rapidly as under the method of distributions being used as of the date of his death.

Death of Employee Before RMDs Have Started

5-Year Rule (§401(a)(9)(B)(ii))

In general, if an employee dies before the distribution of the employee's interest has begun (i.e., before the RBD), the entire interest of the employee must be distributed within 5 years after the death of such employee.

Life expectancy exception (§401(a)(9)(B)(iii))

This exception to the 5-year rule requires any portion of an employee's interest that is payable to (or for the benefit of) a designated beneficiary be distributed over the life of such beneficiary (or over a period not extending beyond the life expectancy of such beneficiary) as long as such distributions begin no later than one year after the death of the employee.

Special Rule for Surviving Spouse (§401(a)(9)(B)(iv))

UPDATE – The SECURE Act 2.0 (Section 327) amends §401(a)(9)(B)(iv) to allow a surviving spouse to elect to be treated as the deceased employee for purposes of the required minimum distribution rules. This is effective for calendar years beginning after December 31, 2023.

For the life expectancy exception above, if the designated beneficiary is the surviving spouse of the employee and the surviving spouse elects the treatment in this clause:

1. the regulations shall treat the surviving spouse as if the surviving spouse were the employee,
2. the date on which the distributions are required to begin shall not be earlier than the date on which the employee would have attained the applicable age (i.e., age 73), and
3. if the surviving spouse dies before the distributions to such spouse begin, these rules shall be applied as if the surviving spouse is the employee.

NOTE - An election described in this clause shall be made at such time and in such manner as prescribed by the Secretary, shall include a timely notice to the plan administrator, and once made may not be revoked except with the consent of the Secretary.

Life Expectancy (§401(a)(9)(D))

The life expectancy of an employee and the employee's spouse (other than in the case of a life annuity) may be redetermined but not more frequently than annually. (§401(a)(9)(D))

Definitions & Rules Relating to Designated Beneficiaries (§401(a)(9)(E))

Designated beneficiary

The term "designated beneficiary" means any individual designated as a beneficiary by the employee.

Eligible designated beneficiary

The term "eligible designated beneficiary" means, with respect to any employee, any designated beneficiary who is:

1. the surviving spouse of the employee,
2. a child of the employee who has not reached majority (age 21) (withing the meaning of §401(a)(9)(F)).

NOTE - A child shall cease to be an eligible designated beneficiary as of the date the individual reaches majority and any remainder of the portion of the individual's interest shall be distributed within 10 years after such date.

3. disabled (within the meaning of §72(m)(7)),
4. a chronically ill individual (within the meaning of §7702B(c)(2), except that the requirements of subparagraph (A)(i) thereof shall only be treated as met if there is a certification that, as of such date, the period of inability described in such subparagraph with respect to the individual is an indefinite one which is reasonably expected to be lengthy in nature), or
5. an individual not described in any of the preceding subclauses who is not more than 10 years younger than the employee.

NOTE - The determination of whether a designated beneficiary is an eligible designated beneficiary shall be made as of the date of death of the employee.

RMD for IRA Beneficiaries Summary Chart – Death After 2019

	Designated Beneficiary		**No Designated Beneficiary**
	Eligible designated beneficiary	**Non-eligible designated beneficiary**	**Estate, charity and/or some trusts**
IRA owner dies on or after RBD (i.e., age 73)	ALAR rule	Years 1-9 - ALAR rule Year 10 - 10-year rule	ALAR rule will apply using owner's age at birthday in year of death.
IRA owner dies before RBD (i.e., age 73) or Roth IRA owner dies before or after the RBD	Life expectancy rule **or** 10-year rule	10-year rule	5-year rule

An **eligible designated beneficiary** is any of the following:

1. the surviving spouse of the employee (or IRA owner),
2. a child of the employee (or IRA owner) who has not reached majority (age 21),
3. disabled,
4. a chronically ill individual, or
5. an individual not described in any of the preceding subclauses who is not more than 10 years younger than the employee.

ALAR rule – At-least-as-rapidly (ALAR) rule requires RMDs each year after death when death occurs on or after the RBD. Distribute using single life expectancy table of the younger of 1) beneficiary's age in year after death or 2) owner's age at birthday in year of death. Reduce beginning life expectancy by 1 for each subsequent year.

5-year rule - Take entire balance by the end of the 5th year following year of death.

10-year rule - Take entire balance by the end of the 10th year following year of death. Minor child of the beneficiary can delay until they reach age 21. The 10-year rule applies if 1) the beneficiary is an eligible designated beneficiary who elects the 10-year rule (if the owner died before reaching their RBD); or 2) the beneficiary is a designated beneficiary who is not an eligible designated beneficiary, regardless of whether the owner died before reaching their RBD.

Life expectancy rule – This is an exception to the 5/10-year rule. The balance is payable to (or for the benefit of) a designated beneficiary over the life of such beneficiary (or over a period not extending beyond the life expectancy of such beneficiary) as long as such distributions begin no later than one year after the death of the employee. The date on which the distributions are required to begin with respect to surviving spouses will not be earlier than the date on which the employee would have attained the RBD (i.e., age 73).

Surviving spouse election to treating IRA as own - The surviving spouse of an individual may elect, to treat the surviving spouse's entire interest as a beneficiary in the individual's IRA (or the remaining part of that interest if distributions have begun) as the surviving spouse's own IRA.

RMD Final Regulations Issued

Final Regulations (TD 10001)

Amended §§1.401(a)(9)-1 through 1.401(a)(9)-9, 1.403(b)-6(e), and 1.408-8 apply for purposes of determining required minimum distributions for calendar years beginning on or after January 1, 2025. Amended §1.402(c)-2 applies for distributions made on or after January 1, 2025. Amended §54.4974-1 applies for taxable years beginning on or after January 1, 2025. For earlier years, taxpayers must apply the preexisting final regulations, but taking into account a reasonable, good faith interpretation of the amendments made by sections 114 and 401 of the SECURE Act. Compliance with the proposed regulations (REG-105954-20) will satisfy that requirement. For the 2023 and 2024 distribution calendar years, taxpayers must also take into account a reasonable, good faith interpretation of the amendments made by sections 107, 201, 202, 204, and 337 of the SECURE 2.0 Act.

- §1.401(a)(9)-0 - Required minimum distributions; table of contents
- §1.401(a)(9)-1 - Minimum distribution requirement in general
- §1.401(a)(9)-2 - Distributions commencing during an employee's lifetime
- §1.401(a)(9)-3 - Death before required beginning date
- §1.401(a)(9)-4 - Determination of the designated beneficiary
- §1.401(a)(9)-5 - Required minimum distributions from defined contribution plans
- §1.401(a)(9)-6 - Required minimum distributions for defined benefit plans and annuity contracts
- §1.401(a)(9)-7 - Rollovers and transfers
- §1.401(a)(9)-8 - Special rules
- §1.401(a)(9)-9 - Life expectancy and distribution period tables
- §1.402(c)-2 - Eligible rollover distributions
- §1.403(b)-6(e) - Minimum required distributions for eligible plans
- §1.408-8 - Distribution requirements for individual retirement plans
- §54.4974-1 - Excise tax on accumulations in qualified retirement plans

UPDATE – Notice 2024-35

A defined contribution plan that failed to make a specified RMD will not be treated as having failed to satisfy §401(a)(9) merely because it did not make that distribution. Thus, no excise tax under §4974 will be assessed. A specified RMD is any distribution that, under the interpretation included in the proposed regulations, would be required to be made in 2024 under a defined contribution plan or IRA for the year in which the employee (or designated beneficiary) died if that payment would be required to be made to:

- a designated beneficiary of an employee under the plan (or IRA owner) if: (1) the employee (or IRA owner) died in 2020, 2021, 2022, or 2023, and on or after the employee's (or IRA owner's) required beginning date, and (2) the designated beneficiary is not using the lifetime or life expectancy payments exception or
- a beneficiary of an eligible designated beneficiary (including a designated beneficiary who is treated as an eligible designated beneficiary) if: (1) the eligible designated beneficiary died in 2020, 2021, 2022, or 2023, and (2) that eligible designated beneficiary was using the lifetime or life expectancy payments.

  NOTE – Notice 2022-53 provided similar relief for 2021 and 2022 distributions. Notice 2023-54 provided similar relief for 2023 distributions.

Deductions & Adjustments

Basic Standard Deduction (§63(c)(2) & (7))

Individuals who do not elect to itemize deductions are allowed to deduct a standard deduction in determining taxable income. The term "standard deduction" means the sum of:

1. the basic standard deduction AND
2. the additional standard deduction.

NOTE 1 – The standard deduction amount depends on the taxpayer's filing status, whether the taxpayer is 65 or older or blind and whether an exemption can be claimed for the taxpayer by another taxpayer.

NOTE 2 – The standard deduction is not allowed for alternative minimum tax (AMT) purposes.

UPDATE - Basic Standard Deduction Permanently Increased (Post 2025)

The OBBB permanently extends the TCJA increases to the basic standard and further raises the amounts to $31,500 for married individuals filing a joint return (MFJ), $23,625 for head-of-household (HOH) filers, and $15,750 for all other individuals (single/MFS). The amount of the standard deduction is indexed for inflation using the C-CPI-U for taxable years beginning after December 31, 2018.

EFFECTIVE DATE – The OBBB provision is effective for tax years beginning after 2025.

Basic Standard Deduction			
IF the taxpayer's filing status is…	**The taxpayer's standard deduction is…**		
	2026	**2025**	**2024**
Single or married filing separate return	$15,750	$15,000	$14,600
Married filing joint return or qualifying widow(er) with dependent child	$31,500	$30,000	$29,200
Head of Household	$23,625	$22,500	$21,900

Additional Standard Deductions

Age 65 or Older or Blind (§63(f))

The taxpayer can take the higher standard deduction if they or their spouse is age 65 or older or blind and either:

1. the taxpayer files a joint return OR
2. the taxpayer files a separate return and can claim an exemption for the spouse because the spouse had no gross income and an exemption for the spouse could not be claimed by another taxpayer.

Additional Standard Deduction			
Filing Status	**2026**	**2025**	**2024**
Single	$2,050	$2,000	$1,950
Married	$1,650	$1,600	$1,550

Age 65 or Older
If the taxpayer does not itemize deductions, the taxpayer is entitled to a higher standard deduction if the taxpayer is age 65 or older at the end of the year.

Blindness
If the taxpayer is blind on the last day of the year and does not itemize deductions, the taxpayer is entitled to a higher standard deduction. The taxpayer qualifies for this benefit if they are totally or partly blind. If the taxpayer is partly blind, the taxpayer must get a certified statement from an eye doctor or registered optometrist that either:

1. the taxpayer CANNOT see better than **20/200** in the better eye with glasses or contact lenses
2. the taxpayer's field of vision is not more than **20 degrees**
3. If the taxpayer's eye condition will never improve beyond these limits, the statement should include this fact. The taxpayer must keep the statement in their records. If the taxpayer's vision can be corrected beyond these limits only by contact lenses that the taxpayer can wear only briefly because of pain, infection, or ulcers, the taxpayer can take the higher standard deduction for blindness if they otherwise qualify.

Standard Deduction for Dependents (§63(c)(5))

The standard deduction for an individual for whom an exemption can be claimed on another person's tax return is generally limited to the **greater of**:

1. annual amount adjusted for inflation:

2026	2025	2024
$1,350	$1,350	$1,300

Or

2. the individual's earned income for the year **plus** the following amount (but not more than the regular standard deduction amount):

2026	2025	2024
$450	$450	$450

NOTE - If the individual is 65 or older or blind, the standard deduction may be higher.

Earned Income Defined
Earned income is salaries, wages, tips, professional fees, and other amounts received as pay for work that the taxpayer actually performs. For purposes of the standard deduction, earned income also includes any part of a scholarship or fellowship grant that the taxpayer must include in their gross income.

Overall Limitation on Itemized Deductions (§68)

NOTE – Itemized deductions are reported on a *Schedule A (Form 1040) – Itemized Deductions*.

Phase-Out of Itemized Deductions – Pease Limitation (Pre-2018)

Prior to 2018, itemized deductions were reduced for high income taxpayers by the smaller of:

1. 3% of the amount by which the taxpayer's AGI exceeds the annual limits (for 2017: MFJ or surviving spouse $313,800, HOH $287,650, single $261,500 and MFS $156,900)

   or

2. 80% of the taxpayer's itemized deductions that were affected by the limit.

NOTE – All itemized deductions were subject to the limitations other than 1) medical and dental expenses, 2) investment interest expenses, 3) casualty and theft losses and 4) gambling losses.

Phase-Out Suspended (2018-2025) (§68(f))

The TCJA suspended the itemized deduction phase-out for high-income taxpayers for tax years 2018-2025.

NOTE – No itemized deductions were phased-out during this period.

New Limitation on Tax Benefit of Itemized Deductions (Post 2025)

UPDATE – The OBBB Act §70111 modifies IRC §68 and creates a new rule limiting itemized deductions of only taxpayers in the top 37% income tax bracket after 2025.

New limitation

In the case of an individual, the amount of the itemized deductions otherwise allowable for the taxable year (determined without regard to this section) shall be reduced by 2/37 (≈ 5.41%) of the lesser of:

1. such amount of itemized deductions, or
2. so much of the taxable income of the taxpayer for the taxable year (determined without regard to this section and increased by such amount of itemized deductions) as exceeds the dollar amount at which the 37% rate bracket begins with respect to the taxpayer.

NOTE 1 - No carve-outs: Every itemized deduction is subject to the haircut (e.g., gambling losses, medical expenses, charitable contributions).
NOTE 2 - No 80% cap: Unlike Pease, there's no maximum percentage reduction. However, the 2/37 (≈ 5.41%) calculation typically results in a smaller cut.

EXAMPLE - A joint filer has $200,000 of itemized deductions and $150,000 of taxable income exceeding the MFJ threshold for the year. The itemized deductions will be reduced by the lesser of:

1. 2/37 × $200,000 (total itemized deductions) = $10,811,

   or

2. 2/37 × $150,000 (TI + itemized deductions – 37% bracket threshold) = $8,108.

The allowed itemized deduction total is $191,891 (i.e., $200,000 – $8,108).

Medical & Dental Expenses (§213(a))

7.5% of AGI Limitation (After 2017)

There shall be allowed as a deduction the expenses paid during the taxable year, not compensated for by insurance or otherwise, for medical care of the taxpayer, his spouse, or a dependent (as defined in §152, determined without regard to §152(b)(1) (i.e., no dependents of dependents), §152(b)(2) (i.e., married dependents), and §152(d)(1)(B) (i.e., gross income less than the exemption amount)), to the extent that such expenses exceed 7.5% of adjusted gross income.

Limitation with respect to medicine & drugs (§213(b))

An amount paid during the taxable year for medicine or a drug shall be taken into account only if such medicine or drug is a prescribed drug or is insulin.

Medical Care (§213(d)(1))

The term "medical care" means amounts paid:

1. for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body. Reg. §1.213-1(e)(1)(ii) of provides that deductions for medical care expenses under §213 are limited to expenses "incurred primarily for the prevention or alleviation of a physical or mental defect or illness" and do not include deductions for expenses that are merely beneficial to an individual's general health.
2. for transportation primarily for and essential to medical care,
3. for qualified long-term care services (as defined in §7702B(c)), or
4. for insurance (including amounts paid as premiums relating to supplementary medical insurance for the aged) covering medical care referred to in 1 and 2 above or for any qualified long-term care insurance contract (as defined in §7702B(b)).

Medical Reimbursements

Amounts treated as expenses for medical care under §213(d) are eligible to be paid or reimbursed under a health flexible spending arrangement (health FSA), Archer medical savings account (Archer MSA), health reimbursement arrangement (HRA), or health savings account (HSA). However, if an amount is paid or reimbursed under a health FSA, Archer MSA, HRA, HSA, or any other health plan or otherwise, it is not a deductible expense under §213.

Planning Considerations

The proper timing of payments for medical care may enable a taxpayer to claim a medical expense deduction that would otherwise NOT be available without planning.

EXAMPLE – Kathleen (age 50) has an AGI of $40,000 in 2X13 and $50,000 in 2X14. She incurs medical expenses of $4,500 each year. If Kathleen pays her 2X13 medical expenses in 2X13, she would be allowed a $500 medical expense deduction in 2X13 ($4,500 minus $4,000 (10% X $40,000) and $0 in 2X14 ($4,500 minus $5,000 (10% X $50,000)). If Kathleen waits to pay her 2X13 expenses until 2X14, however, she would be allowed a $4,000 medical expense deduction in 2X14 ($9,000 minus $5,000).

Condom Safe Harbor (Notice 2024-71)

This notice provides a safe harbor for deductible medical expenses under §213 for amounts paid for condoms. Thus, the IRS will treat amounts paid for condoms as amounts paid for medical care under §213(d).

Table – Summary of Deductible & Non-Deductible Medical & Dental Expenses

The taxpayer CAN include…	The taxpayer CANNOT include…
• Bandages • Birth control pills prescribed by your doctor • Body scan • Braille books • Breast pump and supplies • Capital expenses for equipment or improvements to your home needed for medical care (see the worksheet in Pub. 502) • Diagnostic devices • Expenses of an organ donor • Eye surgery—to promote the correct function of the eye • Fertility enhancement, certain procedures • Guide dogs or other animals aiding the blind, deaf, and disabled • Hospital services fees (lab work, therapy, nursing services, surgery, etc.) • Lead-based paint removal • Legal abortion • Legal operation to prevent having children such as a vasectomy or tubal ligation • Long-term care contracts, qualified • Meals and lodging provided by a hospital during medical treatment • Medical services fees (from doctors, dentists, surgeons, specialists, and other medical practitioners) • Medicare Part D premiums • Medical and hospital insurance premiums • Nursing services • Oxygen equipment and oxygen • Part of life-care fee paid to retirement home designated for medical care • Physical examination • Pregnancy test kit • Prescription medicines (prescribed by a doctor) and insulin • Psychiatric and psychological treatment • Social security tax, Medicare tax, FUTA, and state employment tax for worker providing medical care (see Wages for nursing services below) • Special items (artificial limbs, false teeth, eye-glasses, contact lenses, hearing aids, crutches, wheelchair, etc.) • Special education for mentally or physically disabled persons • Stop-smoking programs • Transportation for needed medical care • Treatment at a drug or alcohol center (includes meals and lodging provided by the center) • Wages for nursing services • Weight loss, certain expenses for obesity	• Baby sitting and childcare • Bottled water • Contributions to Archer MSAs (see Pub. 969) • Diaper service • Expenses for your general health (even if following your doctor's advice) such as— • —Health club dues • —Household help (even if recommended by a doctor) • —Social activities, such as dancing or swimming lessons • —Trip for general health improvement • Flexible spending account reimbursements for medical expenses (if contributions were on a pre-tax basis) • Funeral, burial, or cremation expenses • Health savings account payments for medical expenses • Operation, treatment, or medicine that is illegal under federal or state law • Life insurance or income protection policies, or policies providing payment for loss of life, limb, sight, etc. • Maternity clothes • Medical insurance included in a car insurance policy covering all persons injured in or by your car • Medicine you buy without a prescription • Nursing care for a healthy baby • Prescription drugs you brought in (or ordered shipped) from another country, in most cases • Nutritional supplements, vitamins, herbal supplements, "natural medicines," etc., unless recommended by a medical practitioner as a treatment for a specific medical condition diagnosed by a physician • Surgery for purely cosmetic reasons • Toothpaste, toiletries, cosmetics, etc. • Teeth whitening • Weight-loss expenses not for the treatment of obesity or other disease

NOTE – This table came from IRS Publication 17. Also refer *to Publication 502 – Medical and Dental Expenses* for more guidance in this area.

Deductible Taxes & SALT Limitations

Deductible Taxes - General Rule (§164(a))

In general, the following taxes shall be allowed as a deduction for the taxable year within which paid or accrued:

1. State and local, and foreign, real property taxes.
2. State and local personal property taxes.
3. State and local, and foreign, income, war profits, and excess profits taxes.
4. The GST tax imposed on income distributions.

§162 & §212 related taxes

In addition, there shall be allowed as a deduction State and local, and foreign, taxes not described in the preceding sentence which are paid or accrued within the taxable year in carrying on a trade or business (§162) or an activity described in §212 (relating to expenses for production of income).

NOTE – These taxes are deductible in computing income on an individual's Schedule C, Schedule E, or Schedule F on such individual's tax return.

Acquisition or disposition taxes

Taxes (not described in the first sentence of this subsection) which is paid or accrued by the taxpayer in connection with an acquisition or disposition of property shall be treated as part of the cost of the acquired property or, in the case of a disposition, as a reduction in the amount realized on the disposition.

Deductibility Tests

The following two tests must be met for any tax to be deductible by the taxpayer:

1. the tax must be imposed on the taxpayer and
2. the tax must be paid during the tax year.

SALT Limitations (Post 2017) (§164(b)(6))

Individual taxpayers may claim an itemized deduction of up to the **applicable limitation (i.e., SALT Cap)** for the aggregate of:

1. State and local property taxes not paid or accrued in carrying on a trade or business, or an activity described in §212, and
2. State and local income, war profits, and excess profits taxes (or sales taxes in lieu of income, etc. taxes) paid or accrued in the taxable year.

NOTE – Foreign real property taxes may not be deducted under this exception.

OBBB UPDATE - Applicable limitation & phase-down (2025-2029)

- The SALT deduction cap is retroactively increased to $40,000 (50% for MFS) for 2025 and then indexed upward by 1% annually through 2029.
- A phaseout applies for taxpayers with MAGI over $500,000 (50% for MFS) in 2025, increasing by 1% annually through 2029.
- For higher-income taxpayers, the SALT cap is reduced by 30% of the MAGI excess over the threshold, but cannot fall below $10,000.
- The cap reverts to $10,000 starting in 2030.

SALT Cap & Phase-Out Ranges – All taxpayers other than married filing separate (MFS)				
Tax Year	**SALT Cap**	**MAGI Threshold**	**Phase-Down Rate**	**Post-Phase-Down Minimum Cap**
2024	$10,000	N/A	N/A	$10,000
2025	$40,000	$500,000	30% of MAGI excess	$10,000
2026	$40,400	$505,000	30% of MAGI excess	$10,000
2027	$40,804	$510,050	30% of MAGI excess	$10,000
2028	$41,212	$515,151	30% of MAGI excess	$10,000
2029	$41,624	$520,302	30% of MAGI excess	$10,000
2030+	$10,000	N/A	N/A	$10,000
NOTE 1 – The SALT Cap, MAGI Threshold and Post-Phase-Down Minimum Cap amounts are 50% of the amounts above. **NOTE 2 –** MAGI means adjusted gross income increased by any amount excluded from gross income under §§911, 931, or 933.				

Recent Guidance

SALT Deduction & Tax Benefit Rule (Rev. Rul. 2019-11)

The IRS held that if a taxpayer received a tax benefit from deducting state or local taxes in a prior taxable year and the taxpayer recovers all or a portion of those taxes in the current taxable year, the taxpayer must include in gross income the lesser of:

1. the difference between the taxpayer's total itemized deductions taken in the prior year and the amount of itemized deductions the taxpayer would have taken in the prior year had the taxpayer paid the proper amount of state and local tax or
2. the difference between the taxpayer's itemized deductions taken in the prior year and the standard deduction amount for the prior year, if the taxpayer was not precluded from taking the standard deduction in the prior year.

NOTE – This holding applies to the recovery of any state or local tax, including state or local income tax and state or local real or personal property tax.

SALT Deduction & Home Office Expense Deduction (TAM 2019-001)

The IRS concluded that if a taxpayer's total individual state and local taxes meet or exceed the $10,000 limitation of §164(b)(6), or if the taxpayer chooses to take the standard deduction instead of itemizing deductions, none of the taxpayer's state and local taxes relating to taxpayer's business use of the home are included as expenses under §280A(b). If a taxpayer's total individual state and local taxes do not meet or exceed the $10,000 limitation of §164(b)(6), and the taxpayer does not opt to take the standard deduction in lieu of itemized deductions, then the taxpayer can include as expenses under §280A(b) the business portion of the state and local taxes up to the difference between the limitation under §164(b)(6) and the amount of individual state and local taxes that the taxpayer actually deducted under §164.

Summary of Deductible Taxes (IRS Pub. 17)		
	The Taxpayer Can Deduct	**The Taxpayer Cannot Deduct**
Fees and Charges	Fees and charges that are expenses of the taxpayer's trade/business or of producing income	- Fees and charges that are ***not*** expenses of the taxpayer's trade/ business or of producing income, such as fees for driver's licenses, car inspections, parking, or charges for water bills - Fines and penalties
Income Taxes	- State and local income taxes - Foreign income taxes - Employee contributions to state funds listed under *Contributions to state benefit funds*	- Federal income taxes - Employee contributions to private or voluntary disability plans - State and local general sales taxes if you choose to deduct state and local income taxes.
General Sales Tax	State and local general sales tax, including compensating use taxes.	State and local income taxes if the taxpayer chooses to deduct state and local general sales taxes
Other Taxes	- Taxes that are expenses of the taxpayer's trade/business or of producing income - Taxes on property producing rent or royalty income - One-half of self-employment tax paid	- Federal excise taxes, such as tax on gasoline, that are not expenses of your trade or business or production of income
Personal Property Taxes	State and local personal property taxes	Customs duties that are not expenses of your trade or business or of producing income
Real Estate Taxes	- State and local real estate taxes - Tenant's share of real estate taxes paid by cooperative housing corporation	- Real estate taxes that are treated as imposed on someone else - Foreign real estate taxes Taxes for local benefits (with exceptions) - Trash and garbage pickup fees (with exceptions) - Rent increase due to higher real estate taxes - Homeowners' association charges

Home Mortgage Interest (§163(h))

UPDATE - The OBBB permanently extends the limitation on acquisition indebtedness to $750,000 ($375,000 for married taxpayers filing separately) for purposes of the mortgage interest deduction and eliminates the deduction for interest on home equity indebtedness. Additionally, for tax years beginning after December 31, 2025, mortgage insurance premiums (PMI) are treated as qualified residence interest, making them deductible under the mortgage interest rules.

The term qualified residence interest means any interest which is paid or accrued during the taxable year on:

1. **acquisition indebtedness** with respect to any qualified residence of the taxpayer, or
2. **home equity indebtedness** with respect to any qualified residence of the taxpayer.

NOTE - The determination of whether any property is a qualified residence of the taxpayer shall be made as of the time the interest is accrued.

Acquisition indebtedness (§163(h)(3)(B))

The term acquisition indebtedness means any indebtedness which:

1. is incurred in acquiring, constructing, or substantially improving any qualified residence of the taxpayer, and
2. is secured by such residence.

NOTE - Such term also includes any indebtedness secured by such residence resulting from the refinancing of indebtedness meeting the requirements above; but only to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.

$1,000,000 limitation

The aggregate amount treated as acquisition indebtedness for any period shall not exceed $1,000,000 ($500,000 in the case of a married individual filing a separate return).

NOTE - Mortgages that the taxpayer took out on or before October 13, 1987 (called grandfathered debt) were not subject to this limitation.

Home equity indebtedness (§163(h)(3)(C))

The term home equity indebtedness means any indebtedness (other than acquisition indebtedness) secured by a qualified residence to the extent the aggregate amount of such indebtedness does not exceed:

1. the fair market value of such qualified residence, reduced by
2. the amount of acquisition indebtedness with respect to such residence.

Limitation

The aggregate amount treated as home equity indebtedness for any period shall not exceed $100,000 ($50,000 in the case of a separate return by a married individual).

Special rules for taxable years after 2017 (§163(h)(3)(F))

Home equity indebtedness disallowed

The OBBB permanently suspends the deduction for interest on home equity indebtedness. Thus, for taxable years beginning after December 31, 2017, a taxpayer may not claim a deduction for interest on home equity indebtedness.

Acquisition indebtedness limited

The OBBB permanently provides that, in the case of taxable years beginning after December 31, 2017, a taxpayer may treat no more than $750,000 as acquisition indebtedness ($375,000 in the case of married taxpayers filing separately). In the case of acquisition indebtedness incurred before December 15, 2017 this limitation is $1,000,000 ($500,000 in the case of married taxpayers filing separately).

Binding contract exception

In the case of a taxpayer who enters into a written binding contract before December 15, 2017, to close on the purchase of a principal residence before January 1, 2018, and who purchases such residence before April 1, 2018, the acquisition indebtedness limitation above shall be applied by substituting "April 1, 2018" for "December 15, 2017".

NOTE – This means that any taxpayer that meets the exception can use the $1,000,000/$500,000 limit.

Treatment of refinancing of indebtedness

In the case of any indebtedness which is incurred to refinance indebtedness, such refinanced indebtedness shall be treated for purposes of the indebtedness incurred on or before December 15, 2017 as incurred on the date that the original indebtedness was incurred to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.

NOTE – This rule shall not apply to any indebtedness after the expiration of the term of the original indebtedness or, if the principal of such original indebtedness is not amortized over its term, the expiration of the term of the 1st refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such 1st refinancing).

Examples at IRS Website

Example 1 – In January 2018, a taxpayer takes out a $500,000 mortgage to purchase a main home with a fair market value of $800,000. In February 2018, the taxpayer takes out a $250,000 home equity loan to put an addition on the main home. Both loans are secured by the main home and the total does not exceed the cost of the home. Because the total amount of both loans does not exceed $750,000, all of the interest paid on the loans is deductible. However, if the taxpayer used the home equity loan proceeds for personal expenses, such as paying off student loans and credit cards, then the interest on the home equity loan would not be deductible.

Example 2 – In January 2018, a taxpayer takes out a $500,000 mortgage to purchase a main home. The loan is secured by the main home. In February 2018, the taxpayer takes out a $250,000 loan to purchase a vacation home. The loan is secured by the vacation home. Because the total amount of both mortgages does not exceed $750,000, all of the interest paid on both mortgages is deductible. However, if the taxpayer took out a $250,000 home equity loan on the main home to purchase the vacation home, then the interest on the home equity loan would not be deductible.

Example 3 – In January 2018, a taxpayer takes out a $500,000 mortgage to purchase a main home. The loan is secured by the main home. In February 2018, the taxpayer takes out a $500,000 loan to purchase a vacation home. The loan is secured by the vacation home. Because the total amount of both mortgages exceeds $750,000, not all of the interest paid on the mortgages is deductible. A percentage of the total interest paid is deductible (see Publication 936).

Secured debt (§1.163-10T(o)(1))

The term "secured debt" means a debt that is on the security of any instrument (such as a mortgage, deed of trust, or land contract):

1. That makes the interest of the debtor in the qualified residence specific security for the payment of the debt,
2. Under which, in the event of default, the residence could be subjected to the satisfaction of the debt with the same priority as a mortgage or deed of trust in the jurisdiction in which the property is situated, and
3. That is recorded, where permitted, or is otherwise perfected in accordance with applicable State law.

NOTE – A debt will not be considered to be secured by a qualified residence if it is secured solely by virtue of a lien upon the general assets of the taxpayer or by a security interest, such as a mechanic's lien or judgment lien, that attaches to the property without the consent of the debtor.

Election to treat debt as not secured by the qualified residence

The regulations under §1.163-10T(o) and Publication 936 both state that taxpayers may make an election to treat a debt that is secured by a qualified residence as not secured by a qualified residence. This election is effective for the year it is made an all subsequent taxable years unless revoked with consent of the IRS (§1.163-10T(o)(5)).

NOTE – The election must apply to the entire indebtedness, and the election is made by reporting the interest on the return as business interest or other deductible interest rather than qualified residence interest. Late elections have been permitted under Reg. §301.9100.

Simplified & Exact methods (§1.163-10T)

Regulation §1.163-10T provides two methods for determining a taxpayer's qualified residence interest when debt exceeds the applicable limitations.

Simplified method (§1.163-10T(d))

Under the simplified method, interest on all secured debts is multiplied by a fraction, the numerator of which is the adjusted purchase price of the qualified residence and the denominator of which is the sum of the average balances of all secured debts. Since enactment of OBRA 1987 the $1,000,000 acquisition indebtedness limitation and the $100,000 home equity indebtedness limitation must be substituted for the adjusted purchase price.

NOTE – When the simplified method is used, a taxpayer is required to treat interest on ALL excess debt as personal interest under the temporary regulations (§1.163-10T(d)(2)).

Exact method (§1.163-10T(e))

Under the exact method, the amount of qualified residence interest is determined on a debt-by-debt basis by comparing the applicable debt limit for the debt to the average balance of each debt. The applicable debt limit is an amount that is different for each debt and is the lesser of the fair market value of the residence on the date the debt is secured and the adjusted purchase price of the qualified residence at the end of the taxable year, reduced by the average balance of each debt that was previously secured by the qualified residence. If the average balance of the debt does not exceed the limitation for that debt, all the interest on that debt is qualified residence interest. If the average balance of the debt exceeds the limitation, the amount of qualified residence interest is determined by multiplying the interest paid or accrued with respect to the debt by a fraction, the numerator of which is the applicable debt limit for that debt and the denominator of which is the average balance of the debt.

NOTE – Under the exact method, a taxpayer is permitted to treat interest on debt that exceeds the limitations according to the use of the debt proceeds under the interest tracing rules in §1.163-8T. See §1.163-10T(e)(4)).

With the substitution of the new statutory limitations into the exact method described in §1.163-10T(e), the regulations may be applied as modified by the statutory changes.

EXAMPLE – Assume a taxpayer owns one qualified residence that secures the following debts incurred in this order:

First: $900,000 acquisition debt

Second: $250,000 home equity debt allocated to personal expenditures

Third: $150,000 allocated to business expenditures

Under the new statutory limits, (1) the applicable debt limit for the first $900,000 debt is $1 million, all of the interest on which is deductible, (2) the applicable debt limit for the second $250,000 debt is $100,000, 10/25ths of the interest on which is deductible, and (3) the applicable debt limit for the third $150,000 debt is 0 ($100,000 reduced by the previous $250,000 debt).

However, since the third debt is allocable to business expenditures, interest on that debt would be deductible, regardless of whether the taxpayer had elected to treat the debt as not secured by the qualified residence, because under the exact method the taxpayer is permitted to treat interest that exceeds the limitation as traced to the particular expenditures for which the debt is used.

Qualified Residence Interest Q&As (CCA 201201017)

The IRS concluded that since the legislative history states that **until regulations are issued a reasonable method of allocating debt in excess of the limitation may be used**, taxpayers may use any reasonable method, including the exact method and the simplified method described in the regulations, the method provided in Publication 936 (similar to the simplified method in the regulations) or a reasonable approximation of those methods.

Conclusion to Question 1

A taxpayer may use any reasonable method, including the exact method, to determine the amount deductible as qualified residence interest when debt exceeds the acquisition and/or home equity debt limitations. Regardless of which reasonable method is used, a taxpayer may allocate the amounts that exceed the limitations in accordance with the use of the debt proceeds, as provided in §1.163-10T(e)(4) and the instructions to line 13 of Publication 936.

Conclusion to Question 2

A taxpayer using the exact method, or any other reasonable method, is not required to make the election under §1.163-10T(o)(5) in order to allocate the interest on the part of the debt that exceeds the qualified residence interest limitations under §1.163-8T. The election under §1.163-10T(o)(5) applies only to the whole amount of a debt and not to part. When the election is made under §1.163-10T(o)(5), the entire debt is treated as not secured by the residence; when the election is not made, only the portion of the debt that exceeds the limitation is traced according to the use of the debt proceeds.

Conclusion to Question 3

A taxpayer using the simplified method may allocate excess interest under the interest tracing rules of §1.163-8T, as described in the instruction to line 13 of the worksheet in Publication 936, without making an election under §1.163-10T(o)(5). The method provided for in Publication 936 is another reasonable method allowed by the legislative history.

Premiums for Mortgage Insurance (PMI)

UPDATE – The OBBB added a provision (§163(h)(3)(F)(iii)) allowing mortgage insurance premiums to be treated as qualified residence interest for tax years beginning after December 31, 2025.

Mortgage insurance premiums treated as interest (§163(h)(3)(E))

Premiums paid or accrued for qualified mortgage insurance by a taxpayer during the taxable year in connection with acquisition indebtedness with respect to a qualified residence of the taxpayer shall be treated as interest that is qualified residence interest.

NOTE – PMI is required to be reported on an annual Form 1098.

Phase-Out of Deduction

The amount otherwise treated as interest shall be reduced (but not below zero) by 10% of such amount for each $1,000 ($500 in the case of a married individual filing a separate return) (or fraction thereof) that the taxpayer's adjusted gross income for the taxable year exceeds $100,000 ($50,000 in the case of a married individual filing a separate return).

NOTE – The deduction is not allowed if the taxpayer's adjusted gross income exceeds $109,000 ($54,500 in the case of married individual filing a separate return).

Qualified Mortgage Interest Defined

For this purpose, qualified mortgage insurance means mortgage insurance provided by the Veterans Administration, the Federal Housing Administration, or the Rural Housing Administration, and private mortgage insurance (defined in section 2 of the Homeowners Protection Act of 1998 as in effect on the date of enactment of the provision). Amounts paid for qualified mortgage insurance that are properly allocable to periods after the close of the taxable year are treated as paid in the period to which they are allocated. No deduction is allowed for the unamortized balance if the mortgage is paid before its term (except in the case of qualified mortgage insurance provided by the Department of Veterans Affairs or Rural Housing Administration).

Charitable Contributions (§170) - Deduction Allowance & AGI Limitations

Allowance of deduction (§170(a))

There shall be allowed as a deduction any charitable contribution (as defined in §170(c)) payment of which is made within the taxable year.

NOTE - The contribution must be made within the tax year for it to be deductible in that year (i.e., the cash or accrual method of accounting governs timing, depending on the taxpayer's method).

Verification Requirement

A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary (e.g., receipts, written acknowledgments, or appraisals for larger gifts).

5 Year Carryover

Contributions in excess of the applicable percentage limits generally may be carried over and deducted over the next 5 taxable years, subject to the relevant percentage limitations on the deduction in each of those years.

NOTE – Current year contributions must be used prior to any carry forward contributions.

Contribution Limits & Ordering Rules – Pre-2026

Total deductible contributions of an individual taxpayer to public charities, private operating foundations, and certain types of private nonoperating foundations generally may not exceed 50% of the taxpayer's contribution base, which is the taxpayer's adjusted gross income for a taxable year (disregarding any net operating loss carryback). To the extent a taxpayer has not exceeded the 50% limitation, (1) contributions of capital gain property to public charities generally may be deducted up to 30% of the taxpayer's contribution base, (2) contributions of cash to most private nonoperating foundations and certain other charitable organizations generally may be deducted up to 30% of the taxpayer's contribution base, and (3) contributions of capital gain property to private foundations and certain other charitable organizations generally may be deducted up to 20% of the taxpayer's contribution base.

UPDATE – The OBBB permanently extends the rule under §170(b) that increases the 50% limitation for "cash" contributions to public charities and certain private foundations to 60% of the taxpayer's AGI. This rule applies for tax years beginning after December 31, 2017.

If contributions are subject to more than one of the limits discussed below, they get deducted as follows:

1. Contributions subject only to the 50% limit, up to 50% of your adjusted gross income.
2. Contributions subject to the 30% limit, up to the lesser of:
   a. 30% of adjusted gross income, or
   b. 50% of adjusted gross income minus your contributions to 50% limit organizations, including contributions of capital gain property subject to the special 30% limit.
3. Contributions of capital gain property subject to the special 30% limit, up to the lesser of:
   a. 30% of adjusted gross income, or
   b. 50% of adjusted gross income minus your other contributions to 50% limit organizations.
4. Contributions subject to the 20% limit, up to the lesser of:
   a. 20% of adjusted gross income,
   b. 30% of adjusted gross income minus your contributions subject to the 30% limit,

c. 30% of adjusted gross income minus your contributions of capital gain property subject to the special 30% limit, or
d. 50% of adjusted gross income minus the total of your contributions to 50% limit organizations and your contributions subject to the 30% limit.
5. Qualified conservation contributions (QCCs) subject to the special 50% limit, up to 50% of adjusted gross income minus any contributions in (1) through (4).
6. QCCs subject to the 100% limit for farmers and ranchers, up to 100% of adjusted gross income minus any contributions in (1) through (5).

50% Limit on Charitable Deductions

This limit applies to the total of all charitable contributions that the taxpayer makes during the year. This means that the taxpayer's deduction for charitable contributions cannot be more than 50% of their AGI for the year.

NOTE – A 30% limit also applies to these gifts if they are gifts of capital gain property for which the taxpayer figures their deduction using the FMV without reduction for appreciation.

The following is a partial list of the types of organizations that are 50% limit organizations:

- churches and conventions or associations of churches
- educational organizations with a regular faculty and curriculum that normally have a regularly enrolled student body attending classes on site
- hospitals and certain medical research organizations associated with these hospitals
- publicly supported charities
- private operating foundations
- private non-operating foundations that make qualifying distributions of 100% of contributions within 2½ months following the year they receive the contributions
- certain private foundations whose contributions are pooled in a common fund, the income and principal of which are paid to public charities

UPDATE – The OBBB permanently extends the rule under §170(b) that increases the 50% limitation for "cash" contributions to public charities and certain private foundations to 60% of the taxpayer's AGI. This rule applies for tax years beginning after December 31, 2017.

30% Limit on Charitable Deductions

A 30% limit applies to the following gifts:

- Gifts to all qualified organizations other than 50% limit organizations. This includes gifts to veterans' organizations, fraternal societies, nonprofit cemeteries, and certain private non-operating foundations.
- Gifts for the use of any organization.

NOTE – If these gifts are of capital gain property, they are subject to the 20% limit, described later, rather than the 30% limit.

Special 30% Limit for Capital Gain Property

A special 30% limit applies to gifts of capital gain property to 50% limit organizations. However, the special 30% limit does not apply when the taxpayer chooses to reduce the fair market value of the property by the amount that would have been long-term capital gain if the taxpayer had sold the property. Instead, only the 50% limit applies.

NOTE – For gifts of capital gain property to other organizations, see 20% Limit discussed next.

20% Limit on Charitable Deductions

This limit applies to all gifts of capital gain property to or for the use of qualified organizations other than gifts of capital gain property to 50% limit organizations.

Qualified conservation contributions

Qualified conservation contributions are one exception to the "partial interest" rule, which generally bars deductions for charitable contributions of partial interests in property. A qualified conservation contribution is a contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes.

NOTE – Qualified organizations include certain governmental units, public charities that meet certain public support tests, and certain supporting organizations.

A qualified real property interest is defined as:

1. the entire interest of the donor other than a qualified mineral interest;
2. a remainder interest; or
3. a restriction (granted in perpetuity) on the use that may be made of the real property.

Conservation purposes include:

1. the preservation of land areas for outdoor recreation by, or for the education of, the general public;
2. the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem;
3. the preservation of open space (including farmland and forest land) where such preservation will yield a significant public benefit and is either for the scenic enjoyment of the general public or pursuant to a clearly delineated Federal, State, or local governmental conservation policy; and
4. the preservation of an historically important land area or a certified historic structure.

50% AGI limitation with 15-year carryforward

The 30% contribution base limitation on deductions for contributions of capital gain property by individuals does not apply to qualified conservation contributions. Instead, individuals may deduct the fair market value of any qualified conservation contribution to the extent of the excess of 50% of the contribution base over the amount of all other allowable charitable contributions. These contributions are not taken into account in determining the amount of other allowable charitable contributions. Individuals are allowed to carry over any qualified conservation contributions that exceed the 50% limitation for up to 15 years.

100% AGI limitation for qualified farmer or rancher

In the case of an individual who is a qualified farmer or rancher for the taxable year in which the contribution is made, a qualified conservation contribution is deductible up to 100% of the excess of the taxpayer's contribution base over the amount of all other allowable charitable contributions.

NOTE – A qualified farmer or rancher means a taxpayer whose gross income from the trade or business of farming (within the meaning of §2032A(e)(5)) is greater than 50% of the taxpayer's gross income for the taxable year.

UPDATE - New 0.5% Floor on Individual Deductions – Post 2025

NOTE – The OBBB enacted new IRC §170(b)(1)(I). This provision is effective for tax years beginning after December 31, 2025.

Charitable contribution deductions shall be allowed only to the extent that the aggregate of such contributions exceeds 0.5% of the taxpayer's contribution base for the taxable year. This rule shall apply in the following order:

1. Capital gain property to non-50% organizations (subparagraph D)
2. Capital gain property to 50% organizations (subparagraph C)
3. Contributions to other non-50% organizations (subparagraph B)
4. Qualified conservation contributions (subparagraph E)
5. General contributions to 50% organizations (subparagraph A)
6. 60% cash gifts to 50% organizations (subparagraph G)

NOTE - The term contribution base means adjusted gross income (computed without regard to any net operating loss carryback to the taxable year under §172).

Special rules

- The 0.5% rule applies to both itemizers and non-itemizers.
- This rule applies before applying other percentage limitations.
- Carryforward are permitted, but only from years when total contributions exceeded the 0.5% floor.

Carryover of Contributions Disallowed by the 0.5% Floor (§170(d)(1)(C))

If total contributions in the current year do not exceed 0.5% of AGI, no carryforward is permitted. If the 0.5% floor is exceeded, contributions disallowed due to other AGI limitations (e.g., 20%, 30%, 60%) may be carried forward under the applicable rule.

Carryover Rule Defined

A "carryover rule" refers to the applicable provision that governs how excess charitable contributions are carried forward. The term carryover rule means:

1. §170(d)(1)(A) – General 5-year carryover
2. §170(b)(1)(C)(ii), (D)(ii), (E)(ii), (G)(ii) – Specific rules for capital gain property, conservation easements, and 60% cash gifts
3. Second sentence of §170(b)(1)(B) – 30% rule for other contributions

Applicable Carryover Rule

The "applicable" rule is determined based on the type of contribution (e.g., appreciated property to a 30% organization follows the 30% limitation rules).

1 - 63

Special Rule - Non-itemizer charitable deduction (Post 2025) (§170(p))

UPDATE – The OBBB provision is effective for taxable years beginning after 2025.

For any taxable year (beginning after 2025) in which an individual does not elect to itemize deductions under §63(g), the individual may claim a charitable contribution deduction equal the amount of otherwise allowable charitable contributions in cash, but not to exceed:

1. $1,000 for single filers, or
2. $2,000 for joint filers.

NOTE - The deduction is classified as a below-the-line deduction under §63(b)(4), meaning it reduces taxable income, not AGI.

Qualified Contributions

Only cash contributions made during the taxable year to qualified public charities described in §170(b)(1)(A) are eligible. The deduction must be determined without regard to:

1. increased AGI limits for disaster contributions,
2. increased limits for COVID-related contributions, and
3. the general carryover rules for excess charitable contributions.

Excluded Contributions

The deduction is not allowed for contributions:

1. To an organization described in §509(a)(3) (i.e., supporting organizations), or
2. For the establishment or maintenance of a donor-advised fund (as defined in §4966(d)(2)).

Casualty & Loss Limitations for Individuals

UPDATE – The OBBB permanently extended and modified the TCJA changes to §165(h)(5)(A).

General Rule for Deductible Losses (§165(a))

Taxpayers may deduct any loss sustained during the taxable year that is not compensated by insurance or otherwise.

NOTE - This general allowance applies to both business and personal losses, but personal losses are heavily limited under §165(c) and §165(h).

Amount of Deduction (§165(b))

The deduction amount is based on the adjusted basis of the property under §1011, as if the property were sold or otherwise disposed of. Any loss is reduced by:

1. Any insurance or other reimbursement received or expected, and
2. Any expected salvage value.

Limitation on Losses of Individuals (§165(c))

For individual taxpayers, deductible losses are limited to the following three categories:

1. **Trade or Business Losses** – losses incurred in a trade or business.
2. **Transactions Entered Into for Profit** – losses incurred in any transaction entered into for profit, even if not connected to a trade or business.
3. **Personal Casualty and Theft Losses** - personal property losses not connected with a trade or business or a profit transaction, only if they arise from fire, storm, shipwreck, or other casualty, or from theft.

   NOTE - These losses are further limited by IRC §165(h) (personal casualty loss rules).

Practice Note

- Personal casualty and theft losses are generally non-deductible unless arising from federally or state-declared disasters under current law.
- Personal casualty and theft losses are subject to floors and disaster limitations.
- Always reduce the loss by any insurance or reimbursement received or expected.
- Compute the loss using the lesser of adjusted basis or decline in fair market value, before applying any §165(h) limitations.
- Any loss arising from theft shall be treated as sustained during the taxable year in which the taxpayer discovers such loss (§165(e)).

When to Deduct a Loss?	
IF the taxpayer has a loss…	THEN deduct it in the year…
from a casualty	the loss occurred
in a presidentially declared disaster area	the disaster occurred or the year immediately before the disaster
from a theft	the theft was discovered

Per-Casualty Floor (§165(h)(1))

Any loss of an individual described in §165(c)(3) shall be allowed only to the extent that the amount of the loss to such individual arising from each casualty, or from each theft, exceeds:

1. $100 per casualty (general rule) or
2. $500 per casualty (qualified disaster relief).

This reduction applies to each total casualty or theft loss. It does not matter how many pieces of property are involved in an event. Only a single $100 reduction applies.

EXAMPLE – A hailstorm damages Will's home and car. Will determines the amount of loss for each of these items. Since the losses are due to a single event, Will combines the losses and reduces the combined amount by $100.

Generally, events closely related in origin cause a single casualty. It is a single casualty when the damage is from two or more closely related causes, such as wind and flood damage caused by the same storm. If the taxpayer has both gains and losses from casualties or thefts to personal-use property, the taxpayer must compare their total gains to their total losses. The taxpayer should do this after they have reduced each loss by any reimbursements and by $100.

CAUTION – Casualty or theft gains do not include gains that the taxpayer chooses to postpone.

If the taxpayer has both gains and losses from casualties or thefts to personal-use property, the taxpayer must compare their total gains to their total losses. The taxpayer should do this after they have reduced each loss by any reimbursements and by $100.

CAUTION – Casualty or theft gains do not include gains that the taxpayer chooses to postpone.

10% AGI Limitation (§165(h)(2))

The taxpayer must first reduce each personal-use casualty or theft loss by $100, then reduce the total of all such losses by 10% of their adjusted gross income.

NOTE - The 10% of AGI limitation waived for qualified disaster losses.

Losses > than Gains

If the taxpayer's losses are more than their recognized gains, subtract the gains from the losses and reduce the result by 10% of the taxpayer's AGI. The rest, if any, is the taxpayer's deductible loss.

Gains > than Losses

If the taxpayer's recognized gains are more than their losses, subtract the losses from the gains. The difference is treated as capital gain and must be reported on Schedule D (Form 1040).

NOTE – The 10% rule does not apply to gains.

Property Used Partly for Business and Partly for Personal Purposes

When property is used for both personal and business (or income-producing) purposes, the casualty or theft loss must be computed separately for each use. The $100-per-loss and 10%-of-AGI limitations apply only to the personal-use portion, while the business or income-producing portion is deductible under the regular business loss rules.

EXAMPLE – In June, Pam discovered that her house had been burglarized. Her loss after insurance reimbursement was $2,000. Pam's AGI for the year she discovered the theft is $29,500. Pam first applies the $100 rule and then the 10% rule. She figures her theft loss deduction as follows:

1) Loss after insurance	$2,000
2) Subtract $100	(100)
3) Loss after $100 rule	$1,900
4) Subtract 10% × $29,500 AGI	(2,950)
5) Theft loss deduction	$ –0–

Pam does not have a theft loss deduction because her losses after she applies the $100 rule ($1,900) is less than 10% of her adjusted gross income ($2,950).

Losses Limited to Disaster Areas After 2017 (§165(h)(5)(A))

In general (with limited exceptions below), in the case of an individual, any personal casualty loss which would be deductible in a taxable year beginning after December 31, 2017, shall be allowed as a deduction only to the extent it is attributable to a Federally declared disaster (as defined in §165(i)(5) or a State declared disaster (as defined in §165(h)(5)(C)).

UPDATE – The OBBB permanently extended the TCJA provision and added State declared disasters to taxable years beginning after 2025.

Exception related to personal casualty gains (§165(h)(5)(B))

If a taxpayer has personal casualty gains in a tax year, losses up to the amount of those gains can still be used to offset the gains even if the losses are not from a declared disaster.

NOTE - Any excess loss is deductible only if related to a federal or state-declared disaster, and the netting rules apply to prevent double-counting of gains.

State-Declared Disaster Defined (§165(h)(5)(C))

The term "State declared disaster" means, with respect to any State, any natural catastrophe (including any hurricane, tornado, storm, high water, wind-driven water, tidal wave, tsunami, earthquake, volcanic eruption, landslide, mudslide, snowstorm, or drought), or, regardless of cause, any fire, flood, or explosion, in any part of the State, which in the determination of the Governor of such State (or the Mayor, in the case of the District of Columbia) and the Secretary causes damage of sufficient severity and magnitude to warrant the application of the rules of this section.

NOTE – The term "State" includes the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

Special Rule for Qualified Disaster Personal Casualty Losses

NOTE - Section 304(b) of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 was permanently extended by the OBBB.

Normally, personal casualty losses are deductible only to the extent they exceed 10% of AGI after the $100 floor. With this special rule:

- Per-casualty floor is $500,
- 10% AGI limit waived for the net disaster loss,
- Loss can increase the standard deduction,
- Deduction applies for both regular tax and AMT.

Additional IRS Guidance

- FAQs for Disaster Victims – click here
- Tax Relief in Disaster Situations – click here
- Disaster Relief by State – click here
- Publication 547 – Casualties, Disasters, and Thefts
- Form 4684 – Casualties and Thefts
- Form 1040X - Amended U.S. Individual Income Tax Return

Miscellaneous Itemized Deductions NOT Subject to the 2% of AGI Limitation

UPDATE – Prior to 2018, taxpayers were allowed to deduct certain miscellaneous itemized deductions to the extent they exceeded 2% of their adjusted gross income. The TCJA temporarily suspended this deduction from 2018 to 2025. After 2025, the OBBB permanently repealed the miscellaneous itemized deduction and created new exceptions for educator expenses by adding them to the list of deductions not subject to §67 disallowance.

Miscellaneous itemized deductions are defined as all itemized deductions other than the following specifically listed exceptions:

1. Interest deductions under §163
2. Taxes under §164
3. Casualty and theft losses under §165(c)(2), §165(c)(3),
4. Gambling loss deductions under §165(d)
5. Charitable contributions under §170 and §642(c)
6. Medical and dental expenses under §213
7. Impairment-related work expenses
8. Estate tax deduction on income in respect of a decedent under §691(c)
9. Short sale expenses related to personal property
10. Restoration of amounts held under claim of right under §1341
11. Annuity loss deduction when annuity ends before investment is recovered under §72(b)(3)
12. Amortizable bond premium under §171
13. Co-op housing deductions under §216
14. Educator expenses under §162 (effective for tax years beginning after 12-31-2025)

NOTE - The taxpayer can deduct the items listed above as miscellaneous itemized deductions not subject to the 2% limit.

Amortizable Premium on Taxable Bonds

In general, if the amount you pay for a bond is greater than its stated principal amount, the excess is bond premium. You can elect to amortize the premium on taxable bonds. The amortization of the premium is generally an offset to interest income on the bond rather than a separate deduction item. Part of the premium on some bonds may be an itemized deduction on Schedule A (Form 1040). For more information, see Amortizable Premium on Taxable Bonds in Pub. 529, and Bond Premium Amortization in chapter 3 of Pub. 550, Investment Income and Expenses.

Casualty and Theft Losses of Income-Producing Property

You can deduct a casualty or theft loss as an itemized deduction on Schedule A (Form 1040), line 16, if the damaged or stolen property was income-producing property (property held for investment, such as stocks, notes, bonds, gold, silver, vacant lots, and works of art). First, report the loss in Form 4684, Section B. You may also have to include the loss on Form 4797, if you're otherwise required to file that form. To figure your deduction, add all casualty or theft losses from this type of property included on Form 4684, lines 32 and 38b, or Form 4797, line 18a. For more information on casualty and theft losses, see chapter 26.

Federal Estate Tax on Income in Respect of a Decedent

You can deduct the federal estate tax attributable to income in respect of a decedent that you as a beneficiary include in your gross income. Income in respect of the decedent is gross income that the decedent would have received had death not occurred and that wasn't properly includible in the decedent's final income tax return. See Pub. 559 for more information.

Impairment-Related Work Expenses

If you have a physical or mental disability that limits your being employed, or substantially limits one or more of your major life activities, such as performing manual tasks, walking, speaking, breathing, learning, and working, you can deduct your impairment-related work expenses. Impairment-related work expenses are ordinary and necessary business expenses for attendant care services at your place of work and for other expenses in connection with your place of work that are necessary for you to be able to work.

NOTE – If you're self-employed, enter your impairment-related work expenses on the appropriate form (Schedule C, C-EZ, E, or F) used to report your business income and expenses.

Repayments Under Claim of Right

If you had to repay more than $3,000 that you included in your income in an earlier year because at the time you thought you had an unrestricted right to it, you may be able to deduct the amount you repaid or take a credit against your tax. See Repayments in chapter 12 for more information.

Unlawful Discrimination Claims

You may be able to deduct, as an adjustment to income on Schedule 1 (Form 1040), line 22 or Form 1040NR, line 35, attorney fees and court costs for actions settled or decided after October 22, 2004, involving a claim of unlawful discrimination, a claim against the U.S. Government, or a claim made under section 1862(b)(3)(A) of the Social Security Act. However, the amount you can deduct is limited to the amount of the judgment or settlement you are including in income for the tax year. See Pub. 525 for more information.

Unrecovered Investment in Annuity

A retiree who contributed to the cost of an annuity can exclude from income a part of each payment received as a tax-free return of the retiree's investment. If the retiree dies before the entire investment is recovered tax free, any unrecovered investment can be deducted on the retiree's final income tax return. See chapter 10 for more information about the tax treatment of pensions and annuities.

Educator Expenses (§67(b)(13))

UPDATE - After 2025, the OBBB creates new exceptions for educator expenses by adding them to the list of deductions not subject to §67 disallowance.

Educator expenses (under §67(b)(13)(g)) means expenses similar to those described under §62(a)(2)(D) (above-the-line deduction for certain expenses of elementary and secondary school teachers), but with important modifications:

1. **No Dollar Cap –** The usual dollar limit (e.g., $300 per teacher) does not apply.
2. **Expanded Scope of Supplies** – The exclusion of nonathletic supplies for health/physical education (PE) is removed. All classroom-related supplies now qualify.
3. **Broader Instructional Setting** – The term “in the classroom” is replaced with “as part of instructional activity”, allowing for more flexible qualification.
4. **Expanded Eligible Roles** – The definition of “educator” includes interscholastic sports administrators and coaches, in addition to teachers, instructors, counselors, and principals.

NOTE - This change allows qualifying educator expenses to be deducted as itemized deductions without limitation and regardless of the 2% AGI floor, effective for tax years beginning after December 31, 2025.

Gambling Losses up to the Amount of Gambling Winnings

The taxpayer must include their gambling winnings in income on *Schedule 1 (Form 1040) – Additional Income & Adjustments*, line 8b. If the taxpayer itemizes their deductions on Schedule A, the taxpayer can deduct gambling losses that the taxpayer had during the year, but only up to the amount of the winnings.

CAUTION – A taxpayer cannot reduce their gambling winnings by gambling losses and report the difference. They must report the full amount of winnings as income and claim the losses (up to the amount of winnings) as an itemized deduction. Therefore, all records should show winnings separately from losses.

TCJA Limitations (2018-2025)

The TCJA of 2017 modified IRC §165(d) to provide that the term wagering losses includes any deduction otherwise allowable incurred in carrying on any wagering transaction **for taxable years beginning after 2017 and before 2026.** The provision is intended to clarify that the limitation on losses from wagering transactions applies not only to the actual costs of wagers incurred by an individual, but to other expenses incurred by the individual in connection with the conduct of that individual's gambling activity.

OBBB Limitation to Wagering Losses (Post 2025)

NOTE – The modification to §165(d) applies to taxable years beginning after December 31, 2025.

For purposes of losses from wagering transactions, the amount allowed as a deduction for any taxable year:

1. shall be equal to 90% of the amount of such losses during such taxable year, and
2. shall be allowed only to the extent of the gains from such transactions during such taxable year.

NEW RULE - The term 'losses from wagering transactions' includes any deduction otherwise allowable incurred in carrying on any wagering transaction.

EXAMPLE – Hotrod went to Las Vegas and had $23,000 in gambling winnings, $20,000 in gambling losses, and $5,000 in other wagering-related expenses, for a total of $25,000 in wagering-related deductions.

Step 1: Limit the $25,000 in wagering-related deductions to 90%, or $22,500.

Step 2: Compare the $22,500 from Step 1 to the gambling winnings. Since his winnings were $23,000, he can deduct the full $22,500.

Diary of winnings and losses

A taxpayer must keep an accurate diary or similar record of their losses and winnings. The diary should contain at least the following information:

1. The date and type of your specific wager or wagering activity.
2. The name and address or location of the gambling establishment.
3. The names of other persons present with you at the gambling establishment.
4. The amount(s) you won or lost.

NOTE – See Rev. Proc. 77-29 and *Publication 529 – Miscellaneous Deductions* for more information.

Self Employed Health Insurance Deduction (§162(l))

Taxpayer's Eligible for Deduction

A taxpayer may be able to deduct, as an adjustment to income, up to 100% of the amount paid for medical and qualified long-term care insurance on behalf of themselves, their spouse, and dependents. This provision applies to if the taxpayer was:

1. self-employed and had a net profit for the year,
2. was a general partner (or a limited partner receiving guaranteed payments) OR
3. received wages from an S corporation in which they were a more than 2% shareholder (who is treated as a partner).

Background – Health Insurance Deduction (§162(l))

Allowance of deduction on Schedule 1 (i.e., adjustment) of the Form 1040

In the case of a taxpayer who is an employee within the meaning of §401(c)(1) (i.e., this includes an individual who is self-employed), there shall be allowed as a deduction equal to the amount paid during the taxable year for insurance which constitutes medical care for the:

1. taxpayer,
2. taxpayer's spouse,
3. taxpayer's dependents, and
4. any child (as defined in §152(f)(1)) of the taxpayer who as of the end of the taxable year has not attained age 27.

NOTE – The Health Care and Education Reconciliation Act of 2010 added number 4 above effective as of March 30, 2010 (i.e., date of enactment).

Dollar Amount Limitation

No deduction shall be allowed to the extent that the amount of such deduction exceeds the taxpayer's earned income (within the meaning of §401(c)) derived by the taxpayer from the trade or business with respect to which the plan providing the medical care coverage is established.

Other coverage limitation

The deduction shall not apply to any taxpayer for any calendar month for which the taxpayer is eligible to participate in any subsidized health plan maintained by any employer of the taxpayer or of the spouse of, or any dependent, or child (as defined in §152(f)(1)) with respect to, the taxpayer. The preceding sentence shall be applied separately with respect to:

1. plans which include coverage for qualified long-term care services or are qualified long-term care insurance contracts, and
2. plans which do not include such coverage and are not such contracts.

NOTE – Per FSA 3042: The word "subsidized," as used in §162(l)(2)(B) generally refers to a health insurance plan where a participant is entitled to a federal income tax benefit by reason of his or her participation in the plan.

Deduction not allowed for self-employment tax purposes

The deduction allowable by reason of this subsection shall not be taken into account in determining an individual's net earnings from self-employment.

NOTE – The deduction is allowable on Form 1040, schedule 1 as an adjustment to gross income and not on Schedule C.

Treatment of certain S corporation shareholders
This subsection shall apply in the case of any individual treated as a partner under §1372(a), except that:

1. for purposes of this subsection, such individual's wages (as defined in §3121) from the S corporation shall be treated as such individual's earned income (within the meaning of §401(c)(1)), and
2. there shall be such adjustments in the application of this subsection as the Secretary may by regulations prescribe.

2% Shareholder Requirements for Deduction on Schedule 1 of Form 1040 (Notice 2008-1)

A 2% shareholder-employee in an S corporation, who otherwise meets the requirements of §162(l), is eligible for the deduction if the plan providing medical care coverage for the 2% shareholder-employee is established by the S corporation. A plan providing medical care coverage for the 2% shareholder-employee in an S corporation is established by the S corporation if:

1. the S corporation makes the premium payments for the accident and health insurance policy covering the 2% shareholder-employee (and his or her spouse or dependents, if applicable) in the current taxable year;

   OR

2. the 2% shareholder makes the premium payments and furnishes proof of premium payment to the S corporation and then the S corporation reimburses the 2% shareholder-employee for the premium payments in the current taxable year.

NOTE – If the accident and health insurance premiums are not paid or reimbursed by the S corporation and included in the 2% shareholder-employee's gross income, a plan providing medical care coverage for the 2% shareholder-employee is not established by the S corporation and the 2% shareholder-employee in an S corporation is NOT allowed the deduction under §162(l).

CAUTION – In order for the 2% shareholder-employee to deduct the amount of the accident and health insurance premiums, the S corporation must report the accident and health insurance premiums paid or reimbursed as wages on the 2% shareholder-employee's Form W-2 in that same year. In addition, the shareholder must report the premium payments or reimbursements from the S corporation as gross income on his or her Form 1040, U.S. Individual Income Tax Return.

Form 7206 - Self-Employed Health Insurance Deduction

This form and its separate instructions have replaced the Self-Employed Health Insurance Deduction Worksheet that was previously published as a worksheet in Pub. 535, Business Expenses. Use this form and its instructions to determine any amount of the self-employed health insurance deduction you may be able to claim and report on Schedule 1 (Form 1040), line 17.

Health Savings Accounts (HSAs)

HSA Background

Individuals with a high deductible health plan (and no other health plan other than a plan that provides certain permitted coverage) may establish a health savings account (HSA). In general, HSAs provide tax-favored treatment for current medical expenses as well as the ability to save on a tax-favored basis for future medical expenses.

NOTE – HSAs are tax-exempt trusts or custodial accounts created exclusively to pay for the qualified medical expenses of the account holder and his or her spouse and dependents. Distributions from the HSA will be reported by the trustee on a Form 1099-SA. Both contributions to and distributions from a HSA are reported on a Form 8889.

Eligible Individual Defined

An "eligible individual" can establish an HSA. An "eligible individual" means, with respect to any month, any individual who:

1. is covered under a high-deductible health plan (HDHP) on the first day of such month;
2. is not also covered by any other health plan that is not an HDHP (with certain exceptions for plans providing certain limited types of coverage);
3. is not enrolled in Medicare (generally, has not yet reached age 65);
   AND
4. may not be claimed as a dependent on another person's tax return.

NOTE – An individual with other coverage in addition to a high deductible health plan is still eligible for an HSA if such other coverage is certain permitted insurance or permitted coverage.

Other Coverage

Generally, an individual is ineligible for an HSA if the individual, while covered under an HDHP, is also covered under a health plan (whether as an individual, spouse, or dependent) that is not an HDHP. An individual does not fail to be eligible for an HSA merely because, in addition to an HDHP, the individual has coverage for any benefit provided by "permitted insurance." **Permitted insurance is:**

1. insurance under which substantially all of the coverage provided relates to:
   a. liabilities incurred under workers' compensation laws,
   b. tort liabilities,
   c. liabilities relating to ownership or use of property (e.g., automobile insurance),
2. insurance for a specified disease or illness, and
3. insurance that pays a fixed amount per day (or other period) of hospitalization.

NOTE – An individual does not fail to be eligible for an HSA merely because, in addition to an HDHP, the individual has coverage (whether provided through insurance or otherwise) for accidents, disability, dental care, vision care, or long-term care.

Health flexible spending arrangement (“FSAs”) and health reimbursement arrangements (“HRAs”) are health plans that constitute other coverage under the HSA rules. An individual who is covered by a high deductible health plan and a health FSA or HRA generally is not eligible to make contributions to an HSA. An individual is eligible to make contributions to an HSA if the health FSA or HRA is:

1. a limited purpose health FSA or HRA;
2. a suspended HRA;

3. a post-deductible health FSA or HRA; or
4. a retirement HRA.

High Deductible Health Plan (HDHP) Defined

Generally, an HDHP is a health plan that satisfies certain requirements with respect to deductibles and out-of-pocket expenses. Amounts are indexed for inflation. A plan does not fail to qualify as an HDHP merely because it does not have a deductible (or has a small deductible) for preventive care (e.g., first dollar coverage for preventive care).

NOTE – However, except for preventive care, a plan may not provide benefits for any year until the deductible for that year is met.

UPDATE – The OBBB updates IRC §223(c)(2)(E) after 2024 (§223(c)(2)(E))

A plan shall not fail to be treated as a high deductible health plan by reason of failing to have a deductible for telehealth and other remote care services.

UPDATE - Expanded definition of HDHP (Post 2025): (§223(c)(2)(H))

The OBBB expands the definition of an HDHP to include any plan that is (i) sold as individual coverage on an Exchange, and (ii) classified as Bronze (§1302(d)(1)(A)) or Catastrophic (§1302(e)). Effective for months after 2025.

UPDATE – Direct primary care (DPC) service arrangements (Post 2025): (§223(c)(1)(E))

The OBBB permits participation in DPC service arrangements without loss of HSA eligibility, provided certain requirements are met. Thus, DPC fees for these arrangements are now qualified medical expenses for HSA purposes, effective for months after December 31, 2025.
What counts: Fixed periodic-fee primary care by primary care practitioners (SSA §1833(x)(2)(A)).
Excludes: (i) procedures needing general anesthesia; (ii) prescription drugs (except vaccines); (iii) labs not typically done in an ambulatory primary-care setting.
Cap: Per month ≤ $150 (single) / $300 (covers >1 individual); indexed for tax years after 2026 (base 2025).

High-deductible health plan (HDHP)?

The term "high deductible health plan" (i.e., HDHP) means a health plan:

4. which has an **annual deductible which is not less than:**

	Self-only coverage	Family coverage
2024	$1,600	$3,200
2025	$1,650	$3,300
2026	$1,700	$3,400

AND

5. the sum of the annual deductible and the other **annual out-of-pocket expenses** required to be paid under the plan (other than for premiums) for covered benefits **does not exceed:**

	Self-only coverage	Family coverage
2024	$8,050	$16,100
2025	$8,300	$16,600
2026	$8,500	$17,000

Contributions to HSAs

Who Can Contribute?

Contributions to an HSA by or on behalf of an eligible individual are deductible (within limits) in determining adjusted gross income (i.e., "above-the-line") of the individual. In addition, employer contributions to HSAs (including salary reduction contributions made through a cafeteria plan) are excludable from gross income and wages for employment tax purposes.

NOTE – Earnings on amounts in HSAs are not taxable.

Employee & Employer Contributions

Contributions to an HSA may be made by both the individual and the individual's employer up to the annual limit. The annual contribution limits are increased for individuals who have attained age 55 (i.e.., catch-up contributions) by the end of the taxable year. All contributions are aggregated for purposes of the maximum annual contribution limit.

NOTE - Employer contributions are required to be reported on the employee's Form W-2.

Married Taxpayers

In the case of individuals who are married to each other and either spouse has family coverage, both spouses are treated as having only the family coverage with the lowest annual deductible. The annual contribution limit (without regard to the catch-up contribution amounts) is divided equally between the spouses unless they agree on a different division (after reduction for amounts paid from any Archer MSA of the spouses).

Aggregate Contribution Limits

All HSA contributions made by or on behalf of an eligible individual to an HSA are aggregated for purposes of applying the limit. The annual limit is decreased by the aggregate contributions to an Archer MSA. The same annual contribution limit applies whether the contributions are made by an employee, an employer, a self-employed person, or a family member.

NOTE – Unlike Archer MSAs, contributions may be made by or on behalf of eligible individuals even if the individuals have no compensation or if the contributions exceed their compensation.

If an individual has more than one HSA, the aggregate annual contributions to all the HSAs are subject to the limit.

Year	Maximum HSA Annual Contribution		
	Self Only H.I. Coverage	**Family H.I. Coverage**	**Catch-up (Age 55+)**
2024	$4,150	$8,300	$1,000
2025	$4,300	$8,550	$1,000
2026	$4,400	$8,750	$1,000

Taxation of Distributions

NOTE – The individual taxpayer will receive a *Form 1099-SA – Distributions from an HSA* reporting distributions from their Health Savings Account (HSA). The taxpayer must attach *Form 8889 – Health Savings Accounts (HDAs)* to their tax return to report and reconcile these distributions, indicating whether they were used for qualified medical expenses (and thus are nontaxable) or for other purposes (which may be taxable and subject to penalty)..

Non-Taxable Distributions

Distributions from an HSA for **qualified medical expenses** of the individual and his or her spouse or dependents generally are excludable from gross income. In general, amounts in an HSA can be used for qualified medical expenses even if the individual is not currently eligible for contributions to the HSA. Qualified medical expenses generally are defined as under §213(d) and include expenses for diagnosis, cure, mitigation, treatment, or prevention of disease. Qualified medical expenses do not include expenses for insurance other than for:

1. long-term care insurance,
2. premiums for health coverage during any period of continuation coverage required by Federal law,
3. premiums for health care coverage while an individual is receiving unemployment compensation under Federal or State law, or
4. in the case of an account beneficiary who has attained the age of Medicare eligibility, health insurance premiums for Medicare, other than premiums for Medigap policies.

NOTE – Such qualified health insurance premiums include, for example, Medicare Part A and Part B premiums, Medicare HMO premiums, and the employee share of premiums for employer-sponsored health insurance including employer-sponsored retiree health insurance. Whether the expenses are qualified medical expenses is determined as of the time the expenses were incurred.

For purposes of determining the itemized deduction for medical expenses, distributions from an HSA for qualified medical expenses are not treated as expenses paid for medical care under §213.

Qualified Medical Expenses - IRC §223(d)(2)(A)

The term "qualified medical expenses" means, with respect to an account beneficiary, amounts paid by such beneficiary for medical care (as defined in §213(d)) for such individual, the spouse of such individual, and any dependent (as defined in §152, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof) of such individual, but only to the extent such amounts are not compensated for by insurance or otherwise. For purposes of this subparagraph, amounts paid for menstrual care products shall be treated as paid for medical care.

UPDATE – For months beginning after 2025, the OBBB modifies §223(d)(2)(C)(v) to include any direct primary care (DPC) service arrangement as qualified medical expenses.

Taxable Distributions & 20% Penalty

Distributions from an HSA that are not for qualified medical expenses are includible in gross income and subject to an additional 20% tax unless made:

1. after death,
2. disability, or
3. the individual attains the age of Medicare eligibility (i.e., age 65).

One Big Beautiful Bill Temporary Adjustments

UPDATE – There is a new *Form 1040, Schedule 1-A – Additional Deductions*, which will be used to calculate deductions for seniors, qualified tips, overtime pay and passenger vehicle loan interest. Click here for IRS Fact Sheet on the OBBB tax deductions.

Deduction for Seniors (2025-2028)

Temporary Deduction for Seniors (§151(d)(5)(C))

In the case of a taxable year beginning before January 1, 2029, there shall be allowed a deduction in an amount equal to $6,000 for each qualified individual with respect to the taxpayer.

NOTE – This shall apply to taxable years beginning after December 31, 2024.

Qualified individual

The term "qualified individual" means:

1. the taxpayer, if the taxpayer has attained age 65 before the close of the taxable year, and
2. in the case of a joint return, the taxpayer's spouse, if such spouse has attained age 65 before the close of the taxable year.

NOTE - If the taxpayer is a married individual (within the meaning of §7703), this subparagraph shall apply only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.

Limitation based on MAGI

In the case of any taxpayer for any taxable year, the $6,000 deduction amount for seniors shall be reduced (but not below zero) by 6% of so much of the taxpayer's modified adjusted gross income as exceeds $75,000 ($150,000 in the case of a joint return).

Modified adjusted gross income

The term "modified adjusted gross income" means the adjusted gross income of the taxpayer for the taxable year increased by any amount excluded from gross income under IRC §§911, 931, or 933 (i.e., specific exclusions from gross income for U.S. taxpayers with certain types of foreign or territorial income).

Social security number required

The deduction for seniors shall not apply with respect to a qualified individual unless the taxpayer includes such qualified individual's social security number on the return of tax for the taxable year.

NOTE - The term "social security number" has the meaning given such term in §24(h)(7).

Deduction for Qualified Tips (No Tax On Tips) (2025-2028)

UPDATE – The OBBB added new IRC §224 providing a temporary (2025-2028) above the line deduction of up to $25,000 for qualified tips for employees and self-employed individuals.

General rule

There shall be allowed as a deduction an amount equal to the qualified tips received during the taxable year that are reported on one of the following forms or other IRS-approved statements:

IRC Section	Form	Purpose
§6041(d)(3)	Form 1099-NEC	Nonemployee compensation tips (requires separate tip and occupation reporting)
§6041A(e)(3)	Form 1099-MISC	Service/direct sales payments, including tipped compensation
§6050W(f)(2)	Form 1099-K	Tips processed via TPSOs (e.g., Square, PayPal)
§6051(a)(18)	Form W-2	Cash tips reported by employees, plus occupation field
N/A	Form 4137	Unreported tips submitted by employee; triggers possible §224 deduction

Deduction Limitation

The amount allowed as a deduction under this section for any taxable year shall not exceed $25,000.

NOTE - The above the line deduction is available whether or not the taxpayer itemizes deductions.

Limitation based on MAGI

The amount allowable as a deduction shall be reduced (but not below zero) by $100 for each $1,000 by which the taxpayer's modified adjusted gross income exceeds $150,000 ($300,000 in the case of a joint return).

NOTE - MAGI means the taxpayer's adjusted gross income for the taxable year increased by any amounts excluded from gross income under §911 (foreign earned income exclusion), §931 (income from Guam, American Samoa, or the Northern Mariana Islands), or §933 (income from Puerto Rico).

Tips received in course of trade or business

In the case of qualified tips received by an individual during any taxable year in the course of a trade or business (other than the trade or business of performing services as an employee) of such individual, such qualified tips shall be taken into account only to the extent that the gross income for the taxpayer from such trade or business for such taxable year (including such qualified tips) exceeds the sum of the deductions (other than the deduction allowed under this section) allocable to the trade or business in which such qualified tips are received by the individual for such taxable year.

Qualified tips

The term "qualified tips" means cash tips received by an individual in an occupation which customarily and regularly received tips on or before December 31, 2024, as provided by the Secretary.

NOTE - The term "cash tips" includes tips received from customers that are paid in cash or charged and, in the case of an employee, tips received under any tip-sharing arrangement. Click here for a list of occupations that customarily and regularly receive tips.

Exclusions
Such term shall not include any amount received by an individual unless:

1. such amount is paid voluntarily without any consequence in the event of nonpayment, is not the subject of negotiation, and is determined by the payor,
2. the trade or business in the course of which the individual receives such amount is not a specified service trade or business (SSTB) (as defined in §199A(d)(2)), and
3. such other requirements as may be established by the Secretary in regulations or other guidance are satisfied.

NOTE - For purposes of subparagraph 2, in the case of an individual receiving tips in the trade or business of performing services as an employee, such individual shall be treated as receiving tips in the course of a trade or business which is a SSTB if the trade or business of the employer is a SSTB.

Other Requirements

Social security number required
No deduction shall be allowed under this section unless the taxpayer includes on the return of tax for the taxable year such individual's social security number.

Married individuals
If the taxpayer is a married individual, this section shall apply only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.

Regulations
The Secretary shall prescribe such regulations or other guidance as may be necessary to prevent reclassification of income as qualified tips, including regulations or other guidance to prevent abuse of the deduction allowed by this section.

No Tax on Overtime (2025-2028)

UPDATE - The OBBB added new IRC §225 providing a temporary (2025-2028) deduction for individuals who receive qualified overtime compensation.

General rule

There shall be allowed as a deduction an amount equal to the qualified overtime compensation received during the taxable year and included on statements furnished to the individual pursuant to

IRC Section	Form	Purpose
§6041(d)(4)	Form 1099-NEC	Nonemployee compensation qualified overtime
§6051(a)(19)	Form W-2	Qualified overtime compensation reported by employees

Deduction Limitation

The amount allowed as a deduction under this section for any taxable year shall not exceed $12,500 ($25,000 in the case of a joint return).

NOTE - The above the line deduction is available whether or not the taxpayer itemizes deductions

Limitation based on MAGI

The amount allowable as a deduction shall be reduced (but not below zero) by $100 for each $1,000 by which the taxpayer's modified adjusted gross income exceeds $150,000 ($300,000 in the case of a joint return).

NOTE - MAGI means the taxpayer's adjusted gross income for the taxable year increased by any amounts excluded from gross income under §911 (foreign earned income exclusion), §931 (income from Guam, American Samoa, or the Northern Mariana Islands), or §933 (income from Puerto Rico

Qualified overtime compensation

Qualified overtime compensation means overtime compensation paid to an individual required under section 7 of the Fair Labor Standards Act of 1938 that is in excess of the regular rate (as used in such section) at which such individual is employed.

NOTE - Qualified overtime compensation shall not include any qualified tip (as defined in §224(d)).

Other Requirements

Social security number required

No deduction shall be allowed under this section unless the taxpayer includes on the return of tax for the taxable year such individual's social security number.

Married individuals

If the taxpayer is a married individual, this section shall apply only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.

Regulations

The Secretary shall prescribe such regulations or other guidance as may be necessary to prevent reclassification of income as qualified tips, including regulations or other guidance to prevent abuse of the deduction allowed by this section.

Qualified Passenger Vehicle Loan Interest (2025-2028)

UPDATE – The OBBB temporarily (2025-2028) allows an "above-the-line" deduction of up to $10,000 for personal interest on qualified passenger vehicle loans. The deduction begins phasing out for taxpayers with modified adjusted gross income over $100,000 ($200,000 for joint filers). This applies only to new, U.S.-assembled vehicles purchased for personal use. Lease financing, used vehicles, and commercial/fleet loans are excluded. (§163(h) & §63(b))

Temporary $10,000 Deduction for Car Loan Interest (2025–2028)

For tax years beginning after December 31, 2024, and before January 1, 2029, the definition of personal interest under §163(h) will exclude "qualified passenger vehicle loan interest". This effectively allows taxpayers to deduct certain car loan interest that would otherwise be nondeductible personal interest.

Deduction Available to Non-Itemizers

IRC §63(b) provides that the deduction for qualified passenger vehicle loan interest is allowed "above-the-line". Thus, taxpayers do not need to itemize deductions to claim this benefit.

Qualified Passenger Vehicle Loan Interest – Definition

Qualified passenger vehicle loan interest is interest paid or accrued during the tax year on debt that:

1. Is incurred after December 31, 2024,
2. Is used to purchase an applicable passenger vehicle,
3. Is secured by a first lien on that vehicle, and
4. The vehicle is purchased for personal use.

Exceptions (Not Qualified)

The following are not considered qualified passenger vehicle loan interest:

1. Loans for fleet sales,
2. Loans for commercial vehicles not used for personal purposes,
3. Lease financing,
4. Loans for salvage-title vehicles,
5. Loans to purchase vehicles intended for scrap or parts.

VIN Requirement

The vehicle identification number (VIN) of the vehicle must be reported on the tax return in any year the deduction is claimed.

Limitations

Dollar Limit

The maximum deductible amount of qualified passenger vehicle loan interest is $10,000 per taxpayer per tax year.

Modified Adjusted Gross Income (MAGI) Phaseout

The otherwise allowable deduction is reduced (but not below zero) by $200 for every $1,000 (or fraction) by which the taxpayer's MAGI exceeds:

- $100,000 for single/MFS filers,
- $200,000 for joint filers.

NOTE - MAGI is defined as adjusted gross income plus any amounts excluded from gross income under IRC §§911, 931, or 933 (e.g., foreign earned income exclusion).

1 - 81

Applicable Passenger Vehicle – Definition

To qualify, a vehicle must:

1. Have original use that begins with the taxpayer,
2. Be manufactured primarily for use on public roads,
3. Have at least two wheels,
4. Be a car, minivan, van, SUV, pickup truck, or motorcycle,
5. Be considered a motor vehicle for purposes of the Clean Air Act,
6. Have a gross vehicle weight rating (GVWR) less than 14,000 pounds, and
7. Have final assembly in the United States.

NOTE - Vehicles failing any of the above tests do not qualify.

Final assembly in the United States

The location of final assembly will be listed on the vehicle information label attached to each vehicle on a dealer's premises. Alternatively, taxpayers may rely on the vehicle's plant of manufacture as reported in the vehicle identification number (VIN) to determine whether a vehicle has undergone final assembly in the United States. The VIN Decoder website for the National Highway Traffic Safety Administration (NHTSA) provides plant of manufacture information. Taxpayers can follow the instructions on that website to determine if the vehicle's plant of manufacture was located in the United States.

Special Rules and Definitions

Final Assembly

Final assembly is defined as the manufacturing process at a U.S. plant where the vehicle is fully assembled and ready for delivery to a dealer.

Refinancing

Refinanced debt qualifies only up to the principal amount of the original qualifying loan and must remain secured by a first lien on the same vehicle.

Related-Party Loans

Loans from related parties (as defined in IRC §§267(b) and 707(b)(1)) do not qualify.

Reporting Requirements (New §6050AA)

- Lenders and other recipients of qualified passenger vehicle loan interest must file information returns with the IRS and provide statements to taxpayers showing the total qualified interest received each year.
- Taxpayers will need these statements (similar to Form 1098 for mortgage interest) to substantiate their deduction.

NOTE - Transition relief will be provided for the 2025 tax year for lenders adapting to the new reporting requirements.

Additional Guidance

IRS Fact Sheet (07-14-25) - OBBB Act: Tax deductions for working Americans and seniors.

Individual Taxes

Individual, Estates & Trust Income Tax Rates (§1)

UPDATE – The OBBB makes the TCJA tax rate reductions and bracket changes, marriage penalty fix, and capital gains/qualified income breakpoints permanent. Thus, the seven tax rates applicable for individuals (i.e., 10%, 12%, 22%, 24%, 32%, 35%, and 37%) will remain in effect and will not revert back to the pre-2018 rate (i.e., 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%).

	2026	2025	2024
Beginning of 12% Bracket (10% below)			
Married filing joint & surviving spouse	$24,800	$23,850	$23,200
Single	$12,400	$11,925	$11,600
Head of household (HOH)	$17,700	$17,000	$16,550
Married filing separate	$12,400	$11,925	$11,600
Estates & non-grantor trusts	N/A	N/A	N/A
Beginning of 22% Bracket			
Married filing joint & surviving spouse	$100,800	$96,950	$94,300
Single	$50,400	$48,475	$47,150
Head of household (HOH)	$67,450	$64,850	$63,100
Married filing separate	$50,400	$48,475	$47,150
Estates & non-grantor trusts	N/A	N/A	N/A
Beginning of 24% Bracket			
Married filing joint & surviving spouse	$211,400	$206,700	$201,050
Single	$105,700	$103,350	$100,525
Head of household (HOH)	$105,700	$103,350	$100,500
Married filing separate	$105,700	$103,350	$100,525
Estates & non-grantor trusts (below at 10%)	$3,300	$3,150	$3,100
Beginning of 32% Bracket			
Married filing joint & surviving spouse	$403,550	$394,600	$383,900
Single	$201,775	$197,300	$191,950
Head of household (HOH)	$201,750	$197,300	$191,950
Married filing separate	$201,775	$197,300	$191,950
Estates & non-grantor trusts	N/A	N/A	N/A
Beginning of 35% Bracket			
Married filing joint & surviving spouse	$512,450	$501,050	$487,450
Single	$256,225	$250,525	$243,725
Head of household (HOH)	$256,200	$250,500	$243,700
Married filing separate	$256,225	$250,525	$243,725
Estates & non-grantor trusts	$11,700	$11,450	$11,150
Beginning of 37% Bracket			
Married filing joint & surviving spouse	$768,700	$751,600	$731,200
Single	$640,600	$626,350	$609,350
Head of household (HOH)	$640,600	$626,350	$609,350
Married filing separate	$384,350	$375,800	$365,600
Estates & non-grantor trusts	$16,000	$15,650	$15,200

Long-Term Capital Gain (LTCG) & Qualified Dividend Rates

Maximum Long-Term Capital Gain Rates			
IF the taxpayer's net capital gain is from …	**THEN the taxpayer's maximum capital gain rate is …**		
Collectibles gain	**28%**		
Gain on qualified small business stock equal to the §1202 exclusion	**28%**		
Unrecaptured §1250 gain (i.e., depreciation gains on real estate not taxed as ordinary income under §1250)	**25%**		
All other long-term capital gains	**20%, 15% or 0% rate (see breakpoint chart below)**		
	2026	**2025**	**2024**
15% LTCG & Qualifying Dividend Tax Rate Beginning (0% below)			
Married filing joint & surviving spouse	$98,900	$96,700	$94,050
Single	$49,450	$48,350	$47,025
Head of household (HOH)	$66,200	$64,750	$63,000
Married filing separate	$49,450	$48,350	$47,025
Estates and non-grantor trusts	$3,300	$3,250	$3,150
20% LTCG & Qualifying Dividend Tax Rate Beginning			
Married filing joint & surviving spouse	$613,700	$600,050	$583,750
Single	$545,500	$566,700	$518,900
Head of household (HOH)	$579,600	$551,350	$551,350
Married filing separate	$306,850	$300,000	$291,875
Estates and non-grantor trusts	$16,250	$15,900	$15,450

28% LTCG Rate – Collectibles & §1202 Gains

28% LTCG Calculation

The term 28% rate gain means the excess (if any) of:

1. The sum of:
    a. collectibles gain AND
    b. §1202 gain (i.e., qualified small business stock)

   OVER

2. the sum of:
    a. collectibles loss;
    b. the net short-term capital loss; and
    c. the amount of long-term capital loss carried forward to the taxable year.

NOTE – If the losses in step 2 above exceed the 28% LTCG, the excess losses will be used next to offset any of the 25% unrecaptured §1250 gain, then the 15% LTCGs.

Collectibles Gain & Loss Defined

The terms "collectibles gain" and "collectibles loss" mean gain or loss (respectively) from the sale or exchange of a collectible which is a capital asset held for more than 1 year but only to the extent such gain is taken into account in computing gross income and such loss is taken into account in computing taxable income. A collectible means any:

1. work of art,
2. rug or antique,
3. metal or gem,
4. stamp or coin,
5. alcoholic beverage OR
6. metal (such as gold, silver, and platinum bullion).

§1202 Gain on Qualified Small Business Stock

If the taxpayer realized a gain from qualified small business stock that they held more than 5 years, they generally can exclude ½ of the gain from income. The ½ of the taxable gain is taxed at a maximum LTCG rate of 28%. The amount of gain eligible for the 50% exclusion in any one taxable year is limited to the greater of:

1. 10 times the taxpayer's basis in the stock (an annual limitation) OR
2. $10 million ($5 million for MFS) gain reduced by the aggregate amount of eligible gain taken for prior taxable years from the sale of stock in that corporation (an aggregate limitation).

OBBB UPDATE – For stock acquired after July 4, 2025, the OBBB increases the cap to $15 million ($7.5 million for MFS) (adjusted for inflation), reduced by prior eligible gain excluded.

Requirements

To be QSB stock, the stock must meet all of the following tests:

1. It must be **stock in a C corporation** (that is, not S corporation stock).
2. It must have been originally issued **after 08-10-1993.**
3. As of the date the stock was issued, the corporation was a domestic C corporation with total **gross assets not in excess of $75 million (adjusted for inflation)**:
    a. at all times after 08-09-1993, and before the stock was issued, and
    b. immediately after the stock was issued.

    NOTE – Gross assets include those of any predecessor of the corporation. All corporations that are members of the same parent-subsidiary controlled group are treated as one corporation.

4. The taxpayer must have acquired the stock at its original issue, either in exchange for money or other property or as pay for services to the corporation. In certain cases, the taxpayer may meet the test if they acquired the stock from another person who met the test (such as by gift or inheritance) or through a conversion or exchange of QSB stock that the taxpayer held.
5. During substantially all the time that the taxpayer held the stock:
    a. the corporation was a C corporation,
    b. at least 80% of the value of the corporation's assets were used in the active conduct of one or more qualified businesses AND
    c. The corporation was not a foreign corporation, DISC, former DISC, regulated investment company, real estate investment trust, REMIC, FASIT, cooperative, or a corporation that has made (or that has a subsidiary that has made) a §936 election.

Qualified Business Defined
A qualified business is any business other than a:
1. Business involving services performed in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, or brokerage services.
2. Business whose principal asset is the reputation or skill of one or more employees.
3. Banking, insurance, financing, leasing, investing, or similar business.
4. Farming business (including the raising or harvesting of trees).
5. Business involving the production of products for which percentage depletion can be claimed. OR
6. Business of operating a hotel, motel, restaurant, or similar business.

Long-Term Capital Gain
The portion of the gain includible in taxable income is taxed at a maximum rate of 28% under the regular tax.

AMT Rate & Preference Item
7% of the excluded gain is an alternative minimum tax (AMT) preference item. The portion of the gain includible in alternative minimum taxable income is taxed at a maximum rate of 28% under the alternative minimum tax.

75% Exclusion on §1202 Gains (Stock Issued > 02-17-09 & < 09-28-10)
The percentage exclusion for qualified small business stock acquired after February 17, 2009, and on or before September 27, 2010, was increased to 75%. As a result of the increased exclusion, gain from the sale of qualified small business stock to which the provision applies is taxed at effective rates of 7% percent under the regular tax and 12.88% under the alternative minimum tax.

100% Gain Exclusion for Regular Tax & AMT (Stock Issued > 09-27-10 and < 07-05-25)
For qualified small business stock acquired after September 27, 2010 the percentage exclusion is increased to 100% and the minimum tax preference does not apply.

NOTE – Thus, no regular tax or AMT is imposed on the sale of §1202 stock held at least five years and acquired after September 27, 2010.

Tiered Gain Exclusion for Regular Tax & AMT (Stock Issued > 07-04-25)
For QSBS acquired after July 4, 2025, the exclusion is tiered based on holding period:
- **50% exclusion** for stock held at least 3 years
- **75% exclusion** for stock held at least 4 years
- **100% exclusion** for stock held at least 5 years

NOTE – The aggregate lifetime gain exclusion per issuer is increased from $10 million to $15 million for QSBS acquired after July 4, 2025. The $15 million cap is indexed for inflation starting in 2026. The existing alternative limit of 10× the taxpayer's basis in the QSBS remains available. If the $15 million cap is exceeded in any single year, the exclusion for that issuer becomes zero in all future years.

25% LTCG Rate – Unrecaptured §1250 Gain

25% LTCG Calculation

The term "unrecaptured section 1250 gain" means the excess (if any) of:

1. the amount of long-term capital gain (not otherwise treated as ordinary income) which would be treated as ordinary income if §1250 included all depreciation as ordinary income (i.e., it is the amount of depreciation taken not taxed as ordinary income under §1250)
   OVER
2. the excess (if any) of:
   a. the sum of:
      i. collectibles loss;
      ii. the net short-term capital loss; and
      iii. the amount of long-term capital loss carried forward to the taxable year
      OVER
   d. sum of:
      i. collectibles gain AND
      ii. §1202 gain (i.e., qualified small business stock)

25% Group Defined

The 25% group consists of unrecaptured §1250 gain (there are no losses in this group). Unrecaptured §1250 gain is long-term capital gain, not otherwise recaptured as ordinary income, attributable to prior depreciation of real property and which is from property held for more than one year.

EXAMPLE – Bill sells a building held greater than one year for $260,000. He purchased the building for $150,000 and had taken $50,000 in straight-line depreciation. Thus, Bill has a $160,000 long-term capital gain (LTCG) of which none is reclassified as ordinary income under §1250 because he used straight-line depreciation. The $50,000 unrecaptured §1250 gain will be taxed no higher than 25% and the remaining $110,000 will be taxed no higher than 15%.

20%, 15 or 0% LTCG Rate – All Other LTCGs & Qualified Dividends

All Other Long-Term Capital Gains

The 20%, 15% and 0% LTCG group consists of:

1. long-term capital gains and losses that are not in the 28% or 25% group and
2. qualified dividends.

NOTE – Qualified dividends are treated as part of the net capital gain tax computation. However, they are not eligible to be used to offset capital losses.

The rates will be:

1. 0% tax on adjusted net capital gain that otherwise would be taxed at a regular tax rate below the 25% rate,
2. 15% tax on adjusted net capital gain that otherwise would be taxed at a regular tax rate above 15% and below the 39.6% rate,
3. 20% tax on adjusted net capital gain in excess of the amount taxed under 1. and 2. (i.e., net capital gain that otherwise would be taxed at a regular tax rate of 39.6%).

Qualified Dividends (§1(h)(11))

Qualified dividends received by an individual shareholder from corporations are taxed at the same 20%, 15% or 0% rates that apply to net capital gain. This treatment applies for purposes of both the regular tax and the alternative minimum tax.

NOTE – After 2012, the ATRA of 2010 increased the qualified dividend rate to 20% for taxpayers with taxable incomes exceeding the 35% ordinary income tax bracket (§1(h)(1)).

Eligible Dividends

Stockholders must hold a share of common stock for more than 60 days during the 120-day period beginning 60 days before the ex-dividend date to be eligible for the reduced rates. Stockholders must hold a share of preferred stock for more than 90 days during the180-day period beginning 90 days before the ex-dividend date to be eligible for the reduced rates.

Reduced Rate Dividends Are Not Investment Income

A dividend is treated as investment income for purposes of determining the amount of deductible investment interest only if the taxpayer elects to treat the dividend as not eligible for the reduced rates (i.e., tax as ordinary dividend income at ordinary tax rates).

Qualified Dividends Taxed at Capital Gains Rates

Qualified dividends are the ordinary dividends subject to the same maximum tax rate that applies to net capital gains.

Qualified Dividend Requirements

To qualify for the lower tax rates, all of the following requirements must be met:

1. the dividends must have been paid by a U.S. corporation or a qualified foreign corporation,
2. the dividends are not of the type listed later under Dividends that are not qualified dividends and
3. the taxpayer meets the holding period.

Holding Period

The taxpayer must have held the stock for more than 60 days during the 121-day period that begins 60 days before the ex-dividend date.

Kiddie Tax

Kiddie Tax Background

Under these rules, the net unearned income of a child over the annual limit is taxed at the parents' tax rates if the parents' tax rates are higher than the tax rates of the child. The remainder of a child's taxable income (i.e., earned income, plus unearned income up to the annual limit, less the child's standard deduction) is taxed at the child's rates, regardless of whether the kiddie tax applies to the child. For these purposes, unearned income is income other than wages, salaries, professional fees, other amounts received as compensation for personal services actually rendered, and distributions from qualified disability trusts. In general, a child is eligible to use the preferential tax rates for qualified dividends and capital gains.

Kiddie Tax Rules (§1(g))

Special rules (generally referred to as the "kiddie tax") apply to the net unearned income of certain children. Generally, the kiddie tax applies to a child if all of the following apply:

1. the child's unearned income exceeds the annual limit adjusted for inflation:

Tax Year	Unearned Income Annual Limit Without Kiddie Tax
2024	$2,600
2025	$2,700
2026	$2,700

2. The child either:
    a. Was under age 18 at the end of the year,
    b. Was age 18 at the end of the year and did not have earned income that was more than half of his or her support, or
    c. Was a full-time student over age 18 and under age 24 at the end of the year and did not have earned income that was more than half of his or her support.
3. At least one of the child's parents was alive at the end of the year, AND
4. the child does not file a joint return during the year.

NOTE – The kiddie tax applies regardless of whether the child may be claimed as a dependent by either or both parents.

Kiddie Tax Calculation

The kiddie tax is calculated by computing the "allocable parental tax." This involves adding the net unearned income of the child to the parent's income and then applying the parent's tax rate. A child's "net unearned income" is the child's unearned income less the sum of:

1. the minimum standard deduction allowed to dependents **($1,350 for 2025)** and
2. the greater of
    a. such minimum standard deduction amount or
    b. the amount of allowable itemized deductions that are directly connected with the production of the unearned income.

NOTE – A child's net unearned income cannot exceed the child's taxable income.

Allocable Parental Tax

The allocable parental tax equals the hypothetical increase in tax to the parent that results from adding the child's net unearned income to the parent's taxable income. If the child has net capital gains or qualified dividends, these items are allocated to the parent's hypothetical taxable income according to the ratio of net unearned income to the child's total unearned income. If a parent has more than one child subject to the kiddie tax, the net unearned income of all children is combined, and a single kiddie tax is calculated. Each child is then allocated a proportionate share of the hypothetical increase, based upon the child's net unearned income relative to the aggregate net unearned income of all of the parent's children subject to the tax.

Reporting

1. **Reporting Tax on Child's Tax Return** – Form 8615 - Tax for Certain Children Who Have Unearned Income
2. **Reporting on Parent's Tax Return** – Form 8814 - Parents' Election To Report Child's Interest and Dividends

Alternative Minimum Tax (AMT) – Modifications (2018-2025)

AMT Exemption

UPDATE - The OBBB makes permanent the higher individual AMT exemption amounts that were put in place by the TCJA.

A taxpayer's alternative minimum taxable income (AMTI), as reduced by the taxpayer's exemption amount (which phases out for AMTI above certain threshold levels) is used to compute the alternative minimum tax (AMT) for individuals. The exemptions are:

AMT Exemption	2026	2025	2024
Married Filing Joint & Qualifying Surviving Spouse	$140,200	$137,000	$133,300
Single or Head of Household	$90,100	$88,100	$85,700
Married Filing Separate	$70,100	$68,500	$66,650
Estates & Non-Grantor Trusts	$31,400	$30,700	$29,900
Child subject to kiddie tax (this amount + earned income)	$9,750	$9,550	$9,250

AMT Exemption Phase-Out

The AMT Exemption is phased out at 25% per dollar of AMTI above the following threshold amounts:

Beginning of Exemption Phase-out	2026	2025	2024
Married Filing Joint & Qualifying Surviving Spouse	$1,000,000	$1,252,700	$1,218,700
Single or Head of Household	$500,000	$626,350	$609,350
Married Filing Separate	$500,000	$626,350	$609,350
Estates & Non-Grantor Trusts	$104,800	$102,450	$99,700

UPDATE - The OBBB resets the AMT exemption phase-out thresholds (the income levels at which the exemption starts to phase out) to $500,000 for single filers and $1,000,000 for joint filers, effective for tax years beginning after 2025, with annual inflation indexing beginning in 2026. The OBBB also increases the phase-out rate for higher-income taxpayers from 25% to 50%.

Tentative Minimum Tax & AMT Tax Rates

The law imposes an alternative minimum tax (AMT) on an individual taxpayer to the extent the taxpayer's tentative minimum tax (TMT) liability exceeds his or her regular income tax liability. If the regular income-tax amount is greater than the TMT, no special action is required. If the TMT is greater than the tax calculated using the regular rules, the difference between the TMT and the regular tax is added to the regular tax amount, so the taxpayer pays the full amount of the TMT, although some of that tax is considered regular tax and some is considered AMT.

Tentative minimum tax (TMT) calculation

An individual's tentative minimum tax is the sum of:

1. 26% of so much of the taxable excess as does not exceed:

Tax Year	2026	2025	2024
MFJ, Qualifying Surviving Spouse, Single & HOH	$244,500	$239,100	$232,600
Married Filing Separate	$122,250	$119,550	$116,300

AND

2. 28% of the remaining taxable excess.

NOTE – The taxable excess is the amount by which the alternative minimum taxable income (AMTI) exceeds an exemption amount.

Personal Tax Credits Offsetting AMT (§26(a))

The ATRA of 2012 permanently allows nonrefundable personal credits (not just specified personal credits) to reduce the AMT in addition to the regular tax (as was the law in 2000 through 2011). Thus, the aggregate amount of nonrefundable personal credits allowed cannot exceed the sum of:

1. the taxpayer's regular tax liability (reduced by the foreign tax credit) for the tax year,
   plus
2. AMT liability for the tax year under §55(a).

EXAMPLE – Dan has a regular tax of $15,000 and tentative minimum tax of $16,000. Thus, Dan is liable for $15,000 of regular tax and $1,000 of AMT. Dan can claim up to $16,000 (i.e., regular tax plus AMT) as nonrefundable personal credits.

AMT Credit (§53)

The portion of the tax that is considered AMT (i.e., the AMT in excess of the regular tax liability) may be available in later years as a "Minimum Tax Credit", reducing the regular income tax due in later years, but not below the taxpayer's TMT level in those later years.

NOTE – A minimum tax credit is allowed as a credit against the current year regular tax liability for the portion of prior year's minimum tax attributed to deferral adjustments only (NOT tax preference items).

Allowable AMT Credit (Form 8801)

The individual AMT attributable to deferral adjustments generates a minimum tax credit that is allowable to the extent the regular tax (reduced by other nonrefundable credits) exceeds the tentative minimum tax in a future taxable year. Unused minimum tax credits are carried forward indefinitely.

Self-Employment Tax (Schedule SE)

Net Earnings from Self-Employment (§1402(a))
The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such individual, **less** the deductions allowed which are attributable to such trade or business, **plus** his distributive share (whether or not distributed) of income or loss from any trade or business carried on by a partnership of which he is a member.

Exception (§1402(a))
Self-employment income excludes the following partnership items:
1. Net income (loss) from rental real estate,
2. Portfolio interest,
3. Dividend income,
4. Capital gains (losses),
5. Gains (losses) from the sale of trade or business property (other than inventory), and
6. Distributive share of any item of income or loss of a limited partner, other than guaranteed payments to that partner for services rendered.

Social Security (OASDI) Tax Rate – 12.4%
Payroll taxes were first collected and benefits under social security were first paid in 1937. The social security (OASDI) tax rate is currently 12.4%. For employees, 6.2% is withheld from the worker and a 6.2% is paid by the employer (i.e., match) of the wages, salaries and other compensation in connection with employment. In the case of self-employed individuals, the tax is 12.4% of net earnings from self-employment, and the entire amount is paid by the self-employed individual. The maximum amount of wages, self-employment income, etc., on which the OASDI tax can be imposed is:

Year	Wages/SE Income
2024	$168,600
2025	$176,100
2026	$184,500

Medicare (HI) Tax Rate – 2.9%
The Medicare (HI) tax rate is currently 2.9%. For employees, 1.45% is withheld from the worker and a 1.45% is paid by the employer (i.e., match) of the wages, salaries and other compensation in connection with employment. In the case of self-employed individuals, the tax is 2.9% of net earnings from self-employment, and the self-employed individual pays the entire amount.

NOTE – After 1992, all of a taxpayer's earned income is subject to the 2.9% Medicare tax.

When Short-Term Rentals are Included in SE Income (CCA 202151005)
This CCA states that whether an activity is a "rental activity" under §469(c)(2) is not determinative of whether the exclusion in §1402(a)(1) applies. Also, in situations not involving a real estate dealer, net rental income from the rental of living quarters is considered "rentals from real estate" excluded from net earnings from self-employment (NESE) when no services are rendered for the occupants. However, if services are rendered for the occupants and the services rendered (1) are not clearly required to maintain the space in a condition for occupancy, and (2) are of such a substantial nature that the compensation for these services can be said to constitute a material portion of the rent, then the net rental income received is not excluded under §1402(a)(1) and is included in NESE.

Additional 0.9% H.I. Tax on Employee Portion High-Income Taxpayers

Calculation of Additional Tax HI (§3101(b)(2))

PPACA of 2010 imposes an additional health insurance (HI) tax on the employee's portion for high-income taxpayers after 2012.

NOTE – Use the ***Form 8959*** **–** ***Additional Medicare Tax*** to report any additional amounts owed.

The employee portion of the HI (Medicare) tax is increased by an additional tax of 0.9% on wages received in excess of the following threshold amounts:

Filing Status	**Threshold Amount**
Married filing jointly	$250,000
Married filing separately	$125,000
Single	$200,000
Head of household (with qualifying person)	$200,000
Qualifying widow(er) with dependent child	$200,000

NOTE 1 – Unlike the general 1.45% HI tax on wages, this additional tax is on the combined wages of the employee and the employee's spouse, in the case of a joint return.

NOTE 2 – For taxpayers with wages in excess of the threshold amount, the overall HI rate will be 3.8% (i.e., 2.35% for the employee and 1.45% for the employer).

Employer's obligation to withhold on wages in excess of $200,000 (§3102(f))

The employer is required to withhold the additional 0.9% HI tax on wages. To the extent the additional tax is not collected by the employer, the employee shall pay such tax.

NOTE – The employer could still be subject to penalties for failure to deduct and withhold the additional tax.

In determining the employer's requirement to withhold and liability for the tax, only wages that the employee receives from the employer in excess of $200,000 for a year are taken into account and the employer must disregard the amount of wages received by the employee's spouse. Thus, the employer is only required to withhold on wages in excess of $200,000 for the year, even though the tax may apply to a portion of the employee's wages at or below $200,000, if the employee's spouse also has wages for the year, they are filing a joint return, and their total combined wages for the year exceed $250,000.

EXAMPLE – If a taxpayer's spouse has wages in excess of $250,000 and the taxpayer has wages of $100,000, the employer of the taxpayer is not required to withhold any portion of the additional tax, even though the combined wages of the taxpayer and the taxpayer's spouse are over the $250,000 threshold. In this instance, the employer of the taxpayer's spouse is obligated to withhold the additional 0.9% HI tax with respect to the $50,000 above the threshold with respect to the wages of $250,000 for the taxpayer's spouse.

Employee's liability for the additional tax

In contrast to the employee portion of the general HI tax of 1.45% of wages for which the employee generally has no direct liability to the IRS to pay the tax, the employee is also liable for this additional 0.9% HI tax to the extent the tax is not withheld by the employer.

NOTE – The amount of this tax not withheld by an employer must also be taken into account in determining a taxpayer's liability for estimated tax.

Additional HI for Self-Employed Individuals (§1402(b))

This same additional HI tax applies to the HI portion of SECA tax on self-employment income in excess of the threshold amount. Thus, an additional tax of 0.9% is imposed on every self-employed individual on self-employment income in excess of the following threshold amounts:

Filing Status	Threshold Amount
Married filing jointly	$250,000
Married filing separately	$125,000
Single	$200,000
Head of household (with qualifying person)	$200,000
Qualifying widow(er) with dependent child	$200,000

NOTE – The threshold amount is reduced (but not below zero) by the amount of wages taken into account in determining the FICA tax with respect to the taxpayer.

Adjustment to AGI for 1/2 of SE Taxes will not apply to the 0.9% (§164(f))

The 1/2 of SECA tax deduction under §164(f) will not apply to the 0.9%.

SECA tax deduction for computing net earnings from SE will not apply to the 0.9% (§1402(a)(12))

The deduction for 1/2 if the SECA tax for computing net earnings from self employment under §1402(a)(12) will also be determined without regard to the additional SECA tax rate.

3-Step Process to Calculate (IRS FAQ-19)

Individuals with wages subject to FICA tax and self-employment income subject to SECA tax calculate their liabilities for Additional Medicare Tax in three steps:

- **Step 1 –** Calculate Additional Medicare Tax on any wages in excess of the applicable threshold for the filing status, without regard to whether any tax was withheld.
- **Step 2 –** Reduce the applicable threshold for the filing status by the total amount of Medicare wages received - but not below zero.
- **Step 3 –** Calculate Additional Medicare Tax on any self-employment income in excess of the reduced threshold.

Additional Resources

Questions & Answers for the Additional Medicare Tax

The IRS Q&As for the Additional Medicare Tax can be found online at: http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Questions-and-Answers-for-the-Additional-Medicare-Tax.

Final Regulations Issued November 26, 2013 (TD 9645)

The IRS final regulations relating to the additional Medicare tax can be found online at: https://s3.amazonaws.com/public-inspection.federalregister.gov/2013-28411.pdf

Net Investment Income Tax (§1411)

3.8% Unearned Income Medicare Contribution Tax

The PPACA of 2010 added **IRC §1411** that imposes an unearned income Medicare contribution tax on individuals, estates, and trusts. The tax is generally levied on income from interest, dividends, annuities, royalties, rents, and capital gains.

EFFECTIVE DATE – The PPACA of 2010 provision applies to taxable years beginning after December 31, 2012.

Individual tax

In the case of an individual, the tax is the 3.8% of the lesser of:

1. net investment income

   OR
2. the excess of modified adjusted gross income (MAGI) over the following threshold amounts:
   a. $250,000 in the case of a joint return or surviving spouse,
   b. $125,000 in the case of a married individual filing a separate return, and
   c. $200,000 in any other case.

NOTE – MAGI is adjusted gross income increased by the amount excluded from income as foreign earned income under §911(a)(1) (net of the deductions and exclusions disallowed with respect to the foreign earned income).

Estate or trust tax

In the case of an estate or trust, the tax is 3.8% of the lesser of:

1. undistributed net investment income or
2. the excess of adjusted gross income (as defined in §67(e)) over the dollar amount at which the highest income tax bracket applicable to an estate or trust begins.

Exceptions to the tax

The tax does not apply to a:

1. non-resident alien,
2. to a trust all the unexpired interests in which are devoted to charitable purposes,
3. trust that is exempt from tax under §501 or
4. charitable remainder trust exempt from tax under §664.

Estimated tax payments required

The tax is subject to the individual estimated tax provisions. The tax is not deductible in computing any tax imposed by subtitle A of the Internal Revenue Code (relating to income taxes).

Tax Reporting

Individuals, estates and trusts must use the *Form 8960 – Net Investment Income Tax (Individuals, Estates, and Trusts)* to calculate the net investment income tax under IRC §1411.

Net Investment Income

Net investment income is investment income reduced by the deductions properly allocable to such income. Investment income is the sum of:

1. gross income from interest, dividends, annuities, royalties, and rents (other than income derived from any trade or business to which the tax does not apply),
2. other gross income derived from any business to which the tax applies, and
3. net gain (to the extent taken into account in computing taxable income) attributable to the disposition of property other than property held in a trade or business to which the tax does not apply.

NOTE – Gross income does not include items, such as interest on tax-exempt bonds, veterans' benefits, and excluded gain from the sale of a principal residence, which are excluded from gross income under the income tax.

Trades or businesses to which tax applies

In the case of a trade or business, the tax applies if the trade or business is:

1. a passive activity with respect to the taxpayer or
2. the trade or business consists of trading financial instruments or commodities (as defined in §475(e)(2)).

NOTE – The term trade or business refers to a trade or business within the meaning of §162.

Income on investment of working capital subject to tax

Income, gain, or loss on working capital is not treated as derived from a trade or business.

Exception for certain active interests in partnerships and S corporations.

In the case of the disposition of a partnership interest or stock in an S corporation, gain or loss is taken into account only to the extent gain or loss would be taken into account by the partner or shareholder if the entity had sold all its properties for fair market value immediately before the disposition.

NOTE – Only net gain or loss attributable to property held by the entity which is not property attributable to an active trade or business is taken into account.

Qualified plan distributions are not investment income

Investment income does not include distributions from a qualified retirement plan or amounts subject to SECA tax. Qualified distributions include:

1. qualified pension, profit-sharing, and stock bonus plans (§401(a));
2. qualified annuity plans (§Sec. 403(a))
3. annuities for employees of tax-exempt organizations or public schools (§403(b))
4. (individual retirement accounts—IRAs) (§408)
5. Roth IRAs (§408A)
6. deferred compensation plans of state and local governments and tax-exempt organizations (§457(b)).

Calculation of Net Investment Income in Special Situations (§1.1411-4(g))

NOTE – Below are selected sections from the Final Regulations under §1.1411-4(g).

Treatment of self-charged interest income (§1.1411-4(g)(5))

Gross income from interest that is received by the taxpayer from a nonpassive activity of such taxpayer, solely for purposes of §1411, is treated as derived in the ordinary course of a trade or business not described in §1.1411-5. The amount of interest income that is treated as derived in the ordinary course of a trade or business not described in §1.1411-5, and thus excluded from the calculation of net investment income, is limited to the amount that would have been considered passive activity gross income under the rules of §1.469-7 if the payor was a passive activity of the taxpayer. For purposes of this rule, the term nonpassive activity does not include a trade or business of trading in financial instruments or commodities (described in §1.1411-5(a)(2)). However, this rule does not apply to the extent the corresponding deduction is taken into account in determining self-employment income that is subject to tax under §1401(b).

Treatment of certain nonpassive rental activities (§1.1411-4(g)(6))

Gross rental income is "deemed" to be derived in the ordinary course of a trade or business within the meaning of §1.1411-4(b) to the extent that gross rental income is treated as not derived from a passive activity by reason of:

1. §1.469-2(f)(6) (which generally recharacterizes what otherwise would be passive rental income from a taxpayer's property as nonpassive when the taxpayer rents the property for use in an activity in which the taxpayer materially participates) or
2. as a consequence of a taxpayer grouping a rental activity with a trade or business activity under §1.469-4(d)(1) and the grouped activity is a nonpassive activity

NOTE – In both of these instances, the final regulations provide that any gain or loss from the assets associated with that rental activity that are treated as nonpassive gain or loss will also be treated as gain or loss attributable to the disposition of property held in a nonpassive trade or business.

Treatment of certain real estate professionals – Safe Harbor (§1.1411-4(g)(7))

In the case of a real estate professional (as defined in §469(c)(7)(B)) that participates in a rental real estate activity for more than 500 hours during such year, OR has participated in such real estate activities for more than 500 hours in any five taxable years (whether or not consecutive) during the ten taxable years that immediately precede the taxable year, then:

1. Such gross rental income from that rental activity is "deemed" to be derived in the ordinary course of a trade or business within the meaning of §1.1411-4(b);

   and

2. Gain or loss resulting from the disposition of property used in such rental real estate activity is "deemed" to be derived from property used in the ordinary course of a trade or business within the meaning of §1.1411-4(d)(4)(i).

NOTE – The inability of a real estate professional to satisfy the safe harbor does not preclude such taxpayer from establishing that such gross rental income and gain or loss from the disposition of property, as applicable, is not included in net investment income under any other provision of §1411.

Participation defined
For purposes of establishing participation under this §1.1411-4(g)(7), any participation in the activity that would count towards establishing material participation under §469 shall be considered.

Rental real estate activity defined
The term rental real estate activity used in §1.1411-4(g)(7) is a rental activity within the meaning of §1.469-1T(e)(3). An election to treat all rental real estate as a single rental activity under §1.469-9(g) also applies for purposes of this section §1.1411-4(g)(7). However, any rental real estate that the taxpayer grouped with a trade or business activity under §1.469-4(d)(1)(i)(A) or (d)(1)(i)(C) is not a rental real estate activity.

Treatment of former passive activities (§1.1411-4(g)(8))

Background
In cases where a taxpayer materially participates in an activity that was formerly a passive activity, the deductions produced by the activity in the current year are not subject to §469. However, the carryover (or ''suspended'') passive losses incurred in prior years when the activity was a passive activity remain disallowed passive losses subject to carryover. §469(f)(1)(A) allows the suspended passive losses when the former passive activity produces current-year net income (even though that income is technically from a nonpassive activity). To the extent the taxpayer has passive losses allocable to a former passive activity in excess of the current year nonpassive income from that activity (the §469(f)(1)(A) amount), §469(f)(1)(C) allows excess passive losses to offset net passive income from other passive activities of the taxpayer. Any suspended passive losses not allowed by §469(f)(1)(A) or (C) remain suspended and are carried over to the following year.

§469(f)(1)(A) losses
Losses allowed in computing taxable income by reason of the rules governing former passive activities in §469(f)(1)(A) are taken into account in computing net gain under §1.1411-4(d) or as properly allocable deductions under §1.1411-4(f), as applicable, in the same manner as such losses are taken into account in computing taxable income.

NOTE – This applies only to the extent the net income or net gain from the former passive activity (as defined in §469(f)(3)) is included in net investment income.

§469(f)(1)(C) losses
Losses allowed in computing taxable income by reason of §469(f)(1)(C) are taken into account in computing net gain under §1.1411-4(d) or as properly allocable deductions under §1.1411-4(f), as applicable, in the same manner as such losses are taken into account in computing taxable income (as defined in §63).

Household Employment Taxes (Schedule H)

NOTE - For more information, refer to Publication 926.

Background

A worker is your employee if you can control not only what work is done, but how it is done. If the worker is your employee, it doesn't matter whether the work is full time or part time or that you hired the worker through an agency or from a list provided by an agency or association. It also doesn't matter whether you pay the worker on an hourly, daily, or weekly basis, or by the job. Household work is work done in or around your home. Examples of workers who do household work are:

- Babysitters,
- Caretakers,
- House cleaning workers,
- Domestic workers,
- Drivers,
- Health aides,
- Housekeepers,
- Maids,
- Nannies,
- Private nurses, and
- Yard workers.

NOTE – Repairmen, plumbers, contractors, and other business people who work for the taxpayer as independent contractors, are not employees.

Social Security & Medicare Wages

The taxpayer generally must withhold social security and Medicare taxes from all cash wages that the taxpayer pays to a household employee if during the year the wages are:

Year	Wages
2024	$2,700 or more
2025	$2,800 or more
2026	$2,900 or more

Unless the taxpayer prefers to pay the employee's share of social security and Medicare taxes from the taxpayer's own funds, the taxpayer should withhold 7.65% (6.2% for social security tax and 1.45% for Medicare tax) from each payment of cash wages. Instead of paying this amount to the employee, the taxpayer pays it to the IRS with a matching amount for the taxpayer's share of the taxes as a household employer.

NOTE – This gets reported on a Like - *Schedule H (Form 1040), Household Employment Taxes*.

Household Employee Taxes NOT Required

The taxpayer should not withhold or pay these taxes from wages that they pay to:

- The taxpayer's **spouse,**
- The taxpayer's **child** who is **under age 21,**
- The **taxpayer's parent**, unless an exception is met,
- An **employee who is under age 18** at any time during the year unless performing household work is the employee's principal occupation. If the employee is a student, providing household work is not considered to be his or her principal occupation.

Parent Exception

A parent's wages are not exempt from social security and Medicare taxes if both the following conditions apply:

1. Your parent cares for your child who is either of the following.
    a. Under the age of 18, or
    b. Has a physical or mental condition that requires the personal care of an adult for at least 4 continuous weeks in the calendar quarter services were performed.
2. Your marital status is one of the following.
    a. You are divorced and haven't remarried,
    b. You are a widow or widower, or
    c. You are living with a spouse whose physical or mental condition prevents him or her from caring for your child for at least 4 continuous weeks in the calendar quarter services were performed.

Federal Income Tax Withholding Requirements

The taxpayer is NOT required to withhold Federal income tax from wages that the taxpayer pays to a household employee unless the household employee makes a request to have taxes withheld. If the taxpayer withholds or pays social security and Medicare taxes, or withholds Federal income tax, the taxpayer will need to file Form W-2 after the end of the year.

FUTA Wages

If the taxpayer paid cash wages to household employees totaling $1,000 or more in any calendar quarter of the year, the taxpayer generally must pay Federal unemployment tax on the first $7,000 of cash wages that the taxpayer pays to each of their household employees during the year. The taxpayer can avoid owing tax with their return if they pay enough Federal income tax before the file their tax return to cover both the employment taxes for the household employee and the taxpayer's income tax. The taxpayer may have to pay an estimated tax penalty if they do not prepay their household employment taxes during the year. Do not count as FUTA wages amounts you pay to:

1. Your spouse,
2. Your child who is under the age of 21, or
3. Your parent.

State employment taxes

You may also have to pay state unemployment tax. Contact your state unemployment tax office for information. You should also find out whether you need to pay or collect other state employment taxes or carry workers' compensation insurance.

NOTE – For a list of state unemployment tax agencies, visit the U.S. Department of Labor's website at https://oui.doleta.gov/unemploy/agencies.asp.

Installment Payment of Tax on Gain from Sale of Qualified Farmland to Qualified Farmers (§1062)

Election to pay tax in installments
IRC §1062 allows individual taxpayers to elect to pay the tax on gain from the sale of qualified farmland property to a qualified farmer in four equal annual installments, easing the tax burden and promoting farmland transfers to active farmers. Effective for sales after July 4, 2025.

Eligibility Criteria
To qualify, the following must apply:

1. **The property sold must be qualified farmland property**, meaning:
    a. It is located in the U.S.,
    b. It was used or leased for farming purposes during substantially all of the prior 10 years, and
    c. It is subject to a covenant or legal restriction limiting non-farm use for 10 years after the sale.
2. **The buyer must be a qualified farmer**, defined as someone actively engaged in farming, using the criteria under §1001(b)-(c) of the Food Security Act of 1985 (7 U.S.C. 1308-1(b), (c)).

Installment Election Mechanics

Installment Election
- Taxpayer may elect to pay the applicable net tax liability in 4 equal annual installments
- The election must be made by the due date (without extension) of the tax return for the year of sale
- Once made, the election is binding unless revoked with IRS consent.
- The election is made on the individual return, even if the sale occurred through a partnership or S corporation
- Taxpayer must include with the return for the year of sale a copy of the legal covenant or restriction placed on the farmland, demonstrating the 10-year farm-use restriction.

Applicable Net Tax Liability Defined
The amount of tax attributable to the gain from the farmland sale:

Net income tax **with** gain
– Net income tax **without** gain
= Applicable net tax liability

Installment Payment Timing
- **1st installment -** Due with the return for the year of sale
- **2nd–4th installments -** Due with the returns for the next 3 successive years

Acceleration of Payment Triggers
- **Missed payment** - All unpaid installments become immediately due.
- **Death of individual taxpayer -** Remaining installments are due with the return for the year of death.

Exclusions and Recapture Triggers
- If the use restriction covenant is not attached, the election is invalid.
- The IRS may revoke installment privileges for fraud, negligence, or rule violations.

Individual Credits

Child & Dependent Care Expenses Credit (§21)

Dependent Care Expense Limit

There is a dollar limit on the amount of the work-related expenses that the taxpayer can use to figure the credit. This limit is **$3,000** for one qualifying person and **$6,000** for two or more qualifying persons.

NOTE – If the taxpayer paid work-related expenses for the care of two or more qualifying persons, the $6,000 limit does not need to be divided equally among them.

EXAMPLE – If the taxpayer's work-related expenses for the care of one qualifying person are $3,200 and the work-related expenses for another qualifying person are $2,800, the taxpayer can use the total of $6,000 when figuring the credit.

Yearly Limit

The dollar limit is a yearly limit. The amount of the dollar limit remains the same no matter how long, during the year, the taxpayer has a qualifying person in their household.

- Use the $3,000 limit if the taxpayer paid work-related expenses for the care of one qualifying person at any time during the year.
- Use $6,000 if the taxpayer paid work-related expenses for the care of more than one qualifying person at any time during the year.

Reduced Dollar Limit

If the taxpayer received dependent care benefits from their employer that were excluded from income, the taxpayer must subtract that amount from the dollar limit that applies to them.

EXAMPLE – George is a widower with one child and earns $24,000 a year. He pays work-related expenses of $2,900 for the care of his 4-year-old child and qualifies to claim the credit for child and dependent care expenses. His employer pays an additional $1,000 under a dependent care benefit plan. This $1,000 is excluded from George's income. Although the dollar limit for his work-related expenses is $3,000 (one qualifying person), George figures his credit on only $2,000 of the $2,900 work-related expenses he paid. This is because his dollar limit is reduced as shown next.

George's Reduced Dollar Limit

1. Maximum allowable expenses for one qualifying person	$3,000
2. Minus: Dependent care benefits George excludes from income	(1,000)
3. Reduced dollar limit on expenses George can use for the credit	$2,000

Amount of Credit (Pre-2026)

To determine the amount of the taxpayer's credit, multiply their work-related expenses (after applying the earned income and dollar limits) by a percentage. This percentage depends on the taxpayer's adjusted gross income.

Dependent Care Credit Percentage – Pre 2026		
IF adjusted gross income is:		**THEN the percentage is:**
Over	**But not over**	
$ 0	$15,000	35%
15,000	17,000	34%
17,000	19,000	33%
19,000	21,000	32%
21,000	23,000	31%
23,000	25,000	30%
25,000	27,000	29%
27,000	29,000	28%
29,000	31,000	27%
31,000	33,000	26%
33,000	35,000	25%
35,000	37,000	24%
37,000	39,000	23%
39,000	41,000	22%
41,000	43,000	21%
43,000	No limit	20%

UPDATE – Credit Enhanced After 2025

After 2025, the OBBB increases the maximum credit rate to 50%, reduced by one percentage point, but not below 35%, for each $2,000 or fraction thereof by which the taxpayer's AGI exceeds $15,000. For AGIs between $43,001 and $75,000 ($86,001 and $150,000, respectively, in the case of a joint return), the credit rate is 35%. This credit rate is further phased down to 20% for AGI between $75,001 and $105,000 ($150,001 and $210,000, respectively, in the case of a joint return).

Dependent Care Credit Percentage – Post 2025		
All taxpayers other than MFJ	**Married filing joint (MFJ) taxpayers**	**Dependent care credit percentage**
0 - 15,000	0 - 15,000	50%
15,001 - 17,000	15,001 - 17,000	49%
17,001 - 19,000	17,001 - 19,000	48%
19,001 - 21,000	19,001 - 21,000	47%
21,001 - 23,000	21,001 - 23,000	46%
23,001 - 25,000	23,001 - 25,000	45%
25,001 - 27,000	25,001 - 27,000	44%
27,001 - 29,000	27,001 - 29,000	43%
29,001 - 31,000	29,001 - 31,000	42%
31,001 - 33,000	31,001 - 33,000	41%
33,001 - 35,000	33,001 - 35,000	40%
35,001 - 37,000	35,001 - 37,000	39%
37,001 - 39,000	37,001 - 39,000	38%
39,001 - 41,000	39,001 - 41,000	37%
41,001 - 43,000	41,001 - 43,000	36%
43,001 - 75,000	43,001 - 150,000	35%
75,001 - 77,000	150,001 - 154,000	34%
77,001 - 79,000	154,001 - 158,000	33%
79,001 - 81,000	158,001 - 162,000	32%
81,000 - 83,000	162,001 - 166,000	31%
83,000 - 85,000	166,001 - 170,000	30%
85,000 - 87,000	170,001 - 174,000	29%
87,000 - 89,000	174,001 - 178,000	28%
89,000 - 91,000	178,001 - 182,000	27%
91,000 - 93,000	182,001 - 186,000	26%
93,000 - 95,000	186,001 - 190,000	25%
95,000 - 97,000	190,001 - 194,000	24%
97,000 - 99,000	194,001 - 198,000	23%
99,000 - 101,000	198,001 - 202,000	22%
101,000 - 103,000	202,001 - 206,000	21%
> $103,000 - No limit	> $206,000 - No limit	20%

American Opportunity vs. Lifetime Learning Credit Chart

Features	American Opportunity Credit	Lifetime Learning Credit
Maximum credit	**Up to $2,500 credit per eligible student** (i.e., 100% of first $2,000 and 25% of second $2,000 qualified expenses)	**Up to $2,000 credit per return** (i.e., 20% of first $10,000 in qualified expenses
Type of credit	Refundable up to 40% of credit unless child claiming credit is subject to the kiddie tax	Non-refundable
MAGI phase-out limits	Single - $80,000 to $90,000 MFJ - $160,000 to $180,000	Single - $80,000 to $90,000 MFJ - $160,000 to $180,000
Number of years of post-secondary education	Available for the first 4 years of postsecondary education (i.e., undergraduate school only)	Available for all years of postsecondary education (i.e., undergraduate & graduate school) and for courses to acquire or improve job skills
Number of tax years credit available	Available only for 4 tax years per eligible student (including any year(s) the Hope scholarship credit was claimed)	Available for an unlimited number of tax years
Type of program required	Student must be pursuing a program leading to a degree or other recognized education credential	Student does not need to be pursuing a program leading to a degree or other recognized education credential
Number of courses	Student must be enrolled at least half-time for at least one academic period during the current tax year (or the first 3 months of year after if the qualified expenses were paid in current tax year)	Available for one or more courses
Felony drug conviction	The student had not been convicted of a felony for possessing or distributing a controlled substance during the tax year	Felony drug convictions do not make the student ineligible
Qualifying expenses	Tuition, required enrollment fees, and course materials that the student needs for a course of study whether or not the materials are bought at the educational institution as a condition of enrollment or attendance	Tuition and required enrollment fees (including amounts required to be paid to the institution for course-related books, supplies, and equipment)
Payments for academic periods	Payments during the calendar year for academic periods beginning in the calendar year or beginning in the first 3 months of the year after	
TIN needed by filing due date	A taxpayer must include on the taxpayer's tax return their (or their spouse's) social security number (SSN) or, for an individual other than the taxpayer or the taxpayer's spouse, that individual's name and SSN.	
Educational institution's EIN	A taxpayer (TP) must include on their tax return for that year, the EIN of any institution to which the taxpayer paid qualified tuition and related expenses taken into account in computing the credit.	N/A
Tax reporting	Form 1040 - Schedule 3 and Form 8863 - Education Credits	Form 1040 - Schedule 3 and Form 8863 - Education Credits
Due diligence	Paid preparers need to file (*Form 8867 – Paid Preparer's Due Diligence Checklist*)	N/A

Child Tax Credit (CTC) & Other Dependents Credit (ODC) (§24)

NOTE 1– Use the *Form 8812 – Credits for Qualifying Children and Other Dependents* to claim both the child tax credits for qualifying children(CTC) and other dependents (ODC).

NOTE 2 – The due diligence requirements (*Form 8867 – Paid Preparer's Due Diligence Checklist*) for paid preparers will apply in determining the eligibility for a taxpayer to claim the CTC, ACTC and ODC. A penalty of $500 (adjusted for inflation) is imposed for each failure to meet these requirements.

UPDATE – The OBBB makes all the TCJA changes to the CTC permanent and for tax years after 2025, the OBBB adds: 1) an increase in the nonrefundable CTC to $2,200 per qualifying child, indexed for inflation using chained CPI with 2024 as the base year and 2) a requirement that the return include the taxpayer's SSN (or one spouse's SSN for joint filers) and the qualifying child's SSN to claim the credit.

Child Tax Credit (CTC)

The Child Tax Credit (CTC) is a nonrefundable credit of up to **$2,000 per qualifying child** under IRC §24. If the taxpayer cannot utilize the full CTC due to insufficient tax liability, they may be eligible for the refundable portion (i.e., the Additional Child Tax Credit (ACTC)), subject to earned income thresholds.

UPDATE - For tax years beginning **after 2025**, the maximum nonrefundable portion of the CTC is increased to **$2,200 per qualifying child and indexed for inflation** using chained CPI with 2024 as the base year, as provided under Act Sec. 70104 of the OBBB.

Additional Child Tax Credit (ACTC)

To the extent the child credit exceeds the taxpayer's tax liability, the taxpayer is eligible for a refundable credit (the additional child tax credit) equal to the greater of:

1. **Earned income formula** - 15% of earned income in excess of $2,500 or
2. **Alternative formula** for families with three or more children – that is the excess of the taxpayer's social security taxes over the taxpayer's earned income credit ("EIC") allowed under IRC §32.

Maximum refundable

The maximum amount refundable may not exceed the following amount per qualifying child:

Year	Maximum Refundable
2024	$1,700
2025	$1,700
2026	$1,700

Earned Income Defined

Earned income is defined as the sum of wages, salaries, tips, and other taxable employee compensation plus net self-employment earnings. Unlike the EIC, which also includes the preceding items in its definition of earned income, the additional child tax credit is based only on earned income to the extent it is included in computing taxable income. For example, some ministers' parsonage allowances are considered self-employment income, and thus are considered earned income for purposes of computing the EIC, but the allowances are excluded from gross income for individual income tax purposes, and thus are not considered earned income for purposes of the additional child tax credit since the income is not included in taxable income.

Exception for taxpayers excluding foreign earned income (§24(d)(3))

The refundable child tax credit shall not apply to any taxpayer for any taxable year if such taxpayer elects to exclude any amount from gross income under §911 (i.e., foreign earned income exclusion) for such taxable year.

Other Dependents Credit (ODC)

A taxpayer can claim a **$500 nonrefundable** ODC for dependents (under §152) other than a qualifying child eligible for the CTC or ACTC.

NOTE – The $500 ODC will generally apply to dependent children not under age 17.

Phase-Out of Credit

The taxpayer must reduce the child tax credit if either (1) or (2) applies:

1. The amount of tax is less than the credit. If the amount of tax is zero, the taxpayer cannot take this credit because there is no tax to reduce. However, the taxpayer may be able to take the additional child tax credit.
2. The taxpayer's modified adjusted gross income (AGI) is above the amount shown below for the taxpayer's filing status:
   - Married filing jointly – **$400,000**
   - All other taxpayers – **$200,000**

NOTE - The amount of the credit allowable under 2 shall be reduced (but not below zero) by $50 for each $1,000 (or fraction thereof) by which the taxpayer's modified adjusted gross income exceeds the threshold amount. These phase-out thresholds are not indexed for inflation.

Modified AGI

the term "modified adjusted gross income" means adjusted gross income increased by any amount excluded from gross income under §§911, 931, or 933.

Qualifying Child

The term "qualifying child" means a qualifying child of the taxpayer (as defined in §152(c)) who has not attained age 17. Thus, a qualifying child for purposes of the CTC must be all of the following:

1. under age 17 at the end of the year,
2. a U.S. citizen, U.S. national or U.S. resident,
3. claimed as a dependent on the taxpayer's return,
4. the taxpayer's:
   a. son, daughter, adopted child, stepchild, or a descendent of any of them
   b. brother, sister, stepbrother, stepsister, or a descendent of any of them if the taxpayer cares for the individual as the taxpayer would their own child
   c. eligible foster child

EXAMPLE – Tami's son turned 17 on December 30, 20X6. He is a citizen of the United States and Tami claimed him as a dependent on her return. He is not a qualifying child for the child tax credit because he was not under age 17 at the end of 20X6.

Adopted Child

An adopted child is always treated as the taxpayer's own child. A child placed with the taxpayer by an authorized agency for legal adoption is considered adopted, even if the adoption is not finalized.

NOTE - To claim the Child Tax Credit, both the taxpayer (or one spouse on a joint return) and each qualifying child must have valid Social Security numbers issued by the SSA to U.S. citizens or qualifying individuals before the tax return due date.

Premium Assistance Tax Credit (§36B)

Eligibility for Premium Tax Credit (§1.36B-2)

General Rule (§1.36B-2(a))

An applicable taxpayer is allowed a premium assistance amount only for any month that one or more members of the applicable taxpayer's family (the applicable taxpayer or the applicable taxpayer's spouse or dependent):

1. Is enrolled in one or more qualified health plans through an Exchange; AND
2. Is not eligible for minimum essential coverage (within the meaning of §1.36B-2(c)) other than coverage described in §5000A(f)(1)(C) (relating to coverage in the individual market).

Applicable taxpayer (§1.36B-2(b))

In general, an applicable taxpayer is a taxpayer whose household income is at least 100% but not more than 400% of the Federal poverty line for the taxpayer's family size for the taxable year.

Poverty guidelines for the 48 contiguous states & the district of Columbia Year 2025		
Persons in family/household	**100% Poverty line**	**400% Poverty line**
1	$15,650	$62,600
2	$21,150	$84,600
3	$26,650	$106,600
4	$32,150	$128,600
5	$37,650	$150,600
6	$43,150	$172,600
7	$48,650	$194,600
8	$54,150	$216,600
more than 8	For families/households with more than 8 persons, add $5,500 for each additional person.	
Website – The poverty guidelines are located at http://aspe.hhs.gov/poverty		

Married taxpayers must file joint return (§1.36B-2(b)(2))

In general, a taxpayer who is married (within the meaning of §7703) at the close of the taxable year is an applicable taxpayer only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.

NOTE – §1.36B-2T(b)(2)(i)-(v) provides exceptions for victims of domestic abuse and abandonment.

Dependents (§1.36B-2(b)(3))

An individual is not an applicable taxpayer if another taxpayer may claim a deduction under §151 for the individual for a taxable year beginning in the calendar year in which the individual's taxable year begins.

Individuals not lawfully present or incarcerated (§1.36B-2(b)(4))

An individual who is not lawfully present in the United States or is incarcerated (other than incarceration pending disposition of charges) is not eligible to enroll in a qualified health plan through an Exchange. However, the individual may be an applicable taxpayer if a family member is eligible to enroll in a qualified health plan.

Family and family size defined (§1.36B-1(d))

A taxpayer's family means the individuals for whom a taxpayer properly claims a deduction for a personal exemption under §151 for the taxable year. Family size means the number of individuals in the family. Family and family size may include individuals who are not subject to or are exempt from the penalty under §5000A for failing to maintain minimum essential coverage.

NOTE – §1.36B-1(f) states that a dependent has the same meaning as in IRC §152.

Household income defined (§1.36B-1(e))

Household income means the sum of:

1. A taxpayer's modified adjusted gross income; and
2. The aggregate modified adjusted gross income of all other individuals who:
   a. Are included in the taxpayer's family (i.e., dependents properly claimed under §151); and
   b. Are required to file a Federal income tax return for the taxable year.

Modified adjusted gross income (MAGI) means adjusted gross income (within the meaning of §62) increased by:

1. Amounts excluded from gross income under §911 (i.e., the foreign earned income exclusion for U.S. citizens or residents living abroad);
2. Tax-exempt interest the taxpayer receives or accrues during the taxable year; and
3. Social security benefits (within the meaning of §86(d)) not included in gross income.

Minimum essential coverage (§1.36B-2(c))

Minimum essential coverage (MEC) is defined in §5000A(f) and regulations issued under that section as:

1. government-sponsored programs,
2. eligible employer-sponsored plans,
3. grandfathered health plans, and
4. certain other health benefits coverage.

NOTE – MEC will be reported on a Form 1095-A, Form 1095-B and/or Form 1095-C.

Employer-sponsored "affordable" coverage (§1.36B-2(c)(3)(v))

Affordability for employee (§1.36B-2(c)(3)(v)(A)(1))

In general, an eligible employer-sponsored plan is affordable for an employee if the portion of the annual premium the employee must pay, whether by salary reduction or otherwise (required contribution), for **self-only coverage does not exceed the required contribution percentage (i.e., 9.5% adjusted annually after 2014) of the applicable taxpayer's household income for the taxable year**.

Plan years beginning in:	Required contribution percentage:
2024	8.39%
2025	9.02%
2026	9.96%

Affordability for related individual (§1.36B-2(c)(3)(v)(A)(2))

In general, an eligible employer- sponsored plan is affordable for a related individual if the portion of the annual premium the employee must pay for **self-only coverage** does not exceed the required contribution percentage (as described in the prior paragraph).

Final Regs. - Employer-sponsored "affordable" coverage (TD 9968)

Final regulations under §36B were issued on October 11, 2022 amending the regulations regarding eligibility for the premium tax credit (PTC) to provide that affordability of employer-sponsored minimum essential coverage (employer coverage) for family members of an employee is determined based on the employee's share of the cost of covering the employee and those family members, not the cost of covering only the employee. The final regulations also add a minimum value rule for family members of employees based on the benefits provided to the family members. The final regulations affect taxpayers who enroll, or enroll a family member, in individual health insurance coverage through a Health Insurance Exchange (Exchange) and who may be allowed a PTC for the coverage.

NOTE – The regulations are effective December 13, 2022. (i.e., 60 days after date of publication).

Affordability for related individual - §1.36B-2(c)(3)(v)(A)(2)

Except as provided in employee safe harbor (§1.36B-2(c)(3)(v)(A)(3)), employer-sponsored plan is affordable for a related individual if the employee's required contribution for family coverage under the plan does not exceed the required contribution percentage of the applicable taxpayer's household income for the taxable year. An employee's required contribution for family coverage is the portion of the annual premium the employee must pay for coverage of the employee and all other individuals included in the employee's family, as defined in §1.36B-1(d), who are offered coverage under the eligible employer-sponsored plan.

NOTE - Employee safe harbor under §1.36B-2(c)(3)(v)(A)(3) states: An eligible employer-sponsored plan is not affordable for an employee or a related individual for a plan year if, when the employee or a related individual enrolls in a qualified health plan for a period coinciding with the plan year (in whole or in part), an Exchange determines that the eligible employer-sponsored plan is not affordable for that plan year.

Multiple offers of coverage - §1.36B-2(c)(3)(v)(A)(8)(B)

An individual who has offers of coverage under eligible employer-sponsored plans from multiple employers, either as an employee or a related individual, has an offer of affordable coverage if at least one of the offers of coverage is affordable under §1.36B-2(c)(3)(v)(A)(1) or (2). Coverage under an eligible employer-sponsored plan is affordable for a part-year period if the annualized required contribution for self-only coverage, in the case of an employee, or family coverage, in the case of a related individual, under the plan for the part-year period does not exceed the required contribution percentage of the applicable taxpayer's household income for the taxable year.

Examples - §1.36B-2(c)(3)(v)(A)(8)(D)

EXAMPLE 1 - Basic determination of affordability

For all of 2023, taxpayer C works for an employer, X, that offers its employees and their spouses a health insurance plan under which, to enroll in self-only coverage, C must contribute an amount for 2023 that does not exceed the required contribution percentage of C's 2023 household income. Because C's required contribution for self-only coverage does not exceed the required contribution percentage of C's household income, X's plan is affordable for C, and C is eligible for minimum essential coverage for all months in 2023.

EXAMPLE 2 - Basic determination of affordability for a related individual

The facts are the same as Example 1, except that C is married to J, they file a joint return, and to enroll C and J, X's plan requires C to contribute an amount for coverage for C and J for 2023 that exceeds the required contribution percentage of C's and J's household income. J does not work for an employer that offers employer-sponsored coverage.

J is a member of C's family as defined in §1.36B-1(d). Because C's required contribution for coverage of C and J exceeds the required contribution percentage of C's and J's household income, X's plan is unaffordable for J. Accordingly, J is not eligible for minimum essential coverage for 2023. However, X's plan is affordable for C, and C is eligible for minimum essential coverage for all months in 2023.

EXAMPLE 3 - Multiple offers of coverage

The facts are the same as in Example 2, except that J works all year for an employer that offers employer-sponsored coverage to employees. J's required contribution for the cost of self-only coverage from J's employer does not exceed the required contribution percentage of C's and J's household income. Although the coverage offered by C's employer for C and J is unaffordable for J, the coverage offered by J's employer is affordable for J. Consequently, J is eligible for minimum essential coverage for all months in 2023.

EXAMPLE 4 - Cost of covering individuals not part of taxpayer's family

D and E are married, file a joint return, and have two children, F and G, under age 26. F is a dependent of D and E, but G is not. D works all year for an employer that offers employer-sponsored coverage to employees, their spouses, and their children under age 26. E, F, and G do not work for employers offering coverage. D's required contribution for self-only coverage under D's employer's coverage does not exceed the required contribution percentage of D's and E's household income. D's required contribution for coverage of D, E, F, and G exceeds the required contribution percentage of D's and E's household income, but D's required contribution for coverage of D, E, and F does not exceed the required contribution percentage of the household income.

E and F are members of D's family as defined in §1.36B-1(d). G is not a member of D's family under §1.36B-1(d), because G is not D's dependent. D's employer's coverage is affordable for D because D's required contribution for self-only coverage does not exceed the required contribution percentage of D's and E's household income. D's employer's coverage also is affordable for E and F, because D's required contribution for coverage of D, E, and F does not exceed the required contribution percentage of D's and E's household income. Although D's cost to cover D, E, F, and G exceeds the required contribution percentage of D's and E's household income, the cost to cover G is not considered in determining whether D's employer's coverage is affordable for E and F, regardless of whether G actually enrolls in the plan, because G is not in D's family. D, E, and F are eligible for minimum essential coverage for all months in 2023. Under the related party rule under §1.36B-2(c)(4)(i), G is considered eligible for the coverage offered by D's employer only if G enrolls in the coverage.

EXAMPLE 5 - More than one family member with an employer offering coverage

K and L are married, file a joint return, and have one dependent child, M. K works all year for an employer that offers coverage to employees, spouses, and children under age 26. L works all year for an employer that offers coverage to employees only. K's required contribution for self-only coverage under K's employer's coverage does not exceed the required contribution percentage of K's and L's household income. Likewise, L's required contribution for self-only coverage under L's employer's coverage does not exceed the required contribution percentage of K's and L's household income. However, K's required contribution for coverage of K, L, and M exceeds the required contribution percentage of K's and L's household income.

L and M are members of K's family as defined in §1.36B-1(d). K's employer's coverage is affordable for K because K's required contribution for self-only coverage does not exceed the required contribution percentage of K's and L's household income. Similarly, L's employer's coverage is affordable for L, because L's required contribution for self-only coverage does not exceed the required contribution percentage of K's and L's household income. Thus, K and L are eligible for minimum essential coverage for all months in 2023. However, K's employer's coverage is unaffordable for M, because K's required contribution for coverage of K, L, and M exceeds the required contribution percentage of K's and L's household income. Accordingly, M is not eligible for minimum essential coverage for 2023.

EXAMPLE 6 - Multiple offers of coverage for a related individual

The facts are the same as in Example 5, except that L works all year for an employer that offers coverage to employees, spouses, and children under age 26. L's required contribution for coverage of K, L, and M does not exceed the required contribution percentage of K's and L's household income.

Although M is not eligible for affordable employer coverage under K's employer's coverage, the multiple offers rule dictates that L's employer coverage must be evaluated to determine whether L's employer coverage is affordable for M. Thus, L's employer's coverage is affordable for M, because L's required contribution for K, L, and M does not exceed the required contribution percentage of K's and L's household income. Accordingly, M is eligible for minimum essential coverage for all months in 2023.

Premium assistance amount (§1.36B-3(d))

In general, the premium assistance amount for a coverage month is the **lesser of:**

1. The premiums for the month, **reduced by any amounts that were refunded in the same taxable year as the premium liability is incurred**, for one or more qualified health plans in which a taxpayer or a member of the taxpayer's family enrolls (enrollment premiums); or
2. The excess of the adjusted monthly premium for the applicable benchmark plan (i.e., second lowest cost silver plan) over 1/12 of the product of a taxpayer's household income and the applicable percentage for the taxable year.

Applicable percentage (§1.36B-3T(g))

The applicable percentage multiplied by a taxpayer's household income determines the taxpayer's annual required share of premiums for the benchmark plan. The required share is divided by 12 and this monthly amount is subtracted from the adjusted monthly premium for the applicable benchmark plan when computing the premium assistance amount. The applicable percentage is computed by first determining the percentage that the taxpayer's household income bears to the Federal poverty line for the taxpayer's family size. The resulting Federal poverty line percentage is then compared to the income categories described in the table below (or successor tables). An applicable percentage within an income category increases on a sliding scale in a linear manner and is rounded to the nearest one-hundredth of one percent.

For taxable years beginning in 2026, the applicable percentage table was		
Household Income (expressed as percent of poverty level)	**Initial Premium (percentage)**	**Final Premium (percentage)**
Less than 133%	2.10	2.10
At least 133% but less than 150%	3.14	4.19
At least 150% but less than 200%	4.19	6.60
At least 200% but less than 250%	6.60	8.44
At least 250% but less than 300%	8.44	9.96
At least 300% but less than 400%	9.96	9.96

Modifications for 2021 to 2025 – Improving Affordability by Expanding Premium Assistance for Consumers

The ARPA temporarily (for 2021 & 2022) expanded the eligibility for and the amount of the premium tax credit (PTC) by modifying the 1) income eligibility criteria by eliminating the current-law phaseout for households with annual incomes above 400% of the federal poverty level (FPL) and 2) credit formula by temporarily increasing the credit amount by reducing the percentage of annual income that eligible households are required to contribute toward the premium. The temporary percentages range from 0.0% to 8.5% of household income, with higher-income groups subject to the larger percentages, as specified.

UPDATE – The Inflation Reduction Act (IRA) of 2022 (H.R. 5376) extended this through 2025.

For taxable years beginning in 2021 through 2025, the applicable percentage table is		
Household Income (expressed as percent of poverty level)	**Initial Premium (percentage)**	**Final Premium (percentage)**
Up to 150%	0	0
150% up to 200%	0	2.0
200% up to 250%	2.0	4.0
250% up to 300%	4.0	6.0
300% up to 400%	6.0	8.5
400% and higher	8.5	8.5

Requirement of income tax return (§1.6011-8(a))

A taxpayer who receives advance payments of the premium tax credit under §36B must file an income tax return for that taxable year on or before the due date for the return (including extension of time for filing).

NOTE – Individuals will be required to attach a ***Form 8962*** ***– Premium Tax Credit (PTC)*** to the individual income tax return in a year they receive any §36B advance payments. A health insurance exchange reports information to the taxpayer and IRS on a Form 1095-A.

Coordination of premium tax credit with advance credit payments (§1.36B-4(a)(1))

A taxpayer must reconcile the amount of credit allowed under §36B with advance credit payments on the taxpayer's income tax return for a taxable year. A taxpayer whose premium tax credit for the taxable year exceeds the taxpayer's advance credit payments may receive the excess as an income tax refund. A taxpayer whose advance credit payments for the taxable year exceed the taxpayer's premium tax credit owes the excess as an additional income tax liability.

NOTE – The additional tax imposed under §1.36B-4(a)(1) on a taxpayer whose household income is less than 400% of the Federal poverty line is limited to the amounts provided in the table below.

Household income percentage of Federal poverty line	**2025 limitation amount for:**	
	single taxpayers	all other taxpayers
Less than 200%	$375	$750
At least 200% but less than 300%	$975	$1,950
At least 300% but less than 400%	$1,625	$3,250

UPDATE – The OBBB removes this cap (by repealing §36B(f)(2)(B)) for tax years after 2025, allowing any excess premium tax credit to be fully recaptured regardless of income level.

Special Rules

The regulations provide special rules for:

1. Changes in filing status (§1.36B-4(b)(1))
2. Taxpayers who marry during the taxable year (§1.36B-4(b)(2))
3. Taxpayers not married to each other at the end of the taxable year (§1.36B-4T(b)(3)) – this is an alternative calculation to possibly reduce the additional tax owed (not increase the §36B credit)
4. Married taxpayers filing separate returns or head of household (§1.36B-4(b)(4))

Information Reporting by Exchanges (§1.36B-5)

In general, an Exchange must report to the Internal Revenue Service (IRS) information required by §36B(f)(3) and this section relating to individual market qualified health plans in which individuals enroll through the Exchange (**Form 1095-A**).

Foreign Account Compliance

Report of Foreign Bank & Financial Accounts (FBAR)

Background – Foreign Bank & Financial Accounts (FBAR)

If you have a financial interest in or signature authority over a foreign financial account, including a bank account, brokerage account, mutual fund, trust, or other type of foreign financial account, exceeding certain thresholds, the Bank Secrecy Act may require you to report the account yearly to the Internal Revenue Service by filing electronically a Financial Crimes Enforcement Network (FinCEN) ***Form 114**, Report of Foreign Bank and Financial Accounts (FBAR).*

NOTE – Click here for Reporting of FBAR information at the IRS website.

Who Must File an FBAR

United States persons are required to file a *Report of Foreign Bank and Financial Accounts (FBAR)* if:

1. The United States person had a financial interest in or signature authority over at least one financial account located outside of the United States; and
2. The aggregate value of all foreign financial accounts exceeded $10,000 at any time during the calendar year to be reported.

NOTE – United States person means United States citizens; United States residents; entities, including but not limited to, corporations, partnerships, or limited liability companies created or organized in the United States or under the laws of the United States; and trusts or estates formed under the laws of the United States.

Exceptions to the Reporting Requirement

Exceptions to the FBAR reporting requirements can be found in the FBAR Instructions. There are filing exceptions for the following United States persons or foreign financial accounts:

1. Certain foreign financial accounts jointly owned by spouses;
2. United States persons included in a consolidated FBAR;
3. Correspondent/Nostro accounts;
4. Foreign financial accounts owned by a governmental entity;
5. Foreign financial accounts owned by an international financial institution;
6. IRA owners and beneficiaries;
7. Participants in and beneficiaries of tax-qualified retirement plans;
8. Certain individuals with signature authority over, but no financial interest in, a foreign financial account;
9. Trust beneficiaries; and
10. Foreign financial accounts maintained on a United States military banking facility.

NOTE – Review the FBAR instructions to determine eligibility for an exception and to review exception requirements.

Reporting & Filing Information

Due October 15th with Automatic 6 month extension

The FBAR is a calendar year report and must be filed on or before April 15 of the year following the calendar year being reported. There is an automatic extension to October 15 if you fail to meet the FBAR annual due date of April 15. You do not need to request an extension to file the FBAR.

Additional extensions

If you are affected by a natural disaster, the government may further extend your FBAR due date.

NOTE – Review relevant FBAR Relief Notices for complete information.

How to file

- The FBAR is not filed with a federal tax return. The FBAR must be filed electronically through FinCEN's BSA E-Filing System.
- If you want to paper-file your FBAR, you must call FinCEN's Regulatory Helpline to request an exemption from e-filing. See Contact Us below to reach this Helpline. If FinCEN approves your request, FinCEN will send you the paper FBAR form to complete and mail to the IRS at the address in the form's instructions. IRS will not accept paper-filings on TD F 90-22.1 (obsolete) or a printed FinCEN Form 114 (for e-filing only).
- If you want someone to file your FBAR on your behalf, use FinCEN Report 114a, Record of Authorization to Electronically File FBARs, to authorize that person to do so. You don't submit FinCEN Report 114a when filing the FBAR; just keep it for your records and make it available to FinCEN or IRS upon request.

Penalties

You may be subject to civil monetary penalties and/or criminal penalties for FBAR reporting and/or recordkeeping violations. Assertion of penalties depends on facts and circumstances. Civil penalty maximums must be adjusted annually for inflation.

NOTE - Click here for current maximum penalty amounts.

Filing Delinquent FBARs

Filing an FBAR late or not at all is a violation and may subject you to the penalties above. If you have not been contacted by IRS about a late FBAR and are not under civil or criminal investigation by IRS, you may file late FBARs and, to keep potential penalties to a minimum, should do so as soon as possible. Go to https://www.fincen.gov/filing-late for additional information. If you are participating in an optional program to resolve FBAR noncompliance, such as Delinquent FBAR Submission Procedures or Streamlined Filing Compliance Procedures, follow the instructions for those programs.

Recordkeeping

You must keep records for each account you must report on an FBAR that establish the:

1. Name on the account,
2. Account number,
3. Name and address of the foreign bank,
4. Type of account, and
5. Maximum value during the year.

The law does not specify the type of document to keep with this information; it can be bank statements or a copy of a filed FBAR, for example, if they have all the information. You must keep these records for five years from the due date of the FBAR.

NOTE – An officer or employee who files an FBAR to report signature authority over an employer's foreign financial account doesn't need to personally keep records on these accounts. The employer must keep the records for these accounts.

Disclosure of Information with Respect to Foreign Financial Assets (§6038D)

Disclosure Statement Required for Specified Foreign Financial Assets

IRC §6038D requires individual taxpayers with an interest in a "specified foreign financial asset" during the taxable year to attach a disclosure statement to their income tax return for any year in which the aggregate value of all such assets is greater than $50,000.

NOTE – This will be reported on the *Form 8938* – *Statement of Specified Foreign Financial Assets*.

Per the instructions to the Form 8938, the reporting threshold depends upon whether the taxpayer is married, files a joint federal income tax return, and lived inside (or outside) the United States.

Filing Status	Taxpayers Living Inside the U.S.	Taxpayer Living Outside the U.S.*
Unmarried taxpayers	If you are not married, you satisfy the reporting threshold only if the total value of your specified foreign financial assets is more than $50,000 on the last day of the tax year or more than $75,000 at any time during the tax year.	If you are not married, you satisfy the reporting threshold only if the total value of your specified foreign financial assets is more than $200,000 on the last day of the tax year or more than $300,000 at any time during the tax year.
Married taxpayers filing a joint income tax return	If you are married and you and your spouse file a joint income tax return, you satisfy the reporting threshold only if the total value of your specified foreign financial assets is more than $100,000 on the last day of the tax year or more than $150,000 at any time during the tax year.	If you are married and you and your spouse file a joint income tax return, you satisfy the reporting threshold only if the total value of your specified foreign financial assets is more than $400,000 on the last day of the tax year or more than $600,000 at any time during the tax year.
Married taxpayers filing separate income tax returns	If you are married and file a separate income tax return from your spouse, you satisfy the reporting threshold only if the total value of your specified foreign financial assets is more than $50,000 on the last day of the tax year or more than $75,000 at any time during the tax year.	If you are married and file a separate income tax return from your spouse, you satisfy the reporting threshold only if the total value of your specified foreign financial assets is more than $200,000 on the last day of the tax year or more than $300,000 at any time during the tax year.

*Note - If your tax home is in a foreign country, you meet one of the presence abroad tests, and no exception applies, file Form 8938 with your income tax return if you satisfy the reporting threshold. You satisfy the presence abroad test if you are one of the following:
- A U.S. citizen who has been a bona fide resident of a foreign country or countries for an uninterrupted period that includes an entire tax year.
- A U.S. citizen or resident who is present in a foreign country or countries at least 330 full days during any period of 12 consecutive months that ends in the tax year being reported.

Specified Foreign Financial Assets Defined

Specified foreign financial assets are:

1. depository or custodial accounts at foreign financial institutions and
2. to the extent not held in an account at a financial institution
    a. stocks or securities issued by foreign persons,
    b. any other financial instrument or contract held for investment that is issued by or has a counterparty that is not a U.S. person, and
    c. any interest in a foreign entity.

Required Information

The information to be included on the statement includes identifying information for each asset and its maximum value during the taxable year. For an account, the name and address of the institution at which the account is maintained and the account number are required. For a stock or security, the name and address of the issuer, and any other information necessary to identify the stock or security and terms of its issuance must be provided. For all other instruments or contracts, or interests in foreign entities, the information necessary to identify the nature of the instrument, contract or interest must be provided, along with the names and addresses of all foreign issuers and counterparties. An individual is not required under this provision to disclose interests that are held in a custodial account with a U.S. financial institution nor is an individual required to identify separately any stock, security instrument, contract, or interest in a foreign financial account disclosed under the provision. In addition, the provision permits the Secretary to issue regulations that would apply the reporting obligations to a domestic entity in the same manner as if such entity were an individual if that domestic entity is formed or availed of to hold such interests, directly or indirectly.

Penalty for Failure to Disclose

Individuals who fail to make the required disclosures are subject to a penalty of $10,000 for the taxable year. An additional penalty may apply if the Secretary notifies an individual by mail of the failure to disclose and the failure to disclose continues. If the failure continues beyond 90 days following the mailing, the penalty increases by $10,000 for each 30-day period (or a fraction thereof), up to a maximum penalty of $50,000 for one taxable period. The computation of the penalty is similar to that applicable to failures to file reports with respect to certain foreign corporations under §6038.

EXAMPLE – Thus, an individual who is notified of his failure to disclose with respect to a single taxable year under this provision and who takes remedial action on the 95th day after such notice is mailed incurs a penalty of $20,000 comprising the base amount of $10,000, plus $10,000 for the fraction (i.e., the five days) of a 30-day period following the lapse of 90 days after the notice of noncompliance was mailed. An individual who postpones remedial action until the 181st day is subject to the maximum penalty of $50,000: the base amount of $10,000, plus $30,000 for the three 30-day periods, plus $10,000 for the one fraction (i.e., the single day) of a 30-day period following the lapse of 90 days after the notice of noncompliance was mailed.

Reasonable Cause Exception

No penalty is imposed under the provision against an individual who can establish that the failure was due to reasonable cause and not willful neglect. Foreign law prohibitions against disclosure of the required information cannot be relied upon to establish reasonable cause.

Presumption the Value of Specified Foreign Financial Assets Exceeds $50,000
To the extent the Secretary determines that the individual has an interest in one or more foreign financial assets but the individual does not provide enough information to enable the Secretary to determine the aggregate value thereof, the aggregate value of such identified foreign financial assets will be presumed to have exceeded $50,000 for purposes of assessing the penalty. The provision also grants authority to promulgate regulations necessary to carry out the intent. Such regulations may include exceptions for nonresident aliens and classes of assets identified by the Secretary, including those assets which the Secretary determines are subject to reporting requirements under other provisions of the Code. In particular, regulatory exceptions to avoid duplicative reporting requirements are anticipated.

6-Year Statute of Limitations

The HIREA of 2010 provision authorizes a new 6-year limitations period for assessment of tax on understatements of income attributable to foreign financial assets.

NOTE – The present exception that provides a 6-year period for substantial omission of an amount equal to 25% of the gross income reported on the return is not changed.

This new limitation period applies if there is an omission of gross income in excess of $5,000 and the omitted gross income is attributable to an asset with respect to which information reports are required under §6038D (i.e., information with respect to foreign financial assets), as applied without regard to the dollar threshold, the statutory exception for nonresident aliens and any exceptions provided by regulation. If a domestic entity is formed or availed of to hold foreign financial assets and is subject to the reporting requirements of §6038D in the same manner as an individual, the 6-year limitations period may also apply to that entity. The Secretary is permitted to assess the resulting deficiency at any time within six years of the filing of the income tax return.

In providing that the applicability of §6038D information reporting requirements is to be determined without regard to the statutory or regulatory exceptions, the statute ensures that the longer limitation period applies to omissions of income with respect to transactions involving foreign assets owned by individuals. Thus, a regulatory provision that alleviates duplicative reporting obligations by providing that a report that complies with another provision of the Code may satisfy one's obligations under new §6038D does not change the nature of the asset subject to reporting. The asset remains one that is subject to the requirements of §6038D for purposes of determining whether the exception to the 3-year statute of limitations applies.

Passive Foreign Investment Corporations
The provision also suspends the limitations period for assessment if a taxpayer fails to provide timely information returns required with respect to passive foreign investment corporations and the new self-reporting of foreign financial assets. The limitations period will not begin to run until the information required by those provisions has been furnished to the Secretary. The provision also clarifies that the extension is not limited to adjustments to income related to the information required to be reported by one of the enumerated sections.

40% Accuracy-Related Penalty

The HIREA of 2010 provision adds a new 40% accuracy related penalty on any understatement attributable to an undisclosed foreign financial asset to IRC §6662.

NOTE – The new provision is subject to the same defenses as are otherwise available under §6662,

Undisclosed Foreign Financial Asset

The term "undisclosed foreign financial asset" includes all assets subject to certain information reporting requirements for which the required information was not provided by the taxpayer as required under the applicable reporting provisions. An understatement is attributable to an undisclosed foreign financial asset if it is attributable to any transaction involving such asset. Thus, a U.S. person who fails to comply with the various self-reporting requirements for a foreign financial asset and engages in a transaction with respect to that asset incurs a penalty on any resulting underpayment that is double the otherwise applicable penalty for substantial understatements or negligence.

EXAMPLE – If a taxpayer fails to disclose amounts held in a foreign financial account, any underpayment of tax related to the transaction that gave rise to the income would be subject to the penalty provision, as would any underpayment related to interest, dividends or other returns accrued on such undisclosed amounts.

Final Regulations Issued

On December 12, 2014 the Internal Revenue Service published final regulations under §6038D (TD 9706). These regulations adopted the 2011 temporary regulations with certain modifications. The regulations did not finalize Prop. Reg. §1.6038D-6 - Specified domestic entities.

NOTE – The regulations apply to taxable years ending after December 19, 2011. Taxpayers may elect to apply the rules to taxable years ending prior to December 19, 2011.

On February 23, 2016 the IRS finalized regulations (TD 9752) under §1.6038D-6 – Specified Domestic Entities.

NOTE – These regulations are effective for taxable years beginning after December 31, 2015.

PFIC Ownership & Filing Final Regulations (TD 9806)

On December 27, 2016 the IRS issued final regulations providing guidance on determining who is an owner of a PFIC, the annual filing requirements for shareholders of PFICs, and statements required to be filed with IRS by persons who are excepted from the Form 5471 filing.

Form 8938 & FBAR Comparison Charts

	Form 8938, Statement of Specified Foreign Financial Assets	**FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR)**
Who Must File?	Specified individuals and specified domestic entities that have an interest in specified foreign financial assets and meet the reporting threshold. **Specified individuals** include U.S citizens, resident aliens, and certain non-resident aliens. **Specified domestic entities** include certain domestic corporations, partnerships, and trusts	U.S. persons, which include U.S. citizens, resident aliens, trusts, estates, and domestic entities that have an interest in foreign financial accounts and meet the reporting threshold
Does the United States include U.S. territories?	No	Yes, resident aliens of U.S territories and U.S. territory entities are subject to FBAR reporting
Reporting Threshold (Total Value of Assets)	***Taxpayers living in the US:*** **Unmarried taxpayer (or married filing separately):** Total value of assets was more than $50,000 on the last day of the tax year, or more than $75,000 at any time during the year. **Married taxpayer filing jointly:** Total value of assets was more than $100,000 on the last day of the tax year, or more than $150,000 at any time during the year. ***Taxpayers living outside the US:*** **Unmarried taxpayer** (or married filing separately): Total value of assets was more than $200,000 on the last day of the tax year, or more than $300,000 at any time during the year. **Married taxpayer filing jointly:** Total value of assets was more than $400,000 on the last day of the tax year, or more than $600,000 at any time during the year. **Specified domestic entities:** Total value of assets was more than $50,000 on the last day of the tax year, or more than $50,000 at any time during the tax year.	Aggregate value of financial accounts exceeds $10,000 at any time during the calendar year. This is a cumulative balance, meaning if you have 2 accounts with a combined account balance greater than $10,000 at any one time, both accounts would have to be reported.

	Form 8938	FinCEN Form 114 (FBAR)
When do you have an interest in an account or asset?	If any income, gains, losses, deductions, credits, gross proceeds, or distributions from holding or disposing of the account or asset are or would be required to be reported, included, or otherwise reflected on your income tax return	**Financial interest:** you are the owner of record or holder of legal title; the owner of record or holder of legal title is your agent or representative; you have a sufficient interest in the entity that is the owner of record or holder of legal title. **Signature authority:** you have authority to control the disposition of the assets in the account by direct communication with the financial institution maintaining the account. See instructions for further details.
What is Reported?	Maximum value of specified foreign financial assets, which include financial accounts with foreign financial institutions and certain other foreign non-account investment assets	Maximum value of financial accounts maintained by a financial institution physically located in a foreign country
How are maximum account or asset values determined and reported?	Fair market value in U.S. dollars in accord with the Form 8938 instructions for each account and asset reported Convert to U.S. dollars using the end of the taxable year exchange rate and report in U.S. dollars.	Use periodic account statements to determine the maximum value in the currency of the account. Convert to U.S. dollars using the end of the calendar year exchange rate and report in U.S. dollars.
When Due?	Form is attached to your annual return and due on the date of that return, including any applicable extensions	Received by April 15 (6-month automatic extension to October 15)
Where to File?	File the Form 8938 with income tax return pursuant to instructions for filing the return.	File electronically through FinCENs BSA E-Filing System. The FBAR is not filed with a federal tax return.
Penalties	Up to $10,000 for failure to disclose and an additional $10,000 for each 30 days of non-filing after IRS notice of a failure to disclose, for a potential maximum penalty of $60,000; criminal penalties may also apply	Civil monetary penalties are adjusted annually for inflation. For civil penalty assessment prior to August 1, 2016, if non-willful, up to $10,000; if willful, up to the greater of $100,000 or 50% of account balances; criminal penalties may also apply.

Types of Foreign Assets and Whether They are Reportable		
Reportable Assets	**Form 8938, Statement of Specified Foreign Financial Assets**	**FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR)**
Financial (deposit and custodial) accounts held at foreign financial institutions	Yes	Yes
Financial account held at a foreign branch of a U.S. financial institution	No	Yes
Financial account held at a U.S. branch of a foreign financial institution	No	No
Foreign financial account for which you have signature authority	No, unless you otherwise have an interest in the account as described above	Yes, subject to exceptions
Foreign stock or securities held in a financial account at a foreign financial institution	The account itself is subject to reporting, but the contents of the account do not have to be separately reported	The account itself is subject to reporting, but the contents of the account do not have to be separately reported
Foreign stock or securities not held in a financial account	Yes	No
Foreign partnership interests	Yes	No
Indirect interests in foreign financial assets through an entity	No	Yes, if sufficient ownership or beneficial interest (i.e., a greater than 50& interest) in the entity. See instructions for further detail.
Foreign mutual funds	Yes	Yes
Domestic mutual fund investing in foreign stocks and securities	No	No
Foreign accounts and foreign non-account investment assets held by foreign or domestic grantor trust for which you are the grantor	Yes, as to both foreign accounts and foreign non-account investment assets	Yes, as to foreign accounts
Foreign-issued life insurance or annuity contract with a cash-value	Yes	Yes
Foreign hedge funds and foreign private equity funds	Yes	No
Foreign real estate held directly	No	No
Foreign real estate held through a foreign entity	No, but the foreign entity itself is a specified foreign financial asset and its maximum value includes the value of the real estate	No

Types of Foreign Assets and Whether They are Reportable		
Reportable Assets	**Form 8938**	**FinCEN Form 114 (FBAR)**
Foreign currency held directly	No	No
Precious Metals held directly	No	No
Personal property, held directly, such as art, antiques, jewelry, cars and other collectibles	No	No
'Social Security'- type program benefits provided by a foreign government	No	No
Source - http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements		

Miscellaneous Topics

Charitable Conservation Easement & Listed Transactions

NOTE – Click here for the IRS list of recognized abusive and listed transactions click here for additional information about abusive tax shelters and transactions.

Prop. Regs. – Certain CRATS are Listed Transactions (REG-108761-22)

On March 22, 2024, proposed regulations were issued to identify certain charitable remainder annuity trust (CRAT) transactions and substantially similar transactions as listed transactions, a type of reportable transaction. Material advisors and certain participants in these listed transactions would be required to file disclosures with the IRS and would be subject to penalties for failure to disclose. The proposed regulations would affect participants in these transactions as well as material advisors but provide that certain organizations whose only role or interest in the transaction is as a charitable remainderman will not be treated as participants in the transaction or as parties to a prohibited tax shelter transaction subject to excise taxes and disclosure requirements. This would be effective after the regulations are finalized.

Qualified Conservation Contributions Final Regulations (TD 9999)

This document contains final regulations concerning the statutory disallowance rule enacted by the SECURE 2.0 Act of 2022 to disallow a Federal income tax deduction for a qualified conservation contribution made by a partnership or an S corporation after December 29, 2022, if the amount of the contribution exceeds 2.5 times the sum of each partner's or S corporation shareholder's relevant basis. These final regulations provide guidance regarding this statutory disallowance rule, including definitions, appropriate methods to calculate the relevant basis of a partner or an S corporation shareholder, the three statutory exceptions to the statutory disallowance rule, and related reporting requirements. In addition, these final regulations provide reporting requirements for partners and S corporation shareholders that receive a distributive share or pro rata share of any noncash charitable contribution made by a partnership or S corporation, regardless of whether the contribution is a qualified conservation contribution (and regardless of whether the contribution is of real property or other noncash property). These final regulations affect partnerships and S corporations that claim qualified conservation contributions, and partners and S corporation shareholders that receive a distributive share or pro rata share, as applicable, of a noncash charitable contribution.

NOTE - These regulations are effective on June 28, 2024, and generally apply to contributions made after December 29, 2022.

IRS sent settlement offer letters to certain taxpayers who participated in Syndicated Conservation Easement transactions (IR-2024-174)

On June 26, 2024, the IRS announced (IR-2024-174) that it sent time-limited settlement offer letters in July to certain taxpayers who had participated in Syndicated Conservation Easement (SCE) transactions or substantially similar arrangements and were under audit. Eligible taxpayers were notified by letter, which outlined the terms and deadlines for the settlement. The settlement required substantial concession of the claimed tax benefits and the acceptance of penalties. Taxpayers who received a letter but chose not to participate remained subject to IRS enforcement, including the potential for full disallowance of the charitable contribution deduction and all applicable penalties. Taxpayers who did not receive a letter, or whose cases were pending in the

U.S. Tax Court, were not eligible for this settlement offer. The IRS continued enforcement actions against all ineligible or non-participating taxpayers.

Final Regulations Identifying Syndicated Conservation Easement Transactions as Abusive Tax Transactions (TD 10007)

On October 7, 2024, the Department of the Treasury and the IRS issued final regulations (TD 10007) identifying certain syndicated conservation easement transactions as listed transactions (i.e., abusive tax transactions that must be reported to the IRS).

NOTE - Syndicated conservation easements have been included in the IRS' annual list of Dirty Dozen tax schemes for many years.

In these transactions, investors typically acquire an interest in a partnership that owns land and then claim an inflated charitable contribution deduction based on a grossly overvalued appraisal. Going forward, participants and material advisors will need to report their participation in these transactions using *Form 8886 - Reportable Transaction Disclosure Statement* and *Form 8918 - Material Advisor Disclosure Statement*.

NOTE – Form more detailed IRS information on recognized abusive and listed transactions click here.

The IRS previously identified certain SCE transactions as listed transactions in Notice 2017-10. These final regulations, consistent with Notice 2017-10, identify certain SCE transactions as listed transactions.

CAUTION - The issuance of these final regulations clarifies that participants and material advisors must report these transactions, including any transactions that were completed in taxable years that are still open.

This listed transaction regulation is part of a multifaceted IRS approach that is succeeding in protecting the integrity of the tax system. On a related front, the IRS has enjoyed significant success in the courts resulting in a number of syndicated partnerships having their grossly inflated easement valuations reduced for tax purposes to what the actual market value was at the time of the donation, with the partners claiming the inflated deduction often incurring substantial penalties.

Chevron Case Overturned (Loper Bright Enterprises)

Chevron Deference Background

Chevron deference is a legal principle that originated from the 1984 Supreme Court case Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc. Under this doctrine, courts defer to a federal agency's interpretation of a law that it administers when the law is ambiguous, as long as the agency's interpretation is reasonable. The principle operates in two steps:

1. **Step One:** The court determines whether the statute is clear regarding the specific issue at hand. If the statute is clear, the court must follow that clear intent of Congress.
2. **Step Two:** If the statute is ambiguous or silent on the issue, the court does not impose its own interpretation but instead defers to the agency's interpretation, as long as it is reasonable.

NOTE - The rationale behind Chevron deference was that agencies, as experts in their respective fields, are better equipped to interpret and implement the complex and technical statutes they are charged with enforcing. This deference has allowed agencies significant flexibility in interpreting laws, which has played a key role in shaping federal regulations and policy.

Loper Bright Enterprises v. Raimondo (SC - 06-28-24 decision)

Background

- This case arose from the fishing industry's (i.e, Loper Bright Enterprises (petitioner)) challenge to a rule imposed by the National Marine Fisheries Service (NMFS), a federal agency under the Department of Commerce that manages and conserves marine fisheries in U.S. waters.
- The rule in question required certain fishing vessels to pay for government-mandated at-sea monitors.
- These monitors were placed on vessels to ensure compliance with various regulations, including those related to catch limits and bycatch reduction.

Legal Issue

- The key legal issue was whether the NMFS had the authority under the Magnuson-Stevens Fishery Conservation and Management Act to require fishing vessels to cover the costs of these at-sea monitors.
- The petitioners argued that the Act did not explicitly grant the agency this power and that such an imposition was unlawful.
- The petitioners further contended that the lower courts had improperly applied Chevron deference to uphold the NMFS's interpretation of the statute.
- They argued that the courts should not have deferred to the agency's interpretation, as it resulted in an undue financial burden on the fishing companies without clear congressional authorization.

Chevron Deference Challenge

- The lower court upheld the NMFS regulation, applying Chevron deference to interpret the statute.
- The petitioners asked the Supreme Court to reconsider or overturn the Chevron deference doctrine, which had been applied by lower courts to uphold the NMFS's authority.
- They argued that the judiciary should have the final say in interpreting ambiguous statutes, rather than deferring to the agency's interpretation.

Supreme Court Ruling - Loper Bright Enterprises v. Raimondo

- The Court, in a 6-3 decision (on 06-28-2024) authored by Chief Justice Roberts, emphasized that courts must exercise their independent judgment when determining whether an agency has acted within its statutory authority.
- The majority opinion underscored that it is the role of the judiciary, not administrative agencies, to interpret the law.
- This stance directly counters the Chevron doctrine, which allowed courts to defer to agencies' reasonable interpretations of ambiguous statutes.

NOTE - The decision restores and reinforces the judiciary's role as the primary interpreter of laws, asserting that courts must independently determine the best reading of a statute, regardless of the agency's expertise or policy preferences. This marks a significant limitation on the power and flexibility of administrative agencies in shaping the interpretation of federal statutes.

Incompatibility with the APA

- The Court's reasoning leaned heavily on the Administrative Procedure Act (APA), which mandates that "the reviewing court" must "decide all relevant questions of law" and "interpret statutory provisions."
- The Court found that this directive from the APA could not be reconciled with Chevron's requirement for courts to accept any "permissible" agency construction of an ambiguous statute. The Court argued that even when a statute is ambiguous, there is still a "best reading," which the court is obliged to identify and adopt.

Rejection of Agency Expertise as Determinative

- One of the core arguments in Chevron was that agencies possess the expertise necessary to interpret complex and technical statutes. However, the Court in Loper Bright rejected the notion that statutory ambiguities should be resolved by agencies based on their expertise or policy decisions.
- Instead, the Court argued that statutory interpretation is a "textual art" in which courts have "special competence." The decision reinforces that it is the judiciary's duty to determine the best reading of a statute, even in areas involving technical matters, based on legal principles and interpretive tools.

Historical and Constitutional Foundation

- The Court referenced Marbury v. Madison to bolster its rationale, quoting Chief Justice Marshall's declaration that "It is emphatically the province and duty of the judicial department to say what the law is."
- The majority opinion suggested that the framers of the Constitution anticipated that courts would often encounter statutory ambiguities and expected that courts, not agencies, would resolve them by exercising independent legal judgment.

Impact on Judicial Review

- The Court concluded that the APA's provisions for reviewing agency actions effectively codify the principle, dating back to Marbury v. Madison, that courts are responsible for deciding legal questions by applying their own judgment.
- This decision reinforces the idea that courts should not abdicate their responsibility to interpret the law, even in the face of statutory ambiguities involving administrative agencies.

Regulations Post Loper Bright Enterprises

NOTE – Click here to see a summary of understanding all IRS guidance.

Final Regulations

- Legally binding and have full force of law.
- Published in the Federal Register and eventually in the Code of Federal Regulations (CFR).
- Can be relied on indefinitely, unless amended or repealed.
- These are the IRS's official interpretation of the tax law.

NOTE - You can rely on final regulations when preparing returns or advising clients.

Proposed Regulations

- Issued for public comment before becoming final.
- Not binding on taxpayers or the IRS, unless the IRS says you can rely on them.
- Often contain a statement like: "Taxpayers may rely on these proposed regulations until final regulations are issued."

NOTE - You can rely on proposed regulations only if the IRS explicitly allows it in the preamble.

Temporary Regulations

- Issued to provide immediate guidance (often after a new law is passed).
- Have the same authority as final regulations while they're in effect.
- Valid for a maximum of 3 years from the date of issuance (under current law).
- Usually accompanied by proposed regulations, which will eventually become final.

NOTE - You can rely on temporary regs just like final regulations until they expire or are replaced.

Type of Regulation	Binding on Taxpayers?	Can You Rely on It?	Court Deference (Post-*Loper Bright*)	Notes
Final Regulations	☑ Yes	☑ Yes	⚖ Court will interpret statute **independently -** no automatic deference	Strongest form of IRS guidance, but more vulnerable to legal challenge
Temporary Regulations	☑ Yes	☑ Yes	⚖ Same as final - court decides if it matches the law	Valid for up to 3 years; often replaced by final regs
Proposed Regulations	✕ Not binding	⚠ Only if IRS says so	✕ No deference at all	Courts don't treat proposed regs as authoritative; IRS must state if you may rely on them
Interpretive (vs. Legislative)	? Depends on court	⚠ Usually, but not guaranteed	⚠ No special weight given anymore	Courts will scrutinize more than before

Rules & Regulations (§7805)

Authorization (§7805(a))

Except where such authority is expressly given by this title to any person other than an officer or employee of the Treasury Department, the Secretary shall prescribe all needful rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.

- §7805(a) is the foundation for most IRS regulations and guidance.
- It is not a grant of unlimited power - rules must still align with the statute and follow the Administrative Procedure Act (APA).
- Courts give less deference to rules issued under this general authority than those issued under specific Congressional direction (called "legislative regulations").

Two Types of IRS Regulations (Post-Loper Bright)

Legislative (Authorized) Regulations

- Issued under a direct grant of authority from the Internal Revenue Code.
- Example: IRC says, "The Secretary shall prescribe regulations to implement this section."
- These are meant to fill in the details of a statute.

NOTE – These still carry the most legal weight, but the Courts now review them independently—they don't defer to the IRS just because the regulation is reasonable. The IRS must now show that the regulation is the best interpretation, not just "a reasonable one."

Interpretive Regulations

- Issued where the Code is silent or ambiguous, and the IRS is interpreting the law on its own.
- The IRS isn't specifically told to issue these regulations, they're based on general authority (e.g., under IRC §7805(a)).

NOTE - Now carry less persuasive authority than before. Courts no longer give them automatic deference and may reject them more often. Especially vulnerable when the interpretation adds burdens, narrows taxpayer rights, or conflicts with plain language of the statute.

Type	Based On	Pre-2024 Deference	Post-2024 Deference	Still Reliable for Taxpayers?
Legislative Regs	Specific IRC authority to issue regs	✅ Strong (Chevron)	⚠️ No deference; court decides	✅ Yes (unless overruled by court)
Interpretive Regs	General authority (e.g., IRC § 7805(a))	⚠️ Some deference	❌ No deference	⚠️ Use with caution

Federal Tax Update – Business Current Developments

Table of Contents

C Corp. Income Taxes & General Business Credits **4**
Regular Income Tax Rates (§11) 4
Corporate Alternative Minimum Tax 5
Accumulated Earnings Tax 6
Personal Holding Company (PHC) Tax 7
Dividends-Received Deduction (DRD) 8
Charitable Contributions (§170) 8
General Business Credit (Form 3800) 10

General Business Provisions **12**
Net Operating Losses (NOL) (§172) 12
Limitation on Excess Business Losses of Non-Corporate Taxpayers (§461(l)) 14
Qualified Business Income Deduction (§199A) 16
QBI Previously Disallowed Losses (§1.199A-3(b)(1)(iv)) 27
QBI Loss Tracking Worksheet (Form 8995-A Instructions) 29
Limitation on Business Interest (§163(j)) 30
Meals Provided at Convenience of Employer 36
Business Entertainment & Meal Expenses 37
Qualified Transportation Fringe 41
Qualified Moving Expense Reimbursement Repealed (§132(g)) 42
Research & Experimental Expenditures 43
Employee or Independent Contractor – Voluntary Classification Settlement Program 45
DOL Issues Final Rule On Worker Classification Under the FLSA 48
Accountable Reimbursement Plans - Overview 49
Below-Market Loans - Overview (§7872) 52
Employee Retention Credit Updates 54
Returns For > $10,000 Cash Received in Trade or Business 55
Information Reporting of Certain Payments (§6041 & §6041A) 56
Information Reporting on Payment Card & Third Party Payment Transactions 58
Installment Payment of Tax on Gain from Sale of Qualified Farmland to Qualified Farmers (§1062) 60
Modifications Related to Foreign Tax Credit Limitation 61

S Corporation & Partnership Provisions **63**
S Corporation Reasonable Compensation Issues 63
Relief for S Corporation & QSub Elections Without 65
S Corporation Shareholders Stock & Debt Basis 67
S Corporation & Partnership Fringe Benefits Issues 69
Schedules K-2 & K-3 - Reporting of International Tax Matters by Pass-Through Entities 73
Overview of Adjustments to Partner's Outside Basis (§705(a)) 74
§754 Election & Revocation 76
Form 8308 - Report of a Sale or Exchange of Certain Partnership Interests 77
IRS Releases New Form 7217 - Partners Report of Property Distributed by a Partnership 78
Partnership Self-Employment Tax Issues 80
Overview of Various Partnership Regulations Issued 83
Business Entity Classification Issues 84
Pass Through Entity (PTE) Income Tax Payments 85

Depreciation **87**
Real Property Depreciation 87
§179 Expense Limitations & Modifications 89
Additional First Year Depreciation (AFYD) 91
Qualifying Property Acquired After to 09-27-17 (§168(k)(2)) 93
Special Depreciation for Allowance for Qualified Production Property (§168(n)) 94
Farm Depreciation Provisions 98

Accounting Method Changes **99**
Cash Method 99
Accounting for Inventories (§471) 101
Uniform Capitalization (§263A) 102
Accounting for Long-Term Contracts 103
Taxable Year of Inclusion Modified (§451) 104
Updated List for Automatic Change in Accounting Methods 106

Miscellaneous Topics **107**
Charitable Conservation Easement & Listed Transactions 107
Chevron Case Overturned (Loper Bright Enterprises) 109
Regulations Post Loper Bright Enterprises 111

C Corp. Income Taxes & General Business Credits

Regular Income Tax Rates (§11)

Corporate Tax Rates After 2017 – Flat 21%

The corporate tax rate is reduced to a flat 21% rate for taxable years beginning after December 31, 2017. This includes personal service corporations (PSCs).

NOTE – The 35% maximum corporate tax rate on net capital gains under §1201 was also repealed because it is obsolete.

Corporate Tax Rates Prior to 2018

The amount of the tax imposed shall be the sum of:

1. 15% of so much of the taxable income as does not exceed $50,000,
2. 25% of so much of the taxable income as exceeds $50,000 but does not exceed $75,000,
3. 34% of so much of the taxable income as exceeds $75,000 but does not exceed $10,000,000, and
4. 35% of so much of the taxable income as exceeds $10,000,000.

Surtax

In the case of a corporation which has taxable income in excess of $100,000 for any taxable year, the amount of tax determined under the preceding sentence for such taxable year shall be increased by the lesser of:

1. 5% of such excess, or
2. $11,750 (i.e., on taxable income between $100,000 and $335,000).

In the case of a corporation which has taxable income in excess of $15,000,000, the amount of the tax determined under the foregoing provisions of this paragraph shall be increased by an additional amount equal to the lesser of :

1. 3% of such excess, or
2. $100,000 (i.e., on taxable income between $15,000,000 and $18,333,333)

Summary of the Tax Rates – Prior to 2018

IF TAXABLE INCOME IS:			
Over –	**But not over –**	**Tax is:**	**Of the amount over –**
$0	$50,000	15%	$0
$50,000	$75,000	$7,500 + 25%	$50,000
$75,000	$100,000	$13,750 + 34%	$75,000
$100,000	$335,000	$22,250 + 39%	$100,000
$335,000	$10,000,000	$113,900 + 34%	$335,000
$10,000,000	$15,000,000	$3,400,000 + 35%	$10,000,000
$15,000,000	$18,333,333	$5,150,000 + 38%	$15,000,000
$18,333,333	N/A	35%	$18,333,333
CAUTION – A qualified personal service corporation (PSC) is taxed at a flat rate of 35% on taxable income.			

Corporate Alternative Minimum Tax

NOTE - The TCJA repealed the corporate alternative minimum tax (AMT) for taxable years beginning after December 31, 2017. The Inflation Reduction Act reinstated the corporate AMT (i.e., modified §55(b) and added §56A for taxable years beginning after December 31, 2022.

Corporate AMT (§55)

This provision creates a new alternative minimum tax of 15% on corporations based on financial income. It would apply to corporations with $1 billion or more in average annual earnings in the previous three years. In the case of U.S. corporations that have foreign parents, it would apply only to income earned in the United States of $100 million or more of average annual earnings in the previous three years (and apply when the international financial reporting group has income of $1 billion or more). It would apply to a new corporation in existence for less than three years based on the earnings in the years of existence.

AMT calculation & credit

The additional tax equals the amount of the minimum tax in excess of the regular income tax plus the additional tax from the Base Erosion and Anti-Abuse tax. Income would be increased by federal and foreign income taxes to place income on a pretax basis. Losses would be allowed in the same manner as with the regular tax, with loss carryovers limited to 80% of taxable income. Domestic credits under the general business tax (such as the R&D credit) would be allowed to offset up to 75% of the combined regular and minimum tax. Foreign tax credits would be allowed based on the allowance for foreign taxes paid in a corporation's financial statement.

NOTE - A credit for additional minimum tax could be carried over to future years to offset regular tax when that tax is higher.

Exceptions from the AMT

The provision excludes Subchapter S corporations, regulated investment companies (RICs), and real estate investment trusts (REITs). The tax applies to large private equity firms organized as partnerships, but excludes portfolio companies owned by these firms (due to a modification made by Section 13904 of the bill).

Consolidated returns

Firms that file consolidated returns would include income allocable to the firm from related firms including controlled foreign corporations (and any disregarded entities); for other related firms, dividends would be included.

Adjusted Financial Statement Income (§56A)

The term "adjusted financial statement income" means, with respect to any corporation for any taxable year, the net income or loss of the taxpayer set forth on the taxpayer's applicable financial statement for such taxable year, adjusted as provided in this section.

Adjustments

The provision allows special deductions for cooperatives and Alaska Native Corporations. It would make adjustments to conform financial accounting to tax accounting for certain defined benefit pension plans. The AMT would apply with respect to items under the unrelated business income tax for tax-exempt entities. Financial income would be adjusted to allow depreciation deductions based on tax rules. It would also be adjusted to allow recovery of wireless spectrum rights as allowed under tax rules (recovered over 15 years).

Accumulated Earnings Tax

Background of the AET (§531-537)

The IRS can impose a tax on a C corporation that avoids the double taxation by not distributing its earnings and profits to the shareholders (taxed as a dividend). However, a corporation can accumulate its earnings for a possible expansion or other bona fide business reasons. If a corporation allows earnings to accumulate beyond the reasonable needs of the business, it may be subject to an accumulated earnings tax of 20%.

NOTE – The AET rate is equivalent to the highest individual dividend rate. Prior to 2013 the rate was 15%.

If the accumulated earnings tax applies, interest applies to the tax from the date the corporate return was originally due, without extensions.

NOTE – This tax is not self-assessed and can only be imposed by the IRS upon an audit.

$250,000 Limit

To determine if the corporation is subject to this tax, first treat an accumulation of $250,000 or less generally as within the reasonable needs of most businesses.

$150,000 Limit if PSC

Treat an accumulation of $150,000 or less as within the reasonable needs of a business whose principal function is performing services in the fields of accounting, actuarial science, architecture, consulting, engineering, health (including veterinary services), law, and the performing arts.

Personal Holding Company (PHC) Tax

Purpose of the PHC Tax

A corporation that satisfies both the stock ownership test and a passive income test is classified as a personal holding company (PHC) for the tax year. Congress enacted the PHC penalty tax to prevent taxpayer's from using the closely held corporations to shelter passive income from the higher individual tax rates. The tax rate applicable to undistributed personal holding company income is 20%.

NOTE 1 – The PHC rate is equivalent to the highest individual dividend rate. Prior to 2013 the rate was 15%.

NOTE 2 – The PHC tax is self-assessed corporate tax at a tax rate equivalent to the highest individual dividend rate.

Compliance & Tax Reporting

Corporations use Schedule PH to figure the personal holding company (PHC) tax. Schedule PH must be attached to Form 1120. Schedule PH incorporates the steps necessary to determine whether a corporation is a PHC.

COMPLIANCE TIP – The IRS CANNOT assess both the PHC tax and the accumulated earnings tax. The PHC tax takes precedence.

Personal Holding Company Defined §542(a))

The term "personal holding company" means any corporation (other than a corporation exempt from the PHC rules) if:

1. At least 60% of its adjusted ordinary gross income for the taxable year is personal holding company income (i.e., **Adjusted Ordinary Gross Income Requirement**), AND
2. At any time during the last half of the taxable year more than 50% in value of its outstanding stock is owned, directly or indirectly, by or for not more than 5 individuals (i.e., **Stock Ownership Requirement**).

PHC Income Defined (§543(a))

In general, PHC income includes:

1. interest,
2. dividends,
3. copyright royalties,
4. produced film rent, AND
5. personal service contracts.

CAUTION – Rents and mineral, gas and oil royalties are PHC income if certain tests are met.

Dividends-Received Deduction (DRD)

A corporation can deduct a percentage of certain dividends received during its tax year. The dividends-received deduction (i.e., DRD) depends on the stock ownership percentage in the company that paid the dividend.

NOTE – Determine ownership, for these rules, by the amount of voting power and value of the paying corporation's stock (other than certain preferred stock) the receiving corporation owns.

Dividends from Domestic Corporations (§243)

50% DRD - Less than 20% Ownership

For taxable years beginning after December 31, 2017 a corporation can deduct (within certain limits) 50% of the dividends received if the corporation receiving the dividend owns less than 20% of the corporation distributing the dividend.

NOTE – The DRD was 70% for taxable years beginning before January 1, 2018.

65% DRD - 20% or more AND less than 80% Ownership

For taxable years beginning after December 31, 2017, a corporation that owns 20% or more of the distributing corporation's stock, can deduct (within certain limits) 65% of the dividends received.

NOTE – The DRD was 80% for taxable years beginning before January 1, 2018.

100% DRD – Affiliated Groups

Members of affiliated groups can deduct 100% of the dividends received if at the close of the day on which such dividend is received, such corporation is a member of the same affiliated group as the corporation distributing such dividend.

100% DRD – Small Business Investment Companies (§243(a)(2) & §1.243-1(a)(2)(ii))

Small business investment companies can deduct 100% of the dividends received from taxable domestic corporations. However, to claim the deduction provided by §243(a)(2) the company must file with its return a statement that it was a Federal licensee under the Small Business Investment Act of 1958 at the time of the receipt of the dividends.

Charitable Contributions (§170)

A corporation can claim a limited deduction for charitable contributions made in cash or other property, if made to, or for the use of, a qualified organization. No deduction is allowed if the net earnings of the recipient organization benefit any private shareholder or individual.

NOTE - For more information on qualified organizations, see IRS Pub. 526, Charitable Contributions.

Timing of Deduction

Cash Method Corporation

A corporation using the cash method of accounting deducts contributions in the tax year paid.

Accrual Method Corporation

A corporation using an accrual method of accounting can choose to deduct unpaid contributions for the tax year the board of directors authorizes them if it pays them within 2½ months after the close of that tax year. Make the choice by reporting the contribution on the corporation's return for the tax year. A declaration stating that the board of directors adopted the resolution during the tax year must accompany the return. The declaration must include the date the resolution was adopted.

Deduction Limits Pre-2026

A corporation cannot deduct charitable contributions that exceed 10% of taxable income (computed without: the charitable deduction itself, the dividends-received deduction, NOL carrybacks, or capital loss carrybacks). Excess contributions may be carried forward for 5 years (FIFO ordering).

EXAMPLE (Pre-2026 Rules) - Goodheart, Inc. donates $8,000 to the Red Cross and has taxable income of $35,000 (before DRD and charitable deduction). The charitable deduction is limited to $3,500 (10% limit). The excess $4,500 will carry forward up to 5 years.

UPDATE – Deduction Limit Post-2025 (OBBB)

A corporation's charitable contribution deduction (other than contributions covered by §170(b)(2)(B) (i.e., qualified conservation contributions) or (C) (i.e., qualified disaster relief contributions) is allowed only to the extent that the total contributions for the taxable year:

1. Exceed 1% of the corporation's taxable income, and
2. Do not exceed 10% of the corporation's taxable income.

Carryforward

If a corporation makes charitable contributions that are disallowed because of the 10% limitation, the excess contributions are carried forward to the next year. But in the next year, when applying the charitable deduction limit, you must first apply current-year contributions, then apply any carryforwards from prior years. Excess contributions may be carried forward for 5 years (FIFO ordering).

EXAMPLE (Post-2025 Rules) - Goodheart, Inc. donates $118,000 to the Red Cross and has taxable income of $1,000,000 (before the DRD and charitable deduction). Under the charitable contribution limits, the first $10,000 (equal to 1% of taxable income) is permanently disallowed and cannot be carried forward. The remaining $108,000 is subject to the 10% cap, which limits the current deduction to $100,000. The $8,000 excess above the cap may be carried forward for up to 5 years.

Coordination rule

Carryforwards cannot create or increase an NOL carryover.

Corporate Charitable Contribution Rules		
Rule	**Pre-2026**	**Post-2025**
Deduction Limit	10% of taxable income (before DRD, NOL, and charitable deduction).	Same 10% of taxable income (before DRD, NOL, and charitable deduction).
Floor	*None* — all contributions potentially deductible.	**1% of taxable income floor** — first 1% is permanently disallowed.
Carryforward	Excess contributions above 10% cap carried forward **5 years** (FIFO).	Excess contributions above 10% cap carried forward **5 years** (FIFO).
What Cannot Be Carried Forward	Nothing initially (only amounts that expire after 5 years).	Contributions under the **1% floor** (permanently lost) + any amounts that expire after 5 years.

General Business Credit (Form 3800)

General Business Credit (§38)

A credit is allowed against income tax for a particular tax year equal to the sum of:

1. the business credit carryforwards carried to the tax year,
2. the current year business credit, and
3. the business credit carrybacks carried to the tax year.

NOTE – The credit is reported on the *Form 3800 – General Business Credit*.

Credit Limitation

The credit allowed for any tax year (except for the empowerment zone employment credit, the New York Liberty Zone business employee credit, and other specified credits) is limited to the excess of taxpayer's net income tax over the **greater of:**

1. the tentative minimum tax for the tax year, or
2. 25% of the amount of the taxpayer's net regular tax that exceeds $25,000.

NOTE – Excess credits can be carried back 1 year and forward 20 years.

Credit ordering rules

General business credits reported on Form 3800 are treated as used on a first-in, first-out basis by offsetting the earliest-earned credits first. Therefore, the order in which the credits are used in any tax year is:

1. Carryforwards to that year, the earliest ones first;
2. The general business credit earned in that year; and
3. The carryback to that year.

When relevant, the components of the general business credit reported on Form 3800 arising in a single tax year are used in the following order.

- Investment credit (in the following order—rehabilitation credit, energy credit, qualifying advanced coal project credit, qualifying gasification project credit, qualifying advanced energy project credit, qualifying therapeutic discovery project credit (carryforward only), and advanced manufacturing investment credit.) (Form 3468, Parts II, III, IV, VI, and VII).
- Work opportunity credit (Form 5884).
- Biofuel producer credit (Form 6478).
- Credit for increasing research activities (Form 6765).
- Low-income housing credit (Form 8586).
- Enhanced oil recovery credit (Form 8830).
- Disabled access credit (Form 8826).
- Renewable electricity production credit (Form 8835).
- Empowerment zone employment credit (Form 8844).
- Renewal community employment credit (carryforward only).
- Indian employment credit (carryfoward only).
- Employer social security and Medicare taxes paid on certain employee tips (Form 8846).
- Orphan drug credit (Form 8820).
- New markets credit (Form 8874).
- Credit for small employer pension plan startup costs (Form 8881, Part I).
- Credit for employer-provided childcare facilities and services (Form 8882).
- Qualified railroad track maintenance credit (Form 8900).

- Biodiesel, renewable diesel (Form 8864).
- Low sulfur diesel fuel production credit (Form 8896).
- Credit for oil and gas production from marginal wells (Form 8904).
- Distilled spirits credit (Form 8906).
- Advanced nuclear power facility production (Form 7213, Part I).
- Nonconventional source fuel credit (carryforward only).
- Energy efficient home credit (Form 8908).
- Energy efficient appliance credit (carryforward only).
- Alternative motor vehicle credit (Form 8910, Part II).
- Alternative fuel vehicle refueling property credit (Form 8911, Part II).
- Mine rescue team training credit (carryforward only).
- Agricultural chemicals security credit (carryforward only).
- Credit for employer differential wage payments (Form 8932).
- Carbon oxide sequestration credit (Form 8933).
- Qualified plug-in electric vehicle credit (carryforward only).
- New clean vehicle credit (Form 8936, Part II).
- Credit for small employer health insurance premiums (Form 8941).
- Employee retention credit for employers affected by qualified disasters (carryforward only).
- Employer credit for paid family and medical leave (Form 8994).
- Credit for auto-enrollment (Form 8881, Part II).
- Zero-emission nuclear power production (Form 7213, Part II).
- Sustainable aviation fuel (Form 8864, line 8).
- Clean hydrogen production (Form 7210).
- Qualified commercial clean vehicle (Form 8936, Part V).
- Advanced manufacturing production (Form 7207).
- Military spouse retirement plan credit (Form 8881, Part III).
- General credits from an electing large partnership (carryforward only).

NOTE – Although these credits are aggregated on Form 3800, keep a separate record of each credit, including whether the credit was an eligible small business credit, to ensure proper accounting of the credits.

General Business Provisions

Net Operating Losses (NOL) (§172)

NOL Background – Pre-2018

A net operating loss (NOL) generally means the amount by which a taxpayer's business deductions exceed its gross income. In general, an NOL may be carried back 2 years and carried over 20 years to offset taxable income in such years. NOLs offset taxable income in the order of the taxable years to which the NOL may be carried. Different carryback periods apply with respect to NOLs arising in different circumstances. Extended carryback periods are allowed for NOLs attributable to specified liability losses and certain casualty and disaster losses. Limitations are placed on the carryback of excess interest losses attributable to corporate equity reduction transactions.

TCJA NOL Deduction Modifications – Post-2017

EFFECTIVE DATE – For losses arising in taxable years **beginning** after December 31, 2017.

Net Operating Loss (NOL) Deduction Allowed (§172(a))

There shall be allowed as a deduction for the taxable year an amount equal to the lesser of:

1. the aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, or
2. 80% of taxable income computed without regard to the deduction allowable under this section.

NOL Carryback & Carryforward (§172(b)(1)(A))

In general, a NOL for any taxable year:

1. shall not be a net operating loss carryback to any taxable year preceding the taxable year of such loss, and
2. shall be a net operating loss carryover to each taxable year following the taxable year of the loss.

NOTE – See the exception for farming losses and insurance companies.

Special rule for losses arising in 2018, 2019, and 2020 (§172(b)(1)(C))

In the case of any net operating loss arising in a taxable year beginning after December 31, 2017, and before January 1, 2021:

1. such loss shall be a net operating loss carryback to each of the 5 taxable years preceding the taxable year of such loss, and
2. §172(b)(1)(B) (i.e., farming losses) and (§172(b)(1)(C)(i) (i.e., insurance co) shall not apply.

Net Operation Loss Summary Chart			
NOL's Arising In	**Carryback**	**Carryforward**	**Limitations**
Pre-2018	2 years	20 years	100% of taxable income
2018-2020	5 years	Indefinite	100% of taxable income (2018-2020) 80% of taxable income (Post 2020)
Post-2020	None (2-year for farmers)	Indefinite	80% of taxable income

Farming Losses (§172(b)(1)(B))
Any part of an NOL for the tax year which is a farming loss of the taxpayer can be carried back to each of the 2 tax years preceding the tax year of the loss. A "farming loss" is the lesser of:
1. the amount that would be the NOL for the tax year if only income and deductions attributable to farming businesses (as defined in §263A(e)(4)) are taken into account, or
2. the amount of the NOL for the tax year.

Coordination with §172(b)(2)
For purposes of applying §172(b)(2) (i.e., the order in which NOLs are absorbed), a farming loss for any taxable year shall be treated as a separate NOL for such taxable year to be taken into account after the remaining portion of the NOL for such taxable year.

Election to forego farming loss carryback
Any taxpayer entitled to a 2-year carryback from any farming loss year may elect not to have such clause apply to such loss year. Such election shall be made in such manner as prescribed by the Secretary and shall be made by the due date (including extensions of time) for filing the taxpayer's return for the taxable year of the net operating loss.

NOTE – Such election, once made for any taxable year, shall be irrevocable for such taxable year.

Amount of Carrybacks and Carryovers (§172(b)(2))
The entire amount of the net operating loss for any taxable year (hereinafter in this section referred to as the "loss year") shall be carried to the earliest of the taxable years to which such loss may be carried. The portion of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the taxable income for each of the prior taxable years to which such loss may be carried. For purposes of the preceding sentence, the taxable income for any such prior taxable year shall:
1. be computed with the modifications specified in §172(d) other than paragraphs (1), (4), and (5) thereof, and by determining the amount of the NOL deduction without regard to the NOL for the loss year or for any taxable year thereafter,
2. not be considered to be less than zero, and
3. not exceed the amount determined under §172(a)(2) for such prior taxable year (i.e., 80% of taxable income, computed without regard to the NOL deduction).

Election to waive carryback (§172(b)(3))
Any taxpayer entitled to a carryback period under §172(b)(1) may elect to relinquish the entire carryback period with respect to a net operating loss for any taxable year. Such election shall be made in such manner as may be prescribed by the Secretary, and shall be made by the due date (including extensions of time) for filing the taxpayer's return for the taxable year of the net operating loss for which the election is to be in effect. Such election, once made for any taxable year, shall be irrevocable for such taxable year.

Net operating loss defined (§172(c))
For purposes of this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income. Such excess shall be computed with the modifications specified in (§172(d).

Limitation on Excess Business Losses of Non-Corporate Taxpayers (§461(l))

UPDATE – The OBBB permanently extended the limitations under §461(l) and renders §461(j) inapplicable to farm losses.

Reporting

Use the *Form 461 – Limitations on Business Losses* to calculate the excess business loss. Report the §461(l) excess business loss adjustments on the *Form 1040, Schedule 1*, line 21. Enter "ELA" and the taxable amount on the dotted line next to line 21.

Limitation (§461(l)(1))

In the case of taxable year of a taxpayer other than a corporation:

1. for any taxable year beginning after December 31, 2017, §461(j) (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and
2. for any taxable year beginning after December 31, 2020, any excess business loss of the taxpayer for the taxable year shall not be allowed.

Disallowed loss carryover (§461(l)(2))

Any loss which is disallowed shall be treated as a net operating loss for the taxable year for purposes of determining any net operating loss carryover under §172(b) for subsequent taxable years.

Excess business loss (§461(l)(3))

The term "excess business loss" means the excess (if any) of the aggregate deductions of the taxpayer for the taxable year which are attributable to trades or businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under §461(l)(1) and without regard to any deduction allowable under §172 or §199A), over the sum of:

1. the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such trades or businesses, plus
2. $250,000 (200% of such amount in the case of a joint return), adjusted annually for inflation:

	2026	2025	2024
Married filing joint	$512,000	$626,000	$610,000
All other taxpayers	$256,000	$313,000	$305,000

NOTE – Such excess shall be determined without regard to any deductions, gross income, or gains attributable to any trade or business of performing services as an employee.

Treatment of capital losses

Deductions for losses from sales or exchanges of capital assets shall not be taken into account.

Treatment of capital gains

The amount of gains from sales or exchanges of capital assets taken into account under shall not exceed the lesser of:

1. the capital gain net income determined by taking into account only gains and losses attributable to a trade or business, or
2. the capital gain net income.

Application to Partnerships & S corporations (§461(l)(4))

In the case of a partnership or S corporation:

1. this subsection shall be applied at the partner or shareholder level, and
2. each partner's or shareholder's allocable share of the items of income, gain, deduction, or loss of the partnership or S corporation for any taxable year from trades or businesses attributable to the partnership or S corporation shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

NOTE – In the case of an S corporation, an allocable share shall be the shareholder's pro rata share of an item.

Additional reporting (§461(l)(5))

The Secretary shall prescribe such additional reporting requirements as the Secretary determines necessary to carry out the purposes of this subsection.

Coordination with the Passive Activity Loss Rules Under §469 (§461(l)(6))

This subsection shall be applied after the application of §469.

Qualified Business Income Deduction (§199A)

UPDATE – The OBBB permanently extends and modifies QBID after 2025.

Qualified Business Income Deduction (§199A(a))

In the case of a taxpayer other than a corporation, there shall be allowed as a deduction for any taxable year an amount equal to the lesser of:

1. the combined qualified business income amount of the taxpayer, or
2. an amount equal to 20% of the excess (if any) of:
    a. the taxable income of the taxpayer for the taxable year, over
    b. the net capital gain (as defined in §1(h)) of the taxpayer for such taxable year.

NOTE - Taxable income shall be computed without regard to section 68 (i.e., overall limitation on itemized deductions) and without regard to any deduction allowable under this section.

UPDATE – Minimum deduction

After 2025, the OBBB introduces a new, inflation-adjusted, minimum deduction of $400 for taxpayers who have at least $1,000 of QBI from one or more active trades or businesses in which the taxpayer materially participates (under §469(h)).

Reporting

- *Form 8995 - Qualified Business Income Deduction Simplified Computation* – used by taxpayers with TI below the threshold amounts above.
- *Form 8995-A - Qualified Business Income Deduction* - used by taxpayers with TI above the threshold amounts above.

Combined Qualified Business Income Amount (§199A(b))

The term "combined qualified business income amount" means, with respect to any taxable year, an amount equal to:

1. the sum of the amounts determined (next paragraph) for each qualified trade or business carried on by the taxpayer **(i.e., QBI component)**, plus
2. 20% of the aggregate amount of the qualified REIT dividends and qualified publicly traded partnership income of the taxpayer for the taxable year **(i.e., REIT/PTP component).**

Determination of deductible amount for each trade or business (i.e., QBI component)

The amount determined with respect to any qualified trade or business is the lesser of:

1. 20% of the taxpayer's qualified business income with respect to the qualified trade or business, or
2. the greater of:
    a. 50% of the W–2 wages with respect to the qualified trade or business, or
    b. the sum of 25% of the W–2 wages with respect to the qualified trade or business, plus 2.5% of the unadjusted basis immediately after acquisition of all qualified property.

NOTE – The wage/capital limitation (under 2 above) does not apply to any taxpayer whose taxable income for the taxable year does not exceed the threshold amounts below.

Phase-in of W-2/Capital Limitation

The wage/capital limit phases in for taxpayers whose taxable income exceeds the annual threshold amounts (i.e., $157,500 and $315,000 for MFJ – adjusted for inflation after 2018) below. The wage/capital limitation applies fully when taxable income exceeds the threshold amount plus:

- $50,000 ($100,000 in the case of a joint return) for 2018 to 2025
- $75,000 ($150,000 in the case of a joint return) after 2025

Year	T.I. Phase-In Threshold Amounts		
	Married filing joint (MFJ)	Single & HOH	Married filing separate (MFS)
2024	$383,900 - $483,900	$191,950 - $241,950	$191,950 - $241,950
2025	$394,600 - $494,600	$197,300 - $247,300	$197,300 - $247,300
2026	$403,150 - $553,150	$201,750 - $276,750	$201,775 - $276,775

EXAMPLE – For 2026, H and W file a joint return on which they report taxable income of $448,150. W has a qualified trade or business that is not a specified service business, such that 20% percent of the qualified business income with respect to the business is $15,000. W's share of wages paid by the business is $20,000, such that 50% of the W-2 wages with respect to the business is $10,000. The $15,000 amount is reduced by 30% ($448,150 - $403,150/$100,000) of the difference between $15,000 and $10,000, or $1,500. H and W take a deduction for $13,500.

Wages Defined

The term "W-2 wages" means, the total wages subject to wage withholding, elective deferrals, and deferred compensation paid by the qualified trade or business with respect to employment of its employees during the calendar year ending during the taxable year of the taxpayer (i.e., amounts described §6051(a)(3) and (8)). Such term **shall not include any amount:**

1. which is not properly allocable to qualified business income or
2. which is not properly included in a return filed with the Social Security Administration on or before the 60th day after the due date (including extensions) for such return.

Acquisitions, dispositions, and short taxable years

The Secretary shall provide for the application of this subsection in cases of a short taxable year or where the taxpayer acquires, or disposes of, the major portion of a trade or business or the major portion of a separate unit of a trade or business during the taxable year.

Qualified property defined

The term "qualified property" means, with respect to any qualified trade or business for a taxable year, tangible property of a character subject to the allowance for depreciation under §167:

1. which is held by, and available for use in, the qualified trade or business at the close of the taxable year,
2. which is used at any point during the taxable year in the production of qualified business income, and
3. the depreciable period for which has not ended before the close of the taxable year.

Depreciable period defined

The term "depreciable period" means, with respect to qualified property of a taxpayer, the period beginning on the date the property was first placed in service by the taxpayer and ending on the later of:

1. the date that is 10 years after such date, or
2. the last day of the last full year in the applicable recovery period that would apply to the property under §168 (determined without regard to §168(g) (i.e., the alternative depreciation system (ADS)).

EXAMPLE – A taxpayer (who is subject to the limit) does business as a sole proprietorship conducting a widget-making business. The business buys a widget-making machine for $100,000 and places it in service in 2020. The business has no employees in 2020. The limitation in 2020 is the greater of (a) 50% of W-2 wages, or $0, or (b) the sum of 25% of W-2 wages ($0) plus 2.5% of the unadjusted basis of the machine immediately after its acquisition: $100,000 x 2.5% = $2,500. The amount of the limitation on the taxpayer's deduction is $2,500.

Special rule with respect to income received from cooperatives

In the case of any qualified trade or business of a patron of a specified agricultural or horticultural cooperative, the amount determined under §199A(b)(2) with respect to such trade or business shall be reduced by the lesser of:

1. 9% of so much of the qualified business income with respect to such trade or business as is properly allocable to qualified payments received from such cooperative, or
2. 50% of so much of the W-2 wages with respect to such trade or business as are so allocable.

NOTE – Report on *Schedule D (Form 8995-A) - Special Rules for Patrons of Agricultural or Horticultural Cooperatives*.

EXAMPLE 1 - Patron Pat is a grain farmer with taxable income of $75,000 (determined without regard to §199A) and has a filing status of married filing jointly. Patron Pat is a member of MAGA Cooperative. During the year, Pat receives $250,000 from MAGA for his grain sales of which $230,000 is per-unit retain allocations (PURPIM) and $20,000 in patronage dividends. Pat has $200,000 of expenses that includes $40,000 of W-2 wages. Pat has $50,000 of qualified business income (QBI). Because Pat's taxable income is below the MFJ threshold of $315,000, his QBI deduction is not limited by the wages/capital limitation. Thus, his tentative QBI deduction is $10,000 (i.e., $50,000 x 20%).

Because all of Pat's tentative QBI deduction is attributable to qualified payments he received from MAGA Coop, he has to determine what portion (if any) of that deduction must be reduced under §199A(b)(7). His QBI deduction must be reduced by the lesser of (1) 9% of QBI allocable to qualified payments from cooperative (i.e., $50,000 x 9% = $4,500) or (2) 50% of W-2 wages attributable to Pat's coop payments (i.e., $40,000 x 50% = $20,000). As a result, Pat's QBI deduction is $5,500 (i.e., $10,000 less $4,500).

EXAMPLE 2 – Same facts as in example 1 except that Pat did not have any wage expense. Pat's QBI deduction must be reduced by the lesser of (1) 9% of QBI allocable to qualified payments from cooperative (i.e., $50,000 x 9% = $4,500) or (2) 50% of W-2 wages attributable to Pat's coop payments (i.e., $0 x 50% = $0). Because Pat paid no wages for his grain business, he is not required to reduce his QBI deduction at all. He is therefore entitled to the full QBI deduction of $10,000.

Qualified business income (§199A(c))

The term "qualified business income" means, for any taxable year, the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer.

NOTE – Such term shall not include any qualified REIT dividends or qualified publicly traded partnership income.

Carryover of losses

If the net amount of qualified income, gain, deduction, and loss with respect to qualified trades or businesses of the taxpayer for any taxable year is less than zero, such amount shall be treated as a loss from a qualified trade or business in the succeeding taxable year.

NOTE – Report losses and carryovers of *Schedule C (Form 8995-A) - Loss Netting and Carryforward*.

EXAMPLE – Taxpayer has qualified business income (QBI) of $20,000 from qualified business A and a qualified business loss of $50,000 from qualified business B in Year 1. Taxpayer is not permitted a deduction for Year 1 and has a carryover qualified business loss of $30,000 to Year 2. The $30,000 negative total QBI amount is treated as negative QBI from a separate trade or business in the succeeding taxable years of the individual for purposes of §199A. In Year 2, Taxpayer has QBI of $20,000 from qualified business A and QBI of $40,000 from qualified business B. The $30,000 carryforward loss must get allocated pro-rata to any business with a net positive QBI. Thus, business A will get allocated $10,000 of the loss and business B $20,000.

Qualified items of income, gain, deduction, and loss

The term "qualified items of income, gain, deduction, and loss" means items of income, gain, deduction, and loss to the extent such items are:

1. effectively connected with the conduct of a trade or business within the United States (within the meaning of §864(c), determined by substituting "qualified trade or business (within the meaning of §199A)" for "nonresident alien individual or a foreign corporation" or for "a foreign corporation" each place it appears), and
2. included or allowed in determining taxable income for the taxable year.

Exceptions

The following investment items shall not be taken into account as a qualified item of income, gain, deduction, or loss:

1. Any item of short-term capital gain, short-term capital loss, long-term capital gain, or long-term capital loss.
2. Any dividend, income equivalent to a dividend, or payment in lieu of dividends described in §954(c)(1)(G).
3. Any interest income other than interest income which is properly allocable to a trade or business.
4. Any item of gain or loss described in subparagraph (C) or (D) of §954(c)(1) (applied by substituting "qualified trade or business" for "controlled foreign corporation").
5. Any item of income, gain, deduction, or loss taken into account under §954(c)(1)(F) (determined without regard to clause (ii) thereof and other than items attributable to notional principal contracts entered into in transactions qualifying under §1221(a)(7)).
6. Any amount received from an annuity which is not received in connection with the trade or business.
7. Any item of deduction or loss properly allocable to an amount described in any of the preceding clauses.

Treatment of reasonable compensation and guaranteed payments

Qualified business income shall not include:

1. reasonable compensation paid to the taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business,
2. any guaranteed payment described in §707(c) paid to a partner for services rendered with respect to the trade or business, and
3. to the extent provided in regulations, any payment described in §707(a) (i.e., partner not acting in capacity as partner) to a partner for services rendered with respect to the trade or business.

Trade or Business Defined (§1.199A-1(b)(14))

Trade or business means a trade or business that is a trade or business under §162 (a §162 trade or business) other than the trade or business of performing services as an employee. In addition, rental or licensing of tangible or intangible property (rental activity) that does not rise to the level of a §162 trade or business is nevertheless treated as a trade or business for purposes of §199A, if the property is rented or licensed to a trade or business conducted by the individual or an RPE which is commonly controlled under §1.199A-4(b)(1)(i) (regardless of whether the rental activity and the trade or business are otherwise eligible to be aggregated under §1.199A-4(b)(1)).

Qualified trade or business (§199A(d))

The term "qualified trade or business" means any trade or business other than:

1. a specified service trade or business, or
2. the trade or business of performing services as an employee.

Specified service trade or business

The term "specified service trade or business" means any trade or business—

1. which is described in §1202(e)(3)(A) (applied without regard to the words "engineering, architecture,") or which would be so described if the term "employees or owners" were substituted for "employees" therein,

> **NOTE –** §1202(e)(3)(A) as modified will read: the term "qualified trade or business" means any trade or business other than any trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of 1 or more of its employees *or owners*.

or

2. which involves the performance of services that consist of investing and investment management, trading, or dealing in securities (as defined in §475(c)(2)), partnership interests, or commodities (as defined in §475(e)(2)).

Exception for specified service businesses based on taxpayer's income

If, for any taxable year, the taxable income of any taxpayer is less than the sum of the threshold amount plus $50,000 ($100,000 in the case of a joint return) for 2018 to 2025 and $75,000 ($150,000 in the case of a joint return) after 2025, then:

1. any specified service trade or business of the taxpayer shall not fail to be treated as a qualified trade or business due to definition of a qualified trade or business, but
2. only the applicable percentage of qualified items of income, gain, deduction, or loss, and the W-2 wages and the unadjusted basis immediately after acquisition of qualified property, of the taxpayer allocable to such specified service trade or business shall be taken into account

in computing the qualified business income, W-2 wages, and the unadjusted basis immediately after acquisition of qualified property of the taxpayer for the taxable year for purposes of applying this section.

Applicable percentage

The term "applicable percentage" means, with respect to any taxable year, 100% reduced (not below zero) by the percentage equal to the ratio of the taxable income of the taxpayer for the taxable year in excess of the threshold amounts (i.e., $157,500 and $315,000 for MFJ – adjusted for inflation after 2018) below, bears to:

- $50,000 ($100,000 in the case of a joint return) for 2018 to 2025
- $75,000 ($150,000 in the case of a joint return) after 2025

NOTE- SSTB income gets phase-out over the same range the wage/capital limitation gets phased in.

Year	SSTB T.I. Phase-Out Threshold Amounts		
	Married filing joint (MFJ)	Single & HOH	Married filing separate (MFS)
2024	$383,900 - $483,900	$191,950 - $241,950	$191,950 - $241,950
2025	$394,600 - $494,600	$197,300 - $247,300	$197,300 - $247,300
2026	$403,150 - $553,150	$201,750 - $276,750	$201,775 - $276,775

NOTE – Use the *Schedule A (Form 8995-A) - Specified Service Trades or Businesses* if the taxable income is in between the annual threshold amounts.

EXAMPLE – For 2026, a married taxpayer has taxable income of $493,150, of which $200,000 is attributable to an accounting sole proprietorship after paying wages of $100,000 to employees. Taxpayer has an applicable percentage of 40% (1 – ($493,150 - $403,150/$150,000)). In determining includible qualified business income, Taxpayer takes into account 40% of $200,000, or $80,000. In determining the includible W-2 wages, Taxpayer takes into account 40% of $100,000, or $40,000. Taxpayer calculates the deduction by taking the lesser of 20% of $80,000 ($16,000) or 50% of $40,000 ($20,000). Taxpayer takes a deduction for $16,000.

Other definitions (§199A(e))

Taxable income

Taxable income shall be computed without regard to section 68 (i.e., overall limitation on itemized deductions) and without regard to any deduction allowable under this section.

Qualified REIT dividend

The term "qualified REIT dividend" means any dividend from a real estate investment trust received during the taxable year which:

1. is not a capital gain dividend, as defined in §857(b)(3) and
2. is not qualified dividend income, as defined in §1(h)(11).

Qualified publicly traded partnership income

The term "qualified publicly traded partnership income" means, with respect to any qualified trade or business of a taxpayer, the sum of:

1. the net amount of such taxpayer's allocable share of each qualified item of income, gain, deduction, and loss (as defined in §199A(c)(3) and determined after the application of §199A(c)(4)) (i.e., wages) from a publicly traded partnership (as defined in §7704(a)) which is not treated as a corporation under §7704(c), **plus**

2. any gain recognized by such taxpayer upon disposition of its interest in such partnership to the extent such gain is treated as an amount realized from the sale or exchange of property other than a capital asset under §751(a).

Final Regulations Issued (TD 9847)

Final regulations were issued on February 1, 2019:

- §1.199A-1 – Operational rules
- §1.199A-2 – Determination of W-2 wages & unadjusted basis immediately after acquisition (UBIA) of qualified property
- §1.199A-3 – Qualified business income, qualified REIT dividends, and qualified PTP
- §1.199A-4 – Aggregation
- §1.199A-5 – Specified service trades or businesses and the trade or business of performing services as an employee
- §1.199A-6 – Relevant passthrough entities (RPEs), publicly traded partnerships (PTPs), trusts & estates

NOTE - On June 25, 2020, amendments were made §1.199A-3 and §1.199A-6. The amendments to §1.199A-3(b)(1)(iv) provide additional rules and clarification on the treatment of suspended losses. §1.199A-3(d) provides guidance that allows a shareholder in a regulated investment company (RIC) within the meaning of §851(a) to take a §199A deduction with respect to certain income of, or distributions from, the RIC. The amendments to §1.199A-6(d) include additional rules related to trusts and estates under §633.

Final Regulations Issued (TD 9947)

On January 14, 2021, the IRS issued final regulations with respect to the application of §199A to cooperatives and their patrons.

- §1.199A-7 - Rules for Cooperatives and their Patrons.
- §1.199A-8 - Deduction for income attributable to domestic production activities of specified agricultural or horticultural cooperatives
- §1.199A-8 - Deduction for income attributable to domestic production activities of specified agricultural or horticultural cooperatives
- §1.199A-9 - Domestic production gross receipts
- §1.199A-10 - Allocation of costs of goods sold (COGS) and other deductions to domestic production gross receipts (DPGR), and other rules
- §1.199A-11 - Wage limitation for the section 199A(g) deduction
- §1.199A-12 - Expanded affiliated groups

Application to Partnerships & S corporations (§199A(f)(1))

In the case of a partnership or S corporation:

1. this section shall be applied at the partner or shareholder level,
2. each partner or shareholder shall take into account such person's allocable share of each qualified item of income, gain, deduction, and loss, and
3. each partner or shareholder shall be treated for purposes of subsection 2 (above) as having W-2 wages and unadjusted basis immediately after acquisition of qualified property for the taxable year in an amount equal to such person's allocable share of the W-2 wages and the unadjusted basis immediately after acquisition of qualified property of the partnership or S corporation for the taxable year (as determined under regulations prescribed by the Secretary).

A partner's or shareholder's allocable share of W-2 wages shall be determined in the same manner as the partner's or shareholder's allocable share of wage expenses. For purposes of such clause, partner's or shareholder's allocable share of the unadjusted basis immediately after acquisition of qualified property shall be determined in the same manner as the partner's or shareholder's allocable share of depreciation. For purposes of this subparagraph, in the case of an S corporation, an allocable share shall be the shareholder's pro rata share of an item.

Computational & Reporting Rules for RPEs (§1.199A-6(b))

In general, an RPE must determine and report information attributable to any trades or businesses it is engaged in necessary for its owners to determine their section 199A deduction.

Computational rules

Using the following four rules, an RPE must determine the items necessary for individuals who own interests in the RPE to calculate their section 199A deduction under §1.199A-1(c) or (d). An RPE that chooses to aggregate trades or businesses under the rules of §1.199A-4 may determine these items for the aggregated trade or business.

1. First, the RPE must determine if it is engaged in one or more trades or businesses. The RPE must also determine whether any of its trades or businesses is an SSTB under the rules of §1.199A-5.
2. Second, the RPE must apply the rules in §1.199A-3 to determine the QBI for each trade or business engaged in directly.
3. Third, the RPE must apply the rules in §1.199A-2 to determine the W-2 wages and UBIA of qualified property for each trade or business engaged in directly.
4. Fourth, the RPE must determine whether it has any qualified REIT dividends as defined in §1.199A-3(c)(1) earned directly or through another RPE. The RPE must also determine the amount of qualified PTP income as defined in §1.199A-3(c)(2) earned directly or indirectly through investments in PTPs.

Reporting rules for RPEs - Trade or business directly engaged in

An RPE must separately identify and report on the Schedule K-1 issued to its owners for any trade or business (including an aggregated trade or business) engaged in directly by the RPE:

1. Each owner's allocable share of QBI, W-2 wages, and UBIA of qualified property attributable to each such trade or business; and
2. Whether any of the trades or businesses described in paragraph (b)(3)(i) of this section is an SSTB.

Reporting rules for RPEs - Other items

An RPE must also report on an attachment to the Schedule K-1, any QBI, W-2 wages, UBIA of qualified property, or SSTB determinations, reported to it by any RPE in which the RPE owns a direct or indirect interest. The RPE must also report each owner's allocated share of any qualified REIT dividends received by the RPE (including through another RPE) as well as any qualified PTP income or loss received by the RPE for each PTP in which the RPE holds an interest (including through another RPE). Such information can be reported on an amended or late filed return to the extent that the period of limitations remains open.

Statement A—QBI Pass-Through Entity Reporting

Pass-through entity's name:			**Pass-through entity's EIN:**	
Shareholder's name:		**Shareholder's identifying number:**		
		Trade or Business 1	**Trade or Business 2**	**Trade or Business 3**
Shareholder's share of:		☐ PTP ☐ Aggregated ☐ SSTB	☐ PTP ☐ Aggregated ☐ SSTB	☐ PTP ☐ Aggregated ☐ SSTB
QBI or qualified PTP items subject to shareholder-specific determinations:				
	Ordinary business income (loss)			
	Rental income (loss)			
	Royalty income (loss)			
	Section 1231 gain (loss)			
	Other income (loss)			
	Section 179 deduction			
	Other deductions			
W-2 wages				
UBIA of qualified property				
Section 199A dividends				

Failure to report information

If an RPE fails to separately identify or report on the Schedule K-1 (or any attachments thereto) issued to an owner an item described in paragraph (b)(3)(i) of this section, the owner's share (and the share of any upper-tier indirect owner) of each unreported item of positive QBI, W-2 wages, or UBIA of qualified property attributable to trades or businesses engaged in by that RPE will be presumed to be zero.

Aggregation Rules (§1.199A-4(b))

Trades or businesses may be aggregated only if an individual or RPE can demonstrate that:

1. The same person or group of persons, directly or by attribution under §267(b) or §707(b), owns 50% or more of each trade or business to be aggregated, meaning in the case of such trades or businesses owned by an S corporation, 50% or more of the issued and outstanding shares of the corporation, or, in the case of such trades or businesses owned by a partnership, 50% or more of the capital or profits in the partnership;
2. The ownership in 1 above exists for a majority of the taxable year, including the last day of the taxable year, in which the items attributable to each trade or business to be aggregated are included in income;
3. All of the items attributable to each trade or business to be aggregated are reported on returns with the same taxable year, not taking into account short taxable years;
4. None of the trades or businesses to be aggregated is a specified service trade or business (SSTB); and
5. The trades or businesses to be aggregated satisfy at least two of the following factors (based on all of the facts and circumstances):
   a. The trades or businesses provide products, property, or services that are the same or customarily offered together.
   b. The trades or businesses share facilities or share significant centralized business elements, such as personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources.
   c. The trades or businesses are operated in coordination with, or reliance upon, one or more of the businesses in the aggregated group (for example, supply chain interdependencies).

Reporting & consistency requirements (§1.199A-4(c)(3))

Once an RPE chooses to aggregate two or more trades or businesses, the RPE must consistently report the aggregated trades or businesses in all subsequent taxable years. A failure to aggregate will not be considered to be an aggregation for purposes of this rule. An RPE that fails to aggregate may not aggregate trades or businesses on an amended return (other than an amended return for the 2018 taxable year). However, an RPE may add a newly created or newly acquired (including through non-recognition transfers) trade or business to an existing aggregated trade or business (including the aggregated trade or business of a lower-tier RPE) if the requirements of §1.199A-4(b)(1) are satisfied. In a subsequent year, if there is a significant change in facts and circumstances such that an RPE's prior aggregation of trades or businesses no longer qualifies for aggregation under the rules of this section, then the trades or businesses will no longer be aggregated within the meaning of this section, and the RPE must reapply the rules in §1.199A-4(b)(1) to determine a new permissible aggregation (if any). An RPE also must report aggregated trades or businesses of a lower-tier RPE in which the RPE holds a direct or indirect interest.

Required annual disclosure (§1.199A-4(c)(4)(i))

For each taxable year, RPEs (including each RPE in a tiered structure) must attach a statement to each owner's Schedule K-1 identifying each trade or business aggregated. The statement must contain:

1. A description of each trade or business;
2. The name and EIN of each entity in which a trade or business is operated;
3. Information identifying any trade or business that was formed, ceased operations, was acquired, or was disposed of during the taxable year;
4. Information identifying any aggregated trade or business of an RPE in which the RPE holds an ownership interest; and
5. Such other information as the Commissioner may require in forms, instructions, or other published guidance.

Statement B—QBI Pass-Through Entity Aggregation Election(s)

Pass-through entity's name: **Pass-through entity's EIN:**

Trade or business aggregation 1*

Provide a description of the aggregated trades or businesses and an explanation of the factors met that allow the aggregation in accordance with Regulations section 1.199A-4. In addition, if the S corporation holds a direct or indirect interest in a relevant pass-through entity (RPE) that aggregates multiple trades or businesses, attach a copy of the RPE's aggregations.

Has this trade or business aggregation changed from the prior year? This includes changes in the aggregation due to a trade or business being formed, acquired, disposed of, or ceased operations. If yes, explain.

* If the pass-through entity's has more than one aggregated group, attach additional Statements B. Name the additional aggregations 2, 3, 4, etc.

Failure to disclose (§1.199A-4(c)(4)(ii))

If an RPE fails to attach the statement required in §1.199A-4(c)(4)(i), the Commissioner may disaggregate the RPE's trades or businesses. The RPE may not aggregate trades or businesses that are disaggregated by the Commissioner for the subsequent three taxable years.

QBI Previously Disallowed Losses (§1.199A-3(b)(1)(iv))

NOTE – The instructions to both the Form 8995 and Form 8995-A have a QBI loss tracking worksheet by year.

General rule

Previously disallowed losses or deductions allowed in the taxable year generally are taken into account for purposes of computing QBI to the extent the disallowed loss or deduction is otherwise allowed by §199A. These previously disallowed losses include, but are not limited to losses disallowed under sections 461(l), 465, 469, 704(d), and 1366(d). These losses are used for purposes of §199A and this section in order from the oldest to the most recent on a first-in, first-out (FIFO) basis and are treated as losses from a separate trade or business. To the extent such losses relate to a PTP, they must be treated as a loss from a separate PTP in the taxable year the losses are taken into account. However, losses or deductions that were disallowed, suspended, limited, or carried over from taxable years ending before January 1, 2018 (including under sections 465, 469, 704(d), and 1366(d)), are not taken into account in a subsequent taxable year for purposes of computing QBI.

Partial allowance

If a loss or deduction attributable to a trade or business is only partially allowed during the taxable year in which incurred, only the portion of the allowed loss or deduction that is attributable to QBI will be considered in determining QBI from the trade or business in the year the loss or deduction is incurred. The portion of the allowed loss or deduction attributable to QBI is determined by multiplying the total amount of the allowed loss by a fraction, the numerator of which is the portion of the total loss incurred during the taxable year that is attributable to QBI and the denominator of which is the amount of the total loss incurred during the taxable year.

Attributes of disallowed loss or deduction determined in year loss is incurred

General rule

Whether a disallowed loss or deduction is attributable to a trade or business, and otherwise meets the requirements of this section, is determined in the year the loss is incurred.

Specified service trades or businesses

If a disallowed loss or deduction is attributable to a specified service trade or business (SSTB), whether an individual has taxable income at or below the threshold amount as defined in §1.199A-1(b)(12), within the phase-in range as defined in §1.199A-1(b)(4), or in excess of the phase-in range is determined in the year the loss or deduction is incurred. If the individual's taxable income is at or below the threshold amount in the year the loss or deduction is incurred, the entire disallowed loss or deduction must be taken into account when applying §1.199A-3(b)(1)(iv)(A) of this section. If the individual's taxable income is within the phase-in range, then only the applicable percentage, as defined in §1.199A-1(b)(2), of the disallowed loss or deduction is taken into account when applying paragraph §1.199A-3(b)(1)(iv)(A) of this section. If the individual's taxable income exceeds the phase-in range, none of the disallowed loss or deduction will be taken into account in applying §1.199A-3(b)(1)(iv)(A) of this section.

Examples (§1.199A-3(b)(1)(D))

EXAMPLE 1 – A is an unmarried individual and a 50% owner of LLC, an entity classified as a partnership for Federal income tax purposes. In 2018, A's allocable share of loss from LLC is $100,000 of which $80,000 is negative QBI. Under section 465, $60,000 of the allocable loss is allowed in determining A's taxable income. A has no other previously disallowed losses under section 465 or any other provision of the Code for 2018 or prior years. Because 80% of A's allocable loss is attributable to QBI ($80,000/$100,000), A will reduce the amount A takes into account in determining QBI proportionately. Thus, A will include $48,000 of the allowed loss in negative QBI (80% of $60,000) in determining A's section 199A deduction in 2018. The remaining $32,000 of negative QBI is treated as negative QBI from a separate trade or business for purposes of computing the section 199A deduction in the year the loss is taken into account in determining taxable income as described in §1.199A-1(d)(2)(iii).

EXAMPLE 2 - B is an unmarried individual and a 50% owner of LLC, an entity classified as a partnership for Federal income tax purposes. After allowable deductions other than the section 199A deduction, B's taxable income for 2018 is $177,500. In 2018, LLC has a single trade or business that is an SSTB. B's allocable share of loss is $100,000, all of which is suspended under section 465. B's allocable share of negative QBI is also $100,000. B has no other previously disallowed losses under section 465 or any other provision of the Code for 2018 or prior years. Because the entire loss is suspended, none of the negative QBI is taken into account in determining B's section 199A deduction for 2018. Further, because the negative QBI is from an SSTB and B's taxable income before the section 199A deduction is within the phase-in range, B must determine the applicable percentage of the negative QBI that must be taken into account in the year that the loss is taken into account in determining taxable income. B's applicable percentage is 100% reduced by 40% (the percentage equal to the amount that B's taxable income for the taxable year exceeds B's threshold amount ($20,000=$177,500-$157,500) over $50,000). Thus, B's applicable percentage is 60%. Therefore, B will have $60,000 (60% of $100,000) of negative QBI from a separate trade or business to be applied proportionately to QBI in the year(s) the loss is taken into account in determining taxable income, regardless of the amount of taxable income and how rules under §1.199A-5 apply in the year the loss is taken into account in determining taxable income.

QBI Loss Tracking Worksheet (Form 8995-A Instructions)

QBI Loss Tracking Worksheet

Use this worksheet to track losses or deductions suspended by other provisions and attributable to QBI using the FIFO method.

Code __________ [Enter the Code section limiting your loss.]

Part I Suspended & Allowed Losses

	A. Total suspended losses in year of disallowance	B. QBI fixed percentage	C. Prior year suspended losses allowed	D. Allowed losses limited by other Code sections
1a. Pre-2018		0.00 %		
b. 2018		%		
c. 2019		%		
d. 2020		%		
e. 2021		%		
f. 2022		%		
g. 2023		%		
h. 20XX		%		
2. Total				

Part II Non-QBI Suspended and Allowed Losses

Allocable to Non-QBI

	E. Suspended losses	F. Allocated prior year suspended losses allowed	G(i). Utilized 2018	G(ii). Utilized 2019	G(iii). Utilized 2020	G(iv). Utilized 2021	G(v). Utilized 2022	G(vi). Utilized 2023	G(vii). Utilized 20XX	H. Remaining suspended losses
1a. Pre-2018										
b. 2018										
c. 2019										
d. 2020										
e. 2021										
f. 2022										
g. 2023										
h. 20XX										
2. Total										
3. Allocation of allowed losses limited by other Code sections . . .										

Part III QBI Suspended and Allowed Losses

Allocable to QBI

	I. Suspended losses	J. Allocated prior year suspended losses allowed	K(i). Utilized 2018	K(ii). Utilized 2019	K(iii). Utilized 2020	K(iv). Utilized 2021	K(v). Utilized 2022	K(vi). Utilized 2023	K(vii). Utilized 20XX	L. Remaining suspended losses
1a. Pre-2018										
b. 2018										
c. 2019										
d. 2020										
e. 2021										
f. 2022										
g. 2023										
h. 20XX										
2. Total										
3. Allocation of allowed losses limited by other Code sections . . .										
4. Total prior year suspended losses allowed that must be included in QBI										

Limitation on Business Interest (§163(j))

NOTE – The TCJA provision applies to taxable years beginning after December 31, 2017.
REPORTING – Use the *Form 8990 - Limitation on Business Interest Expense Under Section 163(j)*.

General Rule (§163(j)(1))

The amount allowed as a deduction under this chapter for any taxable year for business interest shall not exceed the sum of:

1. the business interest income of such taxpayer for such taxable year,
2. 30% of the adjusted taxable income of such taxpayer for such taxable year, plus
3. the floor plan financing interest of such taxpayer for such taxable year.

NOTE – The amount determined under 2. (30% of the adjusted taxable income) shall not be less than zero.

Carryforward of disallowed business interest (§163(j)(2))

The amount of any business interest not allowed as a deduction for any taxable year shall be treated as business interest paid or accrued in the succeeding taxable year.

Exemption for certain small businesses (§163(j)(3))

In the case of any taxpayer (other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under §448(a)(3)) which meets the gross receipts test of §448(c) for any taxable year, the business interest limitation shall not apply to such taxpayer for such taxable year. In the case of any taxpayer which is not a corporation or a partnership, the gross receipts test of §448(c) shall be applied in the same manner as if such taxpayer were a corporation or partnership.

NOTE – This gross receipts test under §448(c) is met if the taxpayer's average annual gross receipts for the 3-tax-year period ending with the prior tax year does not exceed $25 million (adjusted for inflation after 2018).

Application to Partnerships (§163(j)(4)(A))

NOTE – Rules similar to the rules of this subparagraphs shall apply with respect to any S corporation and its shareholders. See §163(j)(4)(D).

In the case of any partnership:

1. this subsection shall be applied at the partnership level and any deduction for business interest shall be taken into account in determining the non-separately stated taxable income or loss of the partnership, and
2. the adjusted taxable income of each partner of such partnership:
    a. shall be determined without regard to such partner's distributive share of any items of income, gain, deduction, or loss of such partnership, and
    b. shall be increased by such partner's distributive share of such partnership's excess taxable income.

NOTE – For purposes of clause 2.b. (above), a partner's distributive share of partnership excess taxable income shall be determined in the same manner as the partner's distributive share of nonseparately stated taxable income or loss of the partnership.

Summary of the double counting rule

The adjusted taxable income of each partner (or shareholder, as the case may be) is determined without regard to such partner's distributive share of the nonseparately stated income or loss of such partnership. In the absence of such a rule, the same dollars of adjusted taxable income of a partnership could generate additional interest deductions as the income is passed through to the partners.

Summary of the additional deduction limit

The limit on the amount allowed as a deduction for business interest is increased by a partner's distributive share of the partnership's excess amount of unused adjusted taxable income limitation. The excess amount with respect to any partnership is the excess (if any) of 30% of the adjusted taxable income of the partnership over the amount (if any) by which the business interest of the partnership (reduced by floor plan financing interest) exceeds the business interest income of the partnership. This allows a partner of a partnership to deduct more interest expense the partner may have paid or incurred to the extent the partnership could have deducted more business interest.

Partnership excess taxable income (§163(j)(4)(C))

NOTE – Rules similar to the rules of this subparagraphs shall apply with respect to any S corporation and its shareholders. See §163(j)(4)(D).

The term "excess taxable income" means, with respect to any partnership, the amount which bears the same ratio to the partnership's adjusted taxable income as:

1. the excess (if any) of:
    a. the amount determined for the partnership under §163(j)(1)(B) (i.e., 30% of adjusted taxable income), over
    b. the amount (if any) by which the business interest of the partnership, reduced by the floor plan financing interest, exceeds the business interest income of the partnership, bears to
2. the amount determined for the partnership under §163(j)(1)(B) (i.e., 30% of adjusted taxable income).

EXAMPLE 1 –ABC is a partnership owned 50-50 by XYZ Corporation and an individual. ABC generates $200 of noninterest income. Its only expense is $60 of business interest. Under the provision the deduction for business interest is limited to 30% of adjusted taxable income, that is, 30% x $200 = $60. ABC deducts $60 of business interest and reports ordinary business income of $140. XYZ's distributive share of the ordinary business income of ABC is $70. XYZ has net taxable income of zero from its other operations, none of which is attributable to interest income and without regard to its business interest expense. XYZ has business interest expense of $25. In the absence of any special rule, the $70 of taxable income from its interest in ABC would permit the deduction of up to an additional $21 of interest (30% x $70 = $21), resulting in a deduction disallowance of only $4. XYZ's $100 share of ABC's adjusted taxable income would generate $51 of interest deductions. If XYZ were instead a passthrough entity, additional deductions could be available at each tier. The double counting rule provides that XYZ has adjusted taxable income computed without regard to the $70 distributive share of the nonseparately stated income of ABC. As a result, XYZ has adjusted taxable income of $0. XYZ's deduction for business interest is limited to 30% x $0 = $0, resulting in a deduction disallowance of $25.

EXAMPLE 2 – The facts are the same as in Example 1 except ABC has only $40 of business interest. As in Example 1, ABC has a limit on its interest deduction of $60. The excess amount for ABC is $20 (i.e., $60 - $40). XYZ's distributive share of the excess amount from ABC partnership is $10. XYZ's deduction for business interest is limited to 30% of its adjusted taxable income plus its distributive share of the excess amount from ABC partnership (30% x $0 + $10 = $10). As a result of the rule, XYZ may deduct $10 of business interest and has an interest deduction disallowance of $15.

Partnerships - special rules for carryforwards (§163(j)(4)(B))

NOTE – This subparagraph shall NOT apply with respect to any S corporation and its shareholders. See §163(j)(4)(D).

The amount of any business interest not allowed as a deduction to a partnership for any taxable year for any taxable year:

1. shall not be carried forward and treated as business interest paid or accrued by the partnership in the succeeding taxable year, and
2. shall, be treated as excess business interest which is allocated to each partner in the same manner as the non-separately stated taxable income or loss of the partnership.

Treatment of excess business interest allocated to partners

If a partner is allocated any excess business interest from a partnership for any taxable year:

1. such excess business interest shall be treated as business interest paid or accrued by the partner in the next succeeding taxable year in which the partner is allocated excess taxable income from such partnership, but only to the extent of such excess taxable income, and
2. any portion of such excess business interest remaining shall be treated as business interest paid or accrued in succeeding taxable years.

NOTE – Excess taxable income allocated to a partner from a partnership for any taxable year shall not be taken into account under §168(j)(1)(A) with respect to any business interest other than excess business interest from the partnership until all such excess business interest for such taxable year and all preceding taxable years has been treated as paid or accrued.

Basis adjustments

In general, the adjusted basis of a partner in a partnership interest shall be reduced (but not below zero) by the amount of excess business interest allocated to the partner. However, if a partner disposes of a partnership interest, the adjusted basis of the partner in the partnership interest shall be increased immediately before the disposition by the amount of the excess (if any) of the amount of the basis reduction over the portion of any excess business interest allocated to the partner which has previously been treated as business interest paid or accrued by the partner. The preceding sentence shall also apply to transfers of the partnership interest (including by reason of death) in a transaction in which gain is not recognized in whole or in part. No deduction shall be allowed to the transferor or transferee under this chapter for any excess business interest resulting in a basis increase under this subclause.

Definitions

Business interest (§163(j)(5))

The term "business interest" means any interest paid or accrued on indebtedness properly allocable to a trade or business. Such term shall not include investment interest (within the meaning of §163(j)(d)).

Business interest income (§163(j)(6))

The term "business interest income" means the amount of interest includible in the gross income of the taxpayer for the taxable year which is properly allocable to a trade or business. Such term shall not include investment income (within the meaning of §163(d)).

Trade or business (§163(j)(7))

The term "trade or business" shall not include:

1. the trade or business of performing services as an employee,
2. any electing real property trade or business,
3. any electing farming business, or
4. the trade or business of the furnishing or sale of:
    a. electrical energy, water, or sewage disposal services,
    b. gas or steam through a local distribution system, or
    c. transportation of gas or steam by pipeline,

    if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, by a public service or public utility commission or other similar body of any State or political subdivision thereof, or by the governing or ratemaking body of an electric cooperative.

Electing real property trade or business (§163(j)(7)(B))

The term "electing real property trade or business" means any trade or business which is described in §469(c)(7)(C) and which makes an election under this subparagraph. Any such election shall be made at such time and in such manner as the Secretary shall prescribe, and, once made, shall be irrevocable.

NOTE – An electing real property trade or business is required to use the alternative depreciation system with respect to any nonresidential real property, residential rental property, and qualified improvement property. See §168(g)(1)(F). The ADS recovery period is 30 years for residential rental property placed in after 2017, and is 40 years if placed in service by before 2018.

Electing farming business (§163(j)(7)(C))

The term "electing real property trade or business" means any trade or business which is described in §469(c)(7)(C) and which makes an election under this subparagraph. Any such election shall be made at such time and in such manner as the Secretary shall prescribe, and, once made, shall be irrevocable.

NOTE – An electing farming business is required to use the alternative depreciation system (ADS) to depreciate any property used in the farming business with a recovery period of 10-years or more. See §168(g)(1)(G).

Adjusted taxable income (§163(j)(8))

The term "adjusted taxable income" means the taxable income of the taxpayer:

1. computed without regard to:
    a. any item of income, gain, deduction, or loss which is not properly allocable to a trade or business,
    b. any business interest or business interest income,
    c. the amount of any net operating loss deduction under §172,
    d. the amount of any deduction allowed under §199A, and
    e. any deduction allowable for depreciation, amortization, or depletion,
    f. the amounts included in gross income under Subpart F income (§951(a)), net CFC tested income (formerly GILTI, §951A(a)), and §78 gross-up amounts, along with related deductions under §245A(a) and §250 (a)(1)(B), and
2. computed with such other adjustments as provided by the Secretary.

UPDATE – The OBBB modified 1e for tax years beginning after 2024. The OBBB adds 1f above for tax years beginning after 2025.

Floor plan financing interest defined (§163(j)(9))
The term "floor plan financing interest" means interest paid or accrued on floor plan financing indebtedness. The term "floor plan financing indebtedness" means indebtedness:
1. used to finance the acquisition of motor vehicles held for sale or lease, and
2. secured by the inventory so acquired.

Motor vehicle
The term "motor vehicle means" a motor vehicle that is any of the following:
1. Any self-propelled vehicle designed for transporting persons or property on a public street, highway, or road.
2. A boat.
3. Farm machinery or equipment.

UPDATE – For tax years beginning after 2024, the OBBB added the following sentence to the end of §163(j)(9)(C): "Such term shall also include any trailer or camper which is designed to provide temporary living quarters for recreational, camping, or seasonal use and is designed to be towed by, or affixed to, a motor vehicle."

Coordination with Interest Capitalization Provisions (§163(j)(10))

UPDATE – The OBBB Act Sec. 70341 added this section for taxable years beginning after 2025. Under the OBBB, the §163(j) limitation applies before interest capitalization, allowable interest is applied first to capitalized amounts, and any carryforward is treated solely as deductible interest.

General rule
The limitation under §163(j)(1) shall apply to business interest without regard to whether the taxpayer would otherwise deduct such business interest or capitalize such business interest under an interest capitalization provision, and any reference in this subsection to a deduction for business interest shall be treated as including a reference to the capitalization of business interest.

Amount allowed applied first to capitalized interest
The amount allowed after taking into account the §163(j)(1) limitation:
1. Shall be applied first to the aggregate amount of business interest which would otherwise be capitalized, and
2. The remainder (if any) shall be applied to the aggregate amount of business interest which would be deducted.

Treatment of disallowed interest carried forward
No portion of any business interest carried forward under §163(j)(2) from any taxable year to any succeeding taxable year shall, for purposes of this title (including any interest capitalization provision which previously applied to such portion), be treated as interest to which an interest capitalization provision applies.

Interest capitalization provision
For purposes of this section, the term "interest capitalization provision" means any provision of this subtitle under which interest:
1. Is required to be charged to capital account, or
2. May be deducted or charged to capital account.

Additional Guidance

§163(j) Final Regulations Issued (TD 9905)

On July 28, 2020, the IRS issued final regulations under §163(j):

- §1.163(j)-1 - Definitions
- §1.163(j)-2 – Deduction for business interest limited
- §1.163(j)-3 - Relationship of business interest deduction limitation to other provisions affecting interest
- §1.163(j)-4 - General rules applicable to C corporations (including REITs, RICs, and members of consolidated groups) and tax-exempt corporations.
- §1.163(j)-5 - General rules governing disallowed business interest expense carryforwards for C corporations
- §1.163(j)-6 - Application of the business interest deduction limitation to partnerships and subchapter S corporations
- §1.163(j)-7 - Application of the business interest deduction limitation to foreign corporations and United States shareholders
- §1.163(j)-8 - Application of the business interest deduction limitation to foreign persons with effectively connected income
- §1.163(j)-9 - provides rules for elections for trades or businesses that are excepted from the rules as well as a safe harbor for certain REITs.
- §1.163(j)-10 - Allocation of interest expense, interest income, and other items of expense and gross income to an excepted trade or business
- §1.163(j)-11 - Transition rules

NOTE - On July 28, 2020, the IRS issued proposed regulations (REG-107911-18) under §163(j) providing further guidance on business interest expense deduction limitations, including complex issues arising from the CARES Act amendments. Subject to certain restrictions, taxpayers may rely on these proposed regulations until final regulations are published in the Federal Register.

FAQs - Aggregation Rules Under §448(c)(2) for the §163(j) Small Business Exemption

The FAQs provide a general overview of the aggregation rules that apply for purposes of the gross receipts test, and that apply to determine whether a taxpayer is a small business that is exempt from the business interest expense deduction limitation.

Qualified residential living facilities safe harbor (Rev. Proc. 2020-59)

This proposed revenue procedure establishes a safe harbor permitting taxpayers engaged in a trade or business that manages or operates qualified residential living facilities to treat that activity as a real property trade or business, solely for purposes of making the §163(j) electing real property trade or business election.

Guidance Issued on the ADS Changes Under TCJA (Rev. Proc. 2019-08)

This revenue procedure explains how real property trades or businesses or farming businesses, electing out of the §163(j) interest deduction limit, change to the ADS for property placed in service before 2018.

Infrastructure TorB Safe Harbor (Rev. Proc. 2018-59)

This revenue procedure provides a safe harbor allowing taxpayers to treat certain infrastructure trades or businesses as real property trades or businesses solely for purposes of qualifying as an electing real property trade or business under §163(j)(7)(B), which allows the business to not qualify as a trade or business under §163(j).

Meals Provided at Convenience of Employer

De Minimis Fringe Benefit Defined (§132(e)(1))

The term “de minimis fringe” means any property or service the value of which is (after taking into account the frequency with which similar fringes are provided by the employer to the employer's employees) so small as to make accounting for it unreasonable or administratively impracticable.

Treatment of certain eating facilities (§132(e)(2))

The operation by an employer of any eating facility for employees shall be treated as a de minimis fringe if:

1. such facility is located on or near the business premises of the employer, and
2. revenue derived from such facility normally equals or exceeds the direct operating costs of such facility.

The preceding sentence shall apply with respect to any highly compensated employee only if access to the facility is available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the employer which does not discriminate in favor of highly compensated employees. For purposes of subparagraph 2. (i.e., revenue derived from such facility), an employee entitled under §119 to exclude the value of a meal provided at such facility shall be treated as having paid an amount for such meal equal to the direct operating costs of the facility attributable to such meal.

Meals or lodging furnished for the convenience of the employer (§119)

There shall be excluded from gross income of an employee the value of any meals or lodging furnished to him, his spouse, or any of his dependents by or on behalf of his employer for the convenience of the employer, but only if:

1. in the case of meals, the meals are furnished on the business premises of the employer, or
2. in the case of lodging, the employee is required to accept such lodging on the business premises of his employer as a condition of his employment.

TCJA Changes to Deductibility of Employer Operated Eating Facilities

For amounts incurred and paid after December 31, 2017 and until December 31, 2025, the provision expands this 50% limitation to expenses of the employer associated with providing food and beverages to employees through an eating facility that meets requirements for de minimis fringes and for the convenience of the employer. Such amounts incurred and paid after December 31, 2025 are not deductible.

NOTE – Prior to 2018, employers could deduct 100% of the cost of business meals that were excludable from the income of employees because they were provided at an employer-operated eating facility for the convenience of the employer. The TJCA removed old §274(n)(2)(B) that protected these expenses from the 50% limitation. Thus, for expenses incurred from 2018 to 2025 only 50% are deductible and after 2025, the expenses are non-deductible.

Meals provided at convenience or employer (§274(o))

Except in the case of §274(e)(8) (i.e., food or beverages sold to customers in a bona fide transaction) or §274(n)(2)(C) (i.e., certain fishing vessels and fish processing facilities north of 50° latitude), no deduction shall be allowed under this chapter for:

1. any expense for the operation of a facility described in §132(e)(2), and any expense for food or beverages, including under §132(e)(1), associated with such facility, or
2. any expense for meals described in §119(a).

EFFECTIVE DATE – Amounts paid or incurred after December 31, 2025.

Business Entertainment & Meal Expenses

Disallowance of entertainment, amusement, recreation, or qualified transportation fringes (§274(a))

No deduction otherwise allowable under this chapter shall be allowed for any item:

1. **Activity -** With respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, or

CAUTION – Prior to 2018, §274 provided an exception that stated "unless the taxpayer establishes that the item was directly related to, or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with, the active conduct of the taxpayer's trade or business." **This section was removed.**

2. **Facility -** With respect to a facility used in connection with an activity referred to in the prior paragraph 1.

NOTE 1 – Dues or fees to any social, athletic, or sporting club or organization shall be treated as items with respect to facilities.
NOTE 2 – An activity described in §212 shall be treated as a trade or business.

Denial of deduction for club dues

Notwithstanding the preceding provisions of this subsection, no deduction shall be allowed under this chapter for amounts paid or incurred for membership in any club organized for business, pleasure, recreation, or other social purpose.

Qualified transportation fringes

No deduction shall be allowed under this chapter for the expense of any qualified transportation fringe (as defined in §132(f)) provided to an employee of the taxpayer.

Specific exceptions to application of §274(a) (§274(e))

The general disallowance under §274(a) shall not apply to the following and any item referred to in shall be treated as an expense:

(1) Food and beverages for employees

Expenses for food and beverages (and facilities used in connection therewith) furnished on the business premises of the taxpayer primarily for his employees.

(2) Expenses treated as compensation

Except as provided in the next paragraph (specified individuals), expenses for goods, services, and facilities, to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation to an employee on the taxpayer's return of tax under this chapter and as wages to such employee for purposes of chapter 24 (relating to withholding of income tax at source on wages).

NOTE – Specified individuals are individuals who, with respect to an employer or other service recipient (or a related party), are subject to the requirements of section 16(a) of the Securities Exchange Act of 1934, or would be subject to such requirements if the employer or service recipient (or related party) were an issuer of equity securities referred to in section 16(a).

As a result, in the case of specified individuals, no deduction is allowed with respect to expenses for (1) a nonbusiness activity generally considered to be entertainment, amusement or recreation, or (2) a facility (e.g., an airplane) used in connection with such activity to the extent that such expenses exceed the amount treated as compensation or includible in income to the specified individual.

EXAMPLE – A company's deduction attributable to aircraft operating costs and other expenses for a specified individual's vacation use of a company aircraft is limited to the amount reported as compensation to the specified individual. However, in the case of other employees or service providers, the company's deduction is not limited to the amount treated as compensation or includible in income.

(3) Reimbursed expenses

Expenses paid or incurred by the taxpayer, in connection with the performance by him of services for another person (whether or not such other person is his employer), under a reimbursement or other expense allowance arrangement with such other person, but this paragraph shall apply:

1. where the services are performed for an employer, only if the employer has not treated such expenses in the manner provided in paragraph (2), or
2. where the services are performed for a person other than an employer, only if the taxpayer accounts (to the extent provided by §273(d)) to such person.

(4) Recreational, etc., expenses for employees

Expenses for recreational, social, or similar activities (including facilities therefor) primarily for the benefit of employees (other than employees who are highly compensated employees (within the meaning of §414(q))). For purposes of this paragraph, an individual owning less than a 10% interest in the taxpayer's trade or business shall not be considered a shareholder or other owner, and for such purposes an individual shall be treated as owning any interest owned by a member of his family (within the meaning of §267(c)(4)). This paragraph shall not apply for purposes of §273(a)(3) (i.e., denial of club dues).

(5) Employee, stockholder, etc., business meetings

Expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors.

(6) Meetings of business leagues, etc

Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in §501(c)(6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under §501(a).

(7) Items available to public

Expenses for goods, services, and facilities made available by the taxpayer to the general public.

(8) Entertainment sold to customers

Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth.

(9) Expenses includible in income of persons who are not employees

Expenses paid or incurred by the taxpayer for goods, services, and facilities to the extent that the expenses are includible in the gross income of a recipient of the entertainment, amusement, or recreation who is not an employee of the taxpayer as compensation for services rendered or as a prize or award under §74. The preceding sentence shall not apply to any amount paid or incurred by the taxpayer if such amount is required to be included (or would be so required except that the amount is less than $600) in any information return filed by such taxpayer under part III of subchapter A of chapter 61 and is not so included.

Business meals (§274(k))

General rule

No deduction shall be allowed under this chapter for the expense of any food or beverages unless:

1. such expense is not lavish or extravagant under the circumstances, and
2. the taxpayer (or an employee of the taxpayer) is present at the furnishing of such food or beverages.

Exceptions

The general rule shall not apply to:

1. any expense described in §274(e)(2), (3), (4), (7), (8), or (9), and
2. any other expense to the extent provided in regulations.

Only 50% of meal expenses allowed as deduction (§274(n))

General rule

The amount allowable as a deduction for any expense for food or beverages shall not exceed 50% of the amount of such expense which would (but for this paragraph) be allowable as a deduction under this chapter.

Exceptions

The general rule shall not apply to any expense if:

1. such expense is described in paragraph §274(e)(2), (3), (4), (7), (8), or (9),
2. in the case of an employer who pays or reimburses moving expenses of an employee, such expenses are includible in the income of the employee under §82, or
3. such expense is for food or beverages:
    a. required by any Federal law to be provided to crew members of a commercial vessel,
    b. provided to crew members of a commercial vessel which is operating on the Great Lakes, the Saint Lawrence Seaway, or any inland waterway of the United States, and which is of a kind which would be required by Federal law to provide food and beverages to crew members if it were operated at sea,
    c. provided on an oil or gas platform or drilling rig if the platform or rig is located offshore,
    d. provided on an oil or gas platform or drilling rig, or at a support camp which is in proximity and integral to such platform or rig, if the platform or rig is located in the United States north of 54 degrees north latitude, or
    e. provided:
        i. on a fishing vessel, fish processing vessel, or fish tender vessel (as such terms are defined in section 2101 of title 46, United States Code), or
        ii. at a facility for the processing of fish for commercial use or consumption which (1) is located in the United States north of 50 degrees north latitude, and (2) is not located in a metropolitan statistical area (within the meaning of §143(k)(2)(B)).

UPDATE – The OBBB added clause 3e for taxable years beginning after 2025.

Special rule for individuals subject to federal hours of service

In the case of any expenses for food or beverages consumed while away from home (within the meaning of §162(a)(2)) by an individual during, or incident to, the period of duty subject to the hours of service limitations of the Department of Transportation, the general limitation shall be applied by substituting "80%" for "50%".

Summary of Business Meals Deductibility			
	Percentage of Meals Deductible		
Exception (§274(e))	**Pre-2018**	**2018–2025**	**Post-2025**
(1) Food & beverages for employees (on business premises)	100%	50%	0%
(2) Expenses treated as compensation	100%	100%	100%
(3) Reimbursed expenses (accountable plan)	100%	100%	100%
(4) Recreational/social activities for employees	100%	100%	100%
(5) Employee/stockholder/director business meetings	50%	50%	50%
(6) Meetings of business leagues, chambers, etc.	50%	50%	50%
(7) Items made available to the public	100%	100%	100%
(8) Entertainment/food sold to customers (bona fide)	100%	100%	100%
(9) Expenses includible in income of nonemployees	100%	100%	100%

Substantiation Required (§274(d))

No deduction or credit shall be allowed:

1. under §162 or §212 for any traveling expense (including meals and lodging while away from home),
2. for any expense for gifts, or
3. with respect to any listed property (as defined in §280F(d)(4)),

unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement

(A) the amount of such expense or other item,
(B) the time and place of the travel or the date and description of the gift,
(C) the business purpose of the expense or other item, and
(D) the business relationship to the taxpayer of the person receiving the benefit.

NOTE – The Secretary may by regulations provide that some or all of the requirements of the preceding sentence shall not apply in the case of an expense which does not exceed an amount prescribed pursuant to such regulations. This subsection shall not apply to any qualified nonpersonal use vehicle (as defined in §274(i)).

Meals and Entertainment Expenses Final Regulations Issued (TD 9925)

On September 30, 2020 the IRS issued final regulations (TD 9925) under §274. This IRC section disallows a business deduction for most entertainment expenses. The regulations clarify the treatment of business deductions for food and beverages that remain deductible, generally limited to 50% of qualifying expenditures, and how taxpayers may distinguish those expenditures from entertainment. The regulations clarify that entertainment does not include food or beverages unless they are provided at or during an entertainment activity and their costs are not separately stated from the entertainment costs.

UPDATE - Meals provided at convenience or employer (§274(o))

Except in the case of §274(e)(8) (i.e., food or beverages sold to customers in a bona fide transaction) or §274(n)(2)(C) (i.e., certain fishing vessels and fish processing facilities north of 50° latitude), no deduction shall be allowed under this chapter for:

3. any expense for the operation of a facility described in §132(e)(2), and any expense for food or beverages, including under §132(e)(1), associated with such facility, or
4. any expense for meals described in §119(a).

EFFECTIVE DATE – Amounts paid or incurred after December 31, 2025.

Qualified Transportation Fringe

Qualified Transportation Fringes Defined (§132(f))

Gross income shall not include any fringe benefit which qualifies as qualified transportation fringe. The term "qualified transportation fringe" means any of the following provided by an employer to an employee:

1. Transportation in a commuter highway vehicle if such transportation is in connection with travel between the employee's residence and place of employment
2. Any transit pass
3. Qualified parking

UPDATE – The exclusion for the qualified bicycle commuting reimbursement was permanently repealed for any taxable year beginning after December 31, 2017.

Limitation on exclusion

The amount of the fringe benefits which are provided by an employer to any employee and which may be excluded from gross income shall not exceed the following amounts adjusted for inflation:

	2026	2025	2024
Commuter highway vehicle, transit pass & qualified parking exclusion	$340/month	$325/month	$315/month

Disallowance of Qualified Transportation Fringes

The TCJA provision disallows a deduction for expenses associated with providing any qualified transportation fringe to employees of the taxpayer, and except as necessary for ensuring the safety of an employee, any expense incurred for providing transportation (or any payment or reimbursement) for commuting between the employee's residence and place of employment.

EFFECTIVE DATE – Amounts paid or incurred after December 31, 2017.

Qualified transportation fringes (§274(a)(4))

No deduction shall be allowed under this chapter for the expense of any qualified transportation fringe (as defined in §132(f)) provided to an employee of the taxpayer.

EFFECTIVE DATE – Amounts paid or incurred after December 31, 2017.

Transportation and commuting benefits (§274(l))

No deduction shall be allowed under this chapter for any expense incurred for providing any transportation, or any payment or reimbursement, to an employee of the taxpayer in connection with travel between the employee's residence and place of employment, except as necessary for ensuring the safety of the employee.

NOTE – In the case of any qualified bicycle commuting reimbursement (as described in §132(f)(5)(F)), this subsection shall not apply for any amounts paid or incurred after December 31, 2017, and before January 1, 2026.

IRS Guidance – Notice 2018-99

This notice provides interim guidance for taxpayers to determine the amount of parking expenses for qualified transportation fringes (QTFs) that is nondeductible under §274(a)(4) and for tax-exempt organizations to determine the corresponding increase in the amount of unrelated business taxable income (UBTI) under §512(a)(7) attributable to the nondeductible parking expenses.

Qualified Moving Expense Reimbursement Repealed (§132(g))

Background (Pre 2018)
Qualified moving expense reimbursements were excluded from gross income if they reimbursed expenses deductible under §217. Excludable amounts also avoided employment taxes. However, reimbursements could not be excluded if the employee also claimed the deduction.

TCJA Temporary Suspension (2018-2025)
The TJCA repealed the exclusion from gross income and wages for qualified moving expense reimbursements except in the case of a member of the Armed Forces (and their spouses or dependents) on active duty who moves pursuant to a military order. This exception applied to both cash reimbursements and in-kind moving/storage expense coverage.

UPDATE - OBBB Permanent Disallowance (Post 2025)
The OBBB permanently extends the repeal of the moving expense reimbursement exclusion. It also expands eligibility for tax-free treatment to **include employees and new appointees of the intelligence community** (as defined in the National Security Act), if the relocation is due to a required change in assignment.

Research & Experimental Expenditures

Background – Pre-2022

Business expenses associated with the development or creation of an asset having a useful life beyond the current year generally must be capitalized and depreciated over such useful life.

Treatment as expense

Taxpayers, however, may elect (under §174) to deduct currently the amount of certain reasonable research or experimentation expenditures paid or incurred in connection with a trade or business.

Capitalize & amortize

Taxpayers may choose to forgo a current deduction, capitalize their research expenditures, and recover them ratably over the useful life of the research, but in no case over a period of less than 60 months. Taxpayers, alternatively, may elect to amortize their research expenditures over a period of 10 years. Research and experimental expenditures deductible under §174 are not subject to capitalization under either §263(a) or §263A.

TCJA - R&E Expenditures to be Amortized (2021-2024) (§174)

EFFECTIVE DATE - For amounts paid or incurred in taxable years beginning after 2021 and before 2025.

Domestic research - 5-year amortization

Amounts defined as specified research or experimental expenditures are required to be capitalized and amortized ratably over a 5-year period, beginning with the midpoint of the taxable year in which the specified research or experimental expenditures were paid or incurred.

Foreign research - 15-year amortization

Specified research or experimental expenditures which are attributable to research that is conducted outside of the United States are required to be capitalized and amortized ratably over a period of 15-years, beginning with the midpoint of the taxable year in which such expenditures were paid or incurred.

UPDATE - Full Expensing of Domestic Research and Experimental Expenditures (New §174A)

EFFECTIVE DATE – This is effective for tax years beginning after December 31, 2024.

OBBB Changes

- OBBB Act Section 70302 creates new §174A, which restores full expensing for domestic R&E expenditures (defined as research connected with the taxpayer's U.S. trade or business and not foreign research within §41(d)(4)(F)).
- Taxpayers may elect to capitalize and amortize domestic R&E costs over a period of not less than 60 months, but immediate expensing is the default.
- Foreign R&E expenditures remain under §174, subject to mandatory 15-year amortization.
- Clarifies that software development costs are treated as R&E.
- Denies expensing for amounts related to land, depreciable/depletable property, or mineral exploration.

Coordination with Other Provisions:

- **Research credit (§41)**: Limited to expenditures treated as domestic R&E under §174A.
- **§280C(c)**: Requires reduction of domestic R&E deduction by the research credit allowed.
- **AMT (§56):** Adjusted to reflect §174A expensing.
- Conforming amendments made throughout the Code (§59(e), §144, §195, §263, §263A, §543, §864, §1016, §1202).

Accounting and Transition Rules:

- Change is treated as an accounting method change under §481, generally applied on a cut-off basis.
- Special transition elections:
    - Small businesses (defined by gross receipts tests under §448(c)) may elect to apply the rule retroactively to post-2021 expenditures.
    - Taxpayers may elect to deduct unamortized domestic R&E expenditures (paid/incurred 2022–2024) either entirely in 2025 or ratably over two years (2025–2026).

Provision	TCJA (2022–2024)	Post-OBBB (2025 and after)
Domestic R&E (U.S.-based)	Mandatory 5-year amortization (beginning with the midpoint of the taxable year in which expenses are paid/incurred). No immediate expensing allowed.	Immediate expensing restored under new §174A. Taxpayer may elect to amortize over ≥60 months, but expensing is default.
Foreign R&E (including software developed outside U.S., §41(d)(4)(F))	Mandatory 15-year amortization.	Mandatory 15-year amortization remains under amended §174 (no expensing option).
Software Development Costs	Mandatory amortization: 5 years (domestic), 15 years (foreign).	Explicitly treated as R&E under §174A/§174; expensing allowed if domestic, 15-year amortization if foreign.
Transition Rules	N/A	Special elections: (i) small businesses may apply rules retroactively to post-2021 expenditures; (ii) unamortized 2022–2024 domestic R&E may be deducted fully in 2025 or ratably over 2025–2026.

Additional Guidance

Rev. Proc. 2025-28 provides procedures for taxpayers to make elections and obtain automatic consent to change accounting methods under OBBBA §70302 for research and experimental (R&E) expenditures. It addresses transitions from TCJA §174 to the new rules under §§174 and 174A, including elections to amortize domestic R&E expenditures, and establishes rules for small business and retroactive elections. It also grants a special automatic extension for certain 2024 returns to allow taxpayers to apply these provisions.

Employee or Independent Contractor – Voluntary Classification Settlement Program

Background - General Classifications

Before you can know how to treat payments that you make for services, you must first know the business relationship that exists between you and the person performing the services. The person performing the services may be:

1. An independent contractor,
2. A common-law employee,
3. A statutory employee, or
4. A statutory non-employee.

Employees

For any worker classified as an employee, the employer is responsible for:

1. Withholding Federal income tax,
2. Withholding and paying the employer social security and Medicare tax (i.e., FICA),
3. Paying Federal unemployment tax (i.e., FUTA),
4. Paying state unemployment tax (i.e., SUTA),
5. Issuing a Form W-2, *Wage and Tax Statement*, annually to each employee,
6. Reporting wages on Form 941, *Employer's Quarterly Federal Tax Return*.
7. Allowing eligible employees to participate in the company retirement plan and fringe benefit packages.

Independent Contractors

For a worker considered to be an independent contractor, the payee is responsible for issuing a Form 1099-MISC, *Miscellaneous Income*, to report compensation annually.

NOTE – The independent contractor is responsible for paying all taxes attributable to his/her income, paying for health insurance and contributing to a retirement plan.

Misclassification of Employees - Consequences (§3509)

If an employer classifies an employee as an independent contractor and has no reasonable basis for doing so, the employer becomes liable for:

1. Employment taxes that should have been withheld from the employee's wages (i.e., FICA, federal and state income taxes)
2. Employer's share of FICA,
3. Federal and state unemployment taxes,
4. Penalties for failure to file the payroll tax returns and for failure to pay the taxes, and
5. Interest on the balances due.

Section 530 Relief of the Revenue Act of 1978

Section 530 is a safe harbor provision that prevents the IRS from retroactively reclassifying "independent contractors" as employees and subjecting the principal to federal employment taxes, penalties and interest for such misclassification. To get this relief, the employer must meet the following three requirements:

1. **Reporting consistency** – the employer filed all Federal tax returns (i.e., Form 1099-MISC),
2. **Substantive consistency** – the employer treated all workers with similar jobs as independent contractors, **AND**
3. **Reasonable basis** – the employer had a reasonable basis for <u>not</u> treating the workers as employees. To establish a reasonable basis one can show <u>either</u>:
   a. They relied on a Federal judicial precedent, published ruling or private letter ruling, or
   b. The taxpayer was audited by the IRS in a prior year and the IRS did not reclassify those workers as employees, or
   c. The taxpayer can cite a long-standing recognized practice of a significant segment of the employer's industry (note: this must be documented prior to paying the first employee of the company), or
   d. Based upon general evidence you had some other reasonable basis.

NOTE – Section 530 does not make or validate workers as independent contractors but rather classifies them as "non-employees" for federal employment tax purposes. Section 530 also does not apply for purposes of federal classifications.

IRS Help

If you want the IRS to determine whether or not a worker is an employee, file Form SS-8, *Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*, with the IRS.

Employee or Independent Contractor?

Control Issue

To determine whether an individual is an employee or an independent contractor under the common law, the relationship of the worker and the business must be examined. In any employee-independent contractor determination, all information that provides evidence of the degree of control and the degree of independence must be considered. Facts that provide evidence of the degree of control and independence fall into three categories: behavioral control, financial control, and the type of relationship of the parties.

IRS Training Manual

The IRS issued Revenue Ruling 87-41 that lists 20 factors to help determine if a worker is an employee or independent contractor. In 1996, the IRS released a training manual he help its agents with this issue. The IRS training manual organizes the 20 factors into the following groups:

1. Behavioral control,
2. Financial control,
3. Relationship factor, and
4. Less important factors.

Behavioral Control

Facts that show whether the business has a right to direct and control how the worker does the task for which the worker is hired include the type and degree of:

1. Instructions - an employee is generally told:
    a. when, where, and how to work,
    b. what tools or equipment to use,
    c. what workers to hire or to assist with the work,
    d. where to purchase supplies and services,
    e. what work must be performed by a specified individual, and
    f. what order or sequence to follow.
2. Training – an employee may be trained to perform services in a particular manner.

Financial Control

Facts that show whether the business has a right to control the business aspects of the worker's job include:

1. The extent to which the worker has unreimbursed expenses,
2. The extent of the worker's investment,
3. The extent to which the worker makes services available to the relevant market,
4. How the business pays the worker, and
5. The opportunity for profit or loss of the worker.

Relationship Factor (i.e., the relationship of the parties)

Type of Relationship – Facts that show the type of relationship include:

1. Written contracts - describing the relationship the parties intended to create,
2. Employee benefits - whether the worker is provided with employee-type benefits,
3. Continuing relationship - the permanency of the relationship, and
4. Integration – if the worker's services are an integral part of the business operations, the worker is generally an employee.

Less Important Factors

The IRS considered the following factors less important than those in the other three groups:

1. Employer's right to fire the worker,
2. Workers right to quit,
3. Full-time or part-time requirement,
4. Work required to be done on employer's premises,
5. Set hours of work,
6. Set order or sequence of the work,
7. Interim oral or written reports requirement.

Recent Cases

Kurek (TC Memo 2013-64)

In the Kurek case, construction workers hired on a project-by-project basis were reclassified as employees. The taxpayer was liable for employment taxes for the year disputed.

Alexander v. FedEx Ground Package System, Inc. (CA 9, 8-27-2014)

The 9th Circuit Court of Appeals reversed the district court and ruled that under the California Labor Code the FedEx drivers were employees in California and not independent contractors.

DOL Issues Final Rule On Worker Classification Under the FLSA

Background

On January 9, 2024, the U.S. Department of Labor (DOL) issued its long-awaited final rule regarding worker classification under the Fair Labor Standards Act (FLSA). This final rule revises the DOL's guidance on how to analyze who is an employee or independent contractor under the Fair Labor Standards Act (FLSA). Specifically, the final rule rescinds the 2021 Independent Contractor Rule that was published on January 7, 2021 and replaces it with guidance for how to analyze employee or independent contractor classification that is more consistent with the FLSA as interpreted by longstanding judicial precedent. The DOL believes that this final rule will reduce the risk that employees are misclassified as independent contractors, while at the same time providing greater consistency for businesses that engage (or wish to engage) with individuals who are in business for themselves.

NOTE - This final rule is effective March 11, 2024. Click here for DOL overview of Final Rule.

Final Rule 6 Factors

This final rule continues to affirm that a worker is not an independent contractor if they are, as matter of economic reality, economically dependent on an employer for work. Consistent with judicial precedent and the DOL's interpretive guidance prior to 2021, the final rule applies the following six factors to analyze employee or independent contractor status under the FLSA:

1. opportunity for profit or loss depending on managerial skill;
2. investments by the worker and the potential employer;
3. degree of permanence of the work relationship;
4. nature and degree of control;
5. extent to which the work performed is an integral part of the potential employer's business; and
6. skill and initiative.

NOTE - No factor or set of factors among this list of six has a predetermined weight, and additional factors may be relevant if such factors in some way indicate whether the worker is in business for themself (i.e., an independent contractor), as opposed to being economically dependent on the employer for work (i.e., an employee under the FLSA).

Observation

The rule explicitly applies only to the FLSA (minimum wage / overtime) and does not alter IRS or other classification tests under the Internal Revenue Code or ERISA. Businesses and advisors must coordinate across multiple tests:

- DOL/FLSA classification (six-factor totality test)
- IRS/Tax classification (common-law control test)
- State and local classification tests (which may vary)

Additional Guidance

- DOL FAQs - click here
- IRS website - Independent contractor (self-employed) or employee? – click here
- IRS Topic 762 - Independent contractor vs. employee – click here
- Form SS-8 - Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding
- Voluntary Classification Settlement Program (VCSP) FAQs – click here
- Publication 15-A - Employer's Supplemental Tax Guide

Accountable Reimbursement Plans - Overview

General Rule (§62(a))
The term "adjusted gross income" means, in the case of an individual, gross income minus the following deductions paid or incurred by the taxpayer, in connection with the performance by him of services as an employee, under a reimbursement or other expense allowance arrangement with his employer. The fact that the reimbursement may be provided by a third party are not determinative of whether or not the preceding sentence applies.

Exception to the General Rule (§62(c))
An arrangement will not be treated as a reimbursement or other expense allowance arrangement if:
1. Such arrangement does not require the employee to substantiate the expenses covered by the arrangement to the payor, or
2. Such arrangement provides the employee the right to retain any amount (i.e., an advance) in excess of the substantiated expenses covered under the arrangement.

Reimbursement or Other Expense Allowance Arrangement (§1.62-2(c)(1))
The phrase "reimbursement or other expense allowance arrangement" means an arrangement that meets the following requirements:
1. Business connection,
2. Substantiation (within a reasonable period of time), AND
3. Returning amounts in excess of expenses (within a reasonable period of time).

NOTE – A payor may have more than one arrangement with respect to a particular employee, depending on the facts and circumstances.

Accountable Plans (§1.62-2(c))
In general, if an arrangement meets the three reimbursement requirements, all amounts paid under the arrangement are treated as paid under an "accountable plan."

Special Rule for Failure to Return Excess
If an arrangement meets the three reimbursement requirements, but the employee fails to return, within a reasonable period of time, any amount in excess of the amount of the expenses substantiated, only the amounts paid under the arrangement that are not in excess of the substantiated expenses are treated as paid under an accountable plan.

Treatment of Payments Under an Accountable Plan
Amounts treated as paid under an accountable plan:
1. Are excluded from the employee's gross income,
2. Are not reported as wages or other compensation on the employee's Form W-2, and
3. Are exempt from the withholding and payment of employment taxes (Federal Insurance Contributions Act (FICA), Federal Unemployment Tax Act (FUTA), Railroad Retirement Tax Act (RRTA), Railroad Unemployment Repayment Tax (RURT), and income tax).

NOTE – If an arrangement does not satisfy one or more of the reimbursement requirements, all amounts paid under the arrangement are treated as paid under a "non-accountable plan."

Treatment of Payments Under Non-Accountable Plans

Amounts treated as paid under a non-accountable plan are:

1. Included in the employee's gross income,
2. Must be reported as wages or other compensation on the employee's Form W-2, and
3. Are subject to withholding and payment of employment taxes (FICA, FUTA, RRTA, RURT, and income tax).

Business Connections (§1.62-2(d))

An arrangement meets the business connections requirements if it provides advances, allowances (including per diem allowances, allowances only for meals and incidental expenses, and mileage allowances), or reimbursements only for business expenses that are allowable as deductions under the Code, and that are paid or incurred by the employee in connection with the performance of services as an employee of the employer.

NOTE – If a payor arranges to pay an amount to an employee regardless of whether the employee incurs (or is reasonably expected to incur) business expenses, the arrangement does not satisfy the business connection requirement and all amounts paid under the arrangement are treated as paid under a non-accountable plan.

Substantiation (§1.62-2(e))

An arrangement meets the substantiation requirements if it requires each business expense to be substantiated to the payor, within a reasonable period of time. See regulation §1.274-5(c)(2) for the detailed substantiation rules.

NOTE – It is not sufficient if an employee merely aggregates expenses into broad categories (such as "travel") or reports individual expenses through the use of vague, non-descriptive terms (such as "miscellaneous business expenses").

Returning Amounts in Excess of Expenses (§1.62-2(f))

An arrangement meets the retuning amounts in excess of expenses requirements if it requires the employee to return to the payor within a reasonable period of time any amount paid under the arrangement in excess of the expenses substantiated. The determination of whether an arrangement requires an employee to return amounts in excess of substantiated expenses will depend on the facts and circumstances. An arrangement whereby money is advanced to an employee to defray expenses will be treated as satisfying the retuning amounts in excess of expenses requirements only if:

1. The amount of money advanced is reasonably calculated not to exceed the amount of anticipated expenditures,
2. The advance of money is made on a day within a reasonable period of the day that the anticipated expenditures are paid or incurred, AND
3. Any amounts in excess of the expenses substantiated are required to be returned to the payor within a reasonable period of time after the advance is received.

Reasonable Period (§1.62-2(g))

The determination of a reasonable period of time will depend on the facts and circumstances. There are two safe harbor methods provided under the regulations:

Fixed Date Method

The following will be treated as having occurred within a reasonable period of time:

1. **Advance -** an advance made within 30 days of when an expense is paid or incurred,
2. **Expense substantiated -** an expense substantiated to the payor within 60 days after it is paid or incurred, or
3. **Amount Returned** - an amount returned to the payor within 120 days after an expense is paid or incurred.

Periodic Statement Method

If a payor provides employees with periodic statements (no less frequently than quarterly) stating the amount, if any, paid under the arrangement in excess of the expenses the employee has substantiated, and requesting the employee to substantiate any additional business expenses that have not yet been substantiated (whether or not such expenses relate to the expenses with respect to which the original advance was paid) and/or to return any amounts remaining unsubstantiated within 120 days of the statement, an expense substantiated or an amount returned within that period will be treated as being substantiated or returned within a reasonable period of time.

Below-Market Loans - Overview (§7872)

Purpose of §7872

§7872 generally treats certain loans in which the interest rate charged is less than the applicable Federal rate as economically equivalent to loans bearing interest at the applicable Federal rate, coupled with a payment by the lender to the borrower sufficient to fund all or part of the payment of interest by the borrower. Such loans are referred to as below-market loans.

NOTE – Each month, the IRS provides various prescribed rates for federal income tax purposes. These rates, known as Applicable Federal Rates (AFRs), are regularly published as revenue rulings. Click here to see the published monthly rates.

Applicable Federal Rates (AFR) – November 2025 (Rev. Rul. 2025-21)

	Period for Compounding			
	Annual	**Semiannual**	**Quarterly**	**Monthly**
Short-term (0 to 3 years)				
AFR	3.69%	3.66%	3.64%	3.63%
110% AFR	4.07%	4.03%	4.01%	4.00%
120% AFR	4.44%	4.39%	4.37%	4.35%
130% AFR	4.82%	4.76%	4.73%	4.71%
Mid-term (3+ to 9 years)				
AFR	3.83%	3.79%	3.77%	3.76%
110% AFR	4.21%	4.17%	4.15%	4.13%
120% AFR	4.60%	4.55%	4.52%	4.51%
130% AFR	4.99%	4.93%	4.90%	4.88%
150% AFR	5.77%	5.69%	5.65%	5.62%
175% AFR	6.74%	6.63%	6.58%	6.54%
Long-term (9+ years)				
AFR	4.62%	4.57%	4.54%	4.53%
110% AFR	5.09%	5.03%	5.00%	4.98%
120% AFR	5.56%	5.48%	5.44%	5.42%
130% AFR	6.03%	5.94%	5.90%	5.87%

Two Types of Below-Market Loans (§7872(e)(1) & (Prop. Reg. §1.7872-3(a))

§7872 does not impute interest on loans which require the payment of interest at the applicable Federal rate. The term "below-market loan" means any loan if:

1. In the case of a **demand loan**, interest is payable at a rate less than the applicable Federal rate; or
2. In the case of a **term loan**, the amount loaned exceeds the present value of all payments due under the loan, determined as of the day the loan is made, using a discount rate equal to the applicable Federal rate in effect on the day the loan is made.

Categories of Below-Market Loans

§7872 applies only to certain categories of below-market loans. These categories are:

1. Gift loans,
2. Compensation-related loans,
3. Corporation-shareholder loans,
4. Tax avoidance loans, and
5. Certain other loans classified in the regulations under §7872 as significant tax effect loans (i.e., loans whose interest arrangements have a significant effect on any Federal tax liability of the lender or the borrower.)

Compensation-Related Loans (Prop Reg. §1.7872-4(c))

A compensation-related loan is a below-market loan that is made in connection with the performance of services, directly or indirectly, between:

1. An employer and an employee,
2. An independent contractor and a person for whom such independent contractor provides services, or
3. A partnership and a partner if the loan is made in consideration for services performed by the partner acting other than in his capacity as a member of the partnership.

Corporation-Shareholder Loans (Prop Reg. §1.7872-4(d))

A below-market loan is a corporation-shareholder loan if the loan is made directly or indirectly between a corporation and any shareholder of the corporation. The amount of money treated as:

1. transferred by the lender to the borrower is a distribution of money (characterized according to §301 for a C corporation or §1368 for an S corporation) if the corporation is the lender, or
2. a contribution to capital if the shareholder is the lender.

NOTE – A below-market loan from a corporation that is not a publicly held corporation to an employee of the corporation who is also a shareholder owning directly or indirectly more than 5% of the total voting power of all classes of stock entitled to vote or more than 5% of the total number of shares of all other classes of stock or 5% of the total value of shares of all classes of stock (including voting stock) of the corporation; will be presumed to be a corporation-shareholder loan, in the absence of clear and convincing evidence that the loan is made solely in connection with the performance of services.

De Minimis Exception for Compensation Related or Corporation-Shareholder Loans (Prop. Reg. §1.7872-9)

Demand Loan (Prop. Reg. §1.7872-9(a))

In the case of any demand loan, the provisions of §7872 do not apply to any day on which the aggregate outstanding amount of loans between the lender and the borrower does not exceed $10,000.

Term Loan (Prop. Reg. §1.7872-9(a))

In the case of any term loan, the provisions of §7872 apply to the loan as of the first day on which the aggregate outstanding amount of loans between the lender and the borrower exceeds $10,000. Once §7872 applies to a term loan, §7872 continues to apply to the loan regardless of whether the $10,000 limitation applies at some later date.

Employee Retention Credit Updates

IRS News Releases

- IRS dirty dozen warnings (03-10-23) (IR-2023-49). To see the entire 2023 dirty dozen list click here.
- Professional Responsibility and the Employee Retention Credit (Issue #2023-02)
- IRS orders immediate stop to new Employee Retention Credit processing amid surge of questionable claims (IR-2023-169)
- IRS reminds businesses to watch out for warning signs of aggressive ERC promotion (IR-2023-170)
- ERC Guidance on Supply Chain Disruptions (TAM 2023-005)
- Initial Voluntary Disclosure Program (IR-2023-247)
- IRS shares more warning signs of incorrect claims for the ERC (IR-2024-198)
- IRS moves forward with ERC claims (IR-2024-203)
- IRS sending up to 30,000 letters to address more than $1 billion in errant claims (IR-2024-212)
- IRS reopens (through November 22) Voluntary Disclosure Program to help businesses with problematic ERC claims (IR-2024-213) (Announcement 2024-30)
- IRS opens new process for payroll companies, third-party payers to help clients resolve incorrect claims for the Employee Retention Credit (IR-2024-246)

Additional Information & Guidance

- IRS issues FAQs to address Employee Retention Credits under ERC compliance provisions of the One, Big, Beautiful Bill (FS-2025-07)
- IRS website ERC information – click here
- IRS ERC Checklist – click here
- Withdraw an Employee Retention Credit (ERC) claim – click here
- FinCEN Alert on COVID-19 Employee Retention Credit Fraud – click here
- ERC Voluntary Disclosure Program – click here
- Understanding Letter 105-C, Disallowance of the Employee Retention Credit – click here

Returns For > $10,000 Cash Received in Trade or Business

Background

§6050I requires any person who receives more than $10,000 in cash in the course of their trade or business to file Form 8300 - Report of Cash Payments Over $10,000 Received in a Trade or Business, and to provide a written statement to the payer. §6050I(f)(2) provides civil and criminal penalties may apply for failure to comply with §6050I.

NOTE - Beginning January 1, 2024, businesses must e-file their Forms 8300 if they are required to e-file at least 10 other information returns, such as Forms 1099 and Forms W-2.

Cash Defined

The act expands §6050I(d)(3) to include digital assets as part of the definitions of cash for reporting purposes.

EFFECTIVE DATE - IIJA Sec. 80603(b)(3) applies to returns required to be filed, and statements required to be furnished, after December 31, 2023.

Update – Announcement 2024-4

This announcement provides transitional guidance on the reporting requirements for transactions involving digital assets under IRC §6050I. This announcement clarifies that, until the IRS issues final regulations, digital assets are not required to be included when determining whether the cash received in a single transaction (or related transactions) meets the $10,000 reporting threshold. The announcement states:

- Until the Treasury Department and the IRS publish regulations under §6050I, persons engaged in a trade or business who, in the course of that trade or business, receive digital assets or digital assets and other cash in one transaction (or two or more related transactions) will not be required to include those digital assets when determining whether cash received has a value in excess of the $10,000 reporting threshold for purposes of determining if reporting is required under §6050I with respect to those transactions.
- Persons engaged in a trade or business who, in the course of that trade or business, receive cash (other than digital assets) in excess of $10,000 in one transaction (or two or more related transactions) must continue to file an information return under section 6050I with respect to that cash received.

Information Reporting of Certain Payments (§6041 & §6041A)

Information at Source General Rule (§6041)

IRC §6041 requires reporting of payments made in the course of a trade or business that are $600 or more (pre-OBBB) in a calendar year, if those payments represent fixed or determinable gains, profits, or income, including but not limited to:

- Rents,
- Salaries, wages, compensation,
- Premiums, annuities, or other gains/profits,
- Nonemployee payments.

Key Applications

- Broad "catch-all" provision requiring businesses to file information returns (Forms 1099) for a wide range of payments.
- Covers payments to individuals, partnerships, and in some cases corporations (unless exempted).
- Historically the main statutory authority for Form 1099-MISC and 1099-NEC reporting.
- Used for reporting nonwage compensation not subject to payroll reporting (different from W-2).

Scope and Exceptions

- Applies to persons engaged in a trade or business making payments to another person.
- Certain payments are excluded (e.g., some payments to corporations, payments to tax-exempt organizations, and others specified by regulation).
- Government entities generally not covered here (they are specifically pulled in under §6041A).

UPDATE - OBBB Changes after 2025

Under OBBB Act Sec. 70433, the §6041(a) threshold of $600 increases to $2,000 for payments made after December 31, 2025, indexed for inflation starting in 2027 (rounded to nearest $100).

NOTE - This change flows through to §6041A (service payments) and backup withholding under §3406.

Returns regarding payments of remuneration for services and direct sales (§6041A)

IRC §6041A requires reporting of payments of $600 or more (pre-OBBB rule) made in the course of a trade or business:

- By a person engaged in a trade or business,
- To another person,
- As remuneration for services performed.

Key Applications

- Covers services performed by nonemployees (similar to Form 1099-NEC reporting).
- Specifically written to ensure broader coverage than §6041, which focuses on "fixed or determinable income" - §6041A makes it explicit that service remuneration is reportable.
- Includes payments by government agencies and tax-exempt organizations (unless specifically excepted).

Special Rule for Subcontractors (§6041A(b))

- Requires persons engaged in the trade or business of renting property to report payments to subcontractors for services performed on rental real estate (e.g., payments to property managers, maintenance contractors).

UPDATE - OBBB Changes after 2025

Under OBBB Act Sec. 70433, the §6041A service payment reporting threshold is tied directly to §6041(a). Thus, the threshold of $600 increases to $2,000 for payments made after December 31, 2025, with inflation indexing beginning in 2027.

Information Reporting – §6041 vs. §6041A		
Feature	**IRC §6041**	**IRC §6041A**
What it covers	Payments of **fixed or determinable income** (e.g., rent, interest, royalties, nonemployee compensation) in the course of a trade or business.	Payments of **remuneration for services** performed in the course of a trade or business.
Threshold (pre-OBBB)	$600	$600
Threshold (post-OBBB, after 12-31-25)	$2,000, indexed for inflation after 2026	$2,000, indexed for inflation after 2026 (linked to §6041(a))
Payors covered	Persons engaged in a trade or business.	Persons engaged in a trade or business, **plus certain government agencies and tax-exempt organizations**.
Special rules	Broad general reporting rule, with many exceptions spelled out elsewhere (e.g., corporate payees, small payments).	Explicitly applies to **service payments**; includes special rule for **subcontractor services on rental real estate** (§6041A(b)).
Tax reporting	Primarily Form **1099-MISC** or **1099-NEC** depending on type of income.	Primarily Form **1099-NEC** (nonemployee compensation) or **1099-MISC** for certain services.

Information Reporting on Payment Card & Third Party Payment Transactions

Form 1099-K Reporting (§6050W)

For payments made after December 31, 2010, the Housing Assistance Tax Act (HATA) of 2008 added IRC §6050W. §6050W requires any payment settlement entity making payment to a participating payee in settlement of reportable payment transactions to report annually to the IRS and to the participating payee the gross amount of such reportable payment transactions, as well as the name, address, and (Taxpayer Identification Numbers) TIN of the participating payees. A "reportable payment transaction" means any payment card transaction (e.g., a credit card or debit card) and any third party network transaction (e.g., PayPal and eBay).

Exception for De Minimis Payments by Third Party Settlement Organizations

A third party settlement organization is not required to report any information with respect to third party network transactions of any participating payee unless:

1. the aggregate value of third party network transactions for the year exceeds $20,000 AND
2. the aggregate number of such transactions exceeds 200.

NOTE – This was effective for returns for calendar years beginning before 01-01-2022.

Modification of Exception (2022 to 2024)

The ARPA of 2021 Sec. 9674 provision modified the threshold (after 2021) for reporting, setting it at $600 per year. Modified §6050W(e) states "A third party settlement organization shall not be required to report any information under §6050W(a) with respect to third party network transactions of any participating payee if the amount which would otherwise be reported under §6050W(a)(2) with respect to such transactions does not exceed $600."

NOTE – The IRS delayed enforcement for 2022–2023 and phased-in $5,000 threshold for 2024.

UPDATE – OBBB Modifications Post 2024

The OBBB reinstates the pre-ARPA de minimis exception for payments , so Form 1099-K reporting is required only if aggregate payments exceed $20,000 and the number of transactions exceeds 200 in a calendar year (§6050W(e)). The same $20,000/200 threshold now applies for backup withholding under §3406, meaning payments through third-party networks are reportable only if both tests are met.

Provision	Pre-2025 (ARPA rule, current law through 2024)	Post-2024 (OBBB change)
Reporting Threshold	$600 with no transaction minimum (single payment could trigger Form 1099-K).	$20,000 AND more than 200 transactions required to trigger Form 1099-K.
Backup Withholding (§3406)	Applied to any reportable third-party network payments once the $600 threshold was reached.	Applies only if the **$20,000/200 transaction threshold** is met; otherwise, not subject to backup withholding.
Effective Date	Applies under ARPA for calendar years after 2021; IRS has delayed enforcement for 2022–2023 and phased-in $5,000 threshold for 2024.	Applies to payments for calendar years **beginning after December 31, 2024**.
Provision	Pre-2025 (ARPA rule, current law through 2024)	Post-2024 (OBBB change)

Relief for Duplicated Reporting After 2010 (Reg. §1.6041-1)

On August 13, 2010, the IRS issued final regulations addressing business purchases made with credit or debit cards that would be exempt from the new reporting requirements (under §6041(a)) because banks and other payment processors already report them under §6050W (i.e., relating to payment card and third party network transactions). The final regulations under §1.6041-1(a)(1)(iv) and §1.6041A-1(d)(4) state that transactions that would otherwise be required to be reported on information returns under §6050W and either §6041 or §6041A, are reported only under §6050W. Solely for purposes of determining whether a payor is eligible for relief from reporting under §6041, the de minimis threshold for third party network transactions in §1.6050W–1(c)(4) is disregarded because §6041 payor will be unable to determine whether the de minimis threshold applies. These regulations apply to payments made after December 31, 2010.

Reg. §1.6041-1(a)(1)(v), Example 1 - Restaurant owner Al, in the course of business, pays $600 of fixed or determinable income to Bill, a repairman, by credit card. Bill is one of a network of unrelated persons that has agreed to accept Al's credit card as payment under an agreement that provides standards and mechanisms for settling the transactions between a merchant acquiring bank and the persons who accept the cards. Merchant acquiring Bank Y is responsible for making the payment to Bill. Al, as payor, is not required to file an information return under §6041 with respect to the transaction because Bank Y, as the payment settlement entity for the payment card transaction, is required to file an information return under §6050W.

Installment Payment of Tax on Gain from Sale of Qualified Farmland to Qualified Farmers (§1062)

Election to pay tax in installments

IRC §1062 allows individual taxpayers to elect to pay the tax on gain from the sale of qualified farmland property to a qualified farmer in four equal annual installments, easing the tax burden and promoting farmland transfers to active farmers. Effective for sales after July 4, 2025.

Eligibility Criteria

To qualify, the following must apply:

1. **The property sold must be qualified farmland property**, meaning:
   a. It is located in the U.S.,
   b. It was used or leased for farming purposes during substantially all of the prior 10 years, and
   c. It is subject to a covenant or legal restriction limiting non-farm use for 10 years after the sale.
2. **The buyer must be a qualified farmer**, defined as someone actively engaged in farming, using the criteria under §1001(b)-(c) of the Food Security Act of 1985 (7 U.S.C. 1308-1(b), (c)).

Installment Election Mechanics

Installment Election

- Taxpayer may elect to pay the applicable net tax liability in 4 equal annual installments
- The election must be made by the due date (without extension) of the tax return for the year of sale
- Once made, the election is binding unless revoked with IRS consent.
- The election is made on the individual return, even if the sale occurred through a partnership or S corporation
- Taxpayer must include with the return for the year of sale a copy of the legal covenant or restriction placed on the farmland, demonstrating the 10-year farm-use restriction.

Applicable Net Tax Liability Defined

The amount of tax attributable to the gain from the farmland sale:

Net income tax **with** gain
<u>– Net income tax **without** gain</u>
= Applicable net tax liability

Installment Payment Timing

- **1st installment -** Due with the return for the year of sale
- **2nd–4th installments -** Due with the returns for the next 3 successive years

Acceleration Triggers

- **Missed payment** - All unpaid installments become immediately due.
- **Death of individual taxpayer -** Remaining installments are due with the return for the year of death.

Exclusions and Recapture Triggers

- If the use restriction covenant is not attached, the election is invalid.
- The IRS may revoke installment privileges for fraud, negligence, or rule violations.

Modifications Related to Foreign Tax Credit Limitation

Background

The foreign tax credit (FTC) is generally limited to a taxpayer's U.S. tax liability on its foreign source taxable income, applied separately by category of income. One such category is net CFC (Controlled Foreign Corporation) tested income, which was previously known as Global Intangible Low-Taxed Income (GILTI).

OBBB Act Sec. 770323 (Post 2025)

Starting with tax years after December 31, 2025, only deductions directly connected to net CFC tested income (formerly GILTI), plus the §250(a)(1)(B) and §164(a)(3) deductions, may be allocated to this category for FTC limitation purposes. Interest and R&E expenses can no longer be allocated to net CFC tested income; instead, they must be allocated to U.S. source income. This change narrows the deductions that reduce the FTC limitation for net CFC tested income, potentially increasing FTC capacity in this category.

NOTE - Individuals, trusts, and estates who are U.S. shareholders of a CFC may make a §962 election to be treated as a domestic corporation for purposes of Subpart F and net CFC tested income inclusions. When this election is made, the new allocation and limitation rules for deductions under IRC §904 apply in the same manner as they do for corporations, including the restrictions on allocating interest and R&E expenses to net CFC tested income.

UPDATE - Allocation of Deductions to Foreign Source Net CFC Tested Income (formerly GILTI) for Foreign Tax Credit Purposes

Beginning with tax years starting after **December 31, 2025**, the Act modifies how deductions are allocated (under §904(b)) to the net CFC tested income category for FTC limitation purposes:

- **Allowed allocations:**
  - The deduction under §250(a)(1)(B) for net CFC tested income, and
  - The deduction under §164(a)(3) for foreign taxes imposed on that income.
- **Prohibited allocations:**
  - No allocation of interest expense, and
  - No allocation of research & experimental (R&E) expenditures.
- **Other deductions:**
  - Allocated to this category only if **directly connected** to net CFC tested income.
- **Reallocation rule:**
  - Any deduction that would otherwise be allocated to net CFC tested income (but for the above restrictions) must instead be allocated to **U.S. source taxable income** for FTC limitation purposes.

Allocation of Deductions to Foreign Source Net CFC Tested Income (formerly GILTI)		
Rule	**Before 2026 (GILTI rules)**	**After 2025 (OBBB – Net CFC Tested Income rules)**
Income Category	Global Intangible Low-Taxed Income (GILTI)	Net Controlled Foreign Corporation (CFC) Tested Income
FTC Limitation	Foreign tax credit (FTC) limit applies by category, including GILTI.	FTC limit applies by category, including Net CFC Tested Income.
Deductions Allocable	Broad allocations of expenses applied, including interest and R&E, under general §861 allocation/apportionment rules.	Only **directly allocable deductions** allowed, plus: (i) §250(a)(1)(B) deduction for net CFC tested income and (ii) §164(a)(3) deduction for taxes on such income.
Interest Expense	Allocated to GILTI under general rules.	**No allocation** of interest expense permitted.
R&E Expenditures	Allocated under general rules (often reducing FTC capacity).	**No allocation** of R&E expense permitted.
Other Deductions	Apportioned under general §861 rules, even if indirectly related.	Only deductible if **directly connected** to net CFC tested income.
Reallocation Rule	Standard allocation under §861 – deductions could reduce foreign income categories like GILTI.	Deductions barred from this category (interest, R&E, indirect) must be **reallocated to U.S. source income** for FTC limitation purposes.
Effective Date	Through tax years beginning before January 1, 2026.	Tax years beginning after December 31, 2025.

S Corporation & Partnership Provisions

S Corporation Reasonable Compensation Issues

Reasonable Compensation (IRS Website)

S corporations must pay reasonable compensation to a shareholder-employee in return for services that the employee provides to the corporation before non-wage distributions may be made to the shareholder-employee. The amount of reasonable compensation will never exceed the amount received by the shareholder either directly or indirectly.

> **NOTE –** The instructions to the Form 1120S, U.S. Income Tax Return for an S Corporation, state "Distributions and other payments by an S corporation to a corporate officer must be treated as wages to the extent the amounts are reasonable compensation for services rendered to the corporation."

Several court cases support the authority of the IRS to reclassify other forms of payments to a shareholder-employee as a wage expense which are subject to employment taxes.

Authority to Reclassify	*Joly vs. Commissioner*, 211 F.3d 1269 (6th Cir., 2000)
Reinforced Employment Status of Shareholders	*Veterinary Surgical Consultants, P.C. vs. Commissioner*, 117 T.C. 141 (2001) *Joseph M. Grey Public Accountant, P.C. vs. Commissioner*, 119 T.C. 121 (2002)
Reasonable Reimbursement for Services Performed	*David E. Watson, PC vs. U.S., 668 F.3d 1008 (8th Cir. 2012)*

The key to establishing reasonable compensation is determining what the shareholder-employee did for the S corporation. As such, **we need to look to the source of the S corporation's gross receipts. The three major sources are:**

1. Services of shareholder,
2. Services of non-shareholder employees, or
3. Capital and equipment.

If the gross receipts and profits come from items 2 and 3, then that should not be associated with the shareholder-employee's personal services and it is reasonable that the shareholder would receive distributions along with compensations.

On the other hand, **if most of the gross receipts and profits are associated with the shareholder's personal services, then most of the profit distribution should be allocated as compensation.**

In addition to the shareholder-employee direct generation of gross receipts, the shareholder-employee should also be compensated for administrative work performed for the other income producing employees or assets. For example, a manager may not directly produce gross receipts, but he assists the other employees or assets which are producing the day-to-day gross receipts.

Some factors in determining reasonable compensation:

- Training and experience
- Duties and responsibilities
- Time and effort devoted to the business
- Dividend history
- Payments to non-shareholder employees
- Timing and manner of paying bonuses to key people
- What comparable businesses pay for similar services
- Compensation agreements
- The use of a formula to determine compensation

S Corporation Unreasonably Low Wages to CPA Shareholder (Watson, P.C. v. U.S., (CA8) - 2012)

David Watson, CPA was the sole shareholder of an S Corporation (Watson, PC.) that provided accounting services to a firm he used to be a partner in

- During the years under audit (2002 & 2003), his salary was $24,000 year.
- David received $203,651 in distributions in 2002 and $175,470 in 2003.
- The 8th circuit court of appeals affirmed the district courts judgment that the CPA shareholder's $24,000 annual wages were unreasonably low.
- The fair market value of the wages was determined to be $91,044 per year.
  Thus, approximately $67,000 of the distributions each year were reclassified as wages subject to FICA taxes.
- The Supreme Court declined to review this case.

Distributions Reclassified as Wages – (Glass Block Unlimited - TC Memo 2013-180)

The Tax Court agreed with the IRS and reclassified S corporation distributions to the sole shareholder as taxable wages even though it created an S corporation loss. The court also rejected the taxpayer's position that the distributions should be reclassified as loan repayments because the wages would result in unreasonable compensation.

Sean McAlary Ltd, Inc., (TC Summary 2013-62)

The Mr. McAlary was the sole shareholder of a real estate S Corporation. The employment contract was supposed to pay him a base salary of $24,000 plus $10,000 for each additional 10 sales agents and associate brokers he recruited. In 2006, the S corporation reported gross receipts of $518,189, various deductions totaling $286,735, and net income of $231,454. The S corporation did not issue a Form W-2 to Mr. McAlary, nor did it claim a deduction for any amount paid as wages or compensation for services. During 2006, Mr. McAlary transferred a total of $240,000 from petitioner's account to his personal account.

NOTE – Whether compensation is reasonable is a question to be resolved on the basis of an examination of all the facts and circumstances of the case, and no single factor is decisive.

The court stated that determining an employee's reasonable compensation is dependent upon a number of factors and is far from an exact science. Considering the totality of the facts and circumstances, including the pertinent wage and labor statistics cited, general market conditions, the taxpayers limited experience, and petitioner's modest operations, the court held that an hourly rate of $40 (i.e., annual compensation of $83,200) represented reasonable compensation for the various services performed.

Relief for S Corporation & QSub Elections Without

Consolidated Late S Election Guidance (Rev. Proc. 2013-30)

Rev. Proc. 2013-30 consolidates and simplifies numerous prior IRS revenue procedures providing automatic and simplified relief for late entity and shareholder elections related to S corporations. It establishes a single, unified framework for requesting relief for late elections under Subchapter S and related provisions. The procedure also extends and modifies relief in certain situations that were previously governed by multiple separate rulings.

Consolidated Relief Coverage

This revenue procedure supersedes and replaces:

- Rev. Proc. 2003-43, 2004-48, and 2007-62 – Late S corporation elections, Electing Small Business Trust (ESBT) elections, Qualified Subchapter S Trust (QSST) elections, and Qualified Subchapter S Subsidiary (QSub) elections.
- Rev. Proc. 97-48 (Situation 1) – Relief for inadvertent late S elections (Situation 2 relief obsolete).
- Rev. Proc. 2004-49 (sections 4.01–4.02) – Late entity-classification elections intended to coincide with an S election (section 4.03 obsolete due to expired timeframe).

NOTE - By merging these into one uniform procedure, the IRS eliminated the need to cross-reference multiple documents and streamlined the process for obtaining late-election relief.

Elections Covered

Rev. Proc. 2013-30 provides the exclusive simplified methods for obtaining late-election relief for:
S Corporation Elections under IRC §1362(b)(5)

1. ESBT Elections under IRC §1361(e)(3)
2. QSST Elections under IRC §1361(d)(2)
3. QSub Elections under IRC §1361(b)(3)(B)(ii)**
4. Entity Classification Elections (Check-the-Box) under Treas. Reg. §301.7701-3(c) - when intended to take effect on the same date as the related S election

Eligibility and Relief Requirements

To qualify for relief:

- The taxpayer must have intended the election to be effective on a specific date but failed to timely file due to reasonable cause.
- The taxpayer must satisfy the general requirements in Section 4 (timely filing history, valid S-status intent, and reasonable cause statement).
- The taxpayer must also satisfy the specific requirements in Sections 5 through 7, depending on the type of late election sought.
- Relief is generally available within 3 years and 75 days after the intended effective date, although certain automatic-relief situations extend beyond that timeframe.

Procedural Guidance

- Relief is automatic when all requirements are met—no private-letter ruling or user fee is required.
- The procedure provides a standardized submission format (typically via Form 2553, Form 8869, or Form 8832) with an attached "Late Election Relief Statement."
- A flowchart accompanying the procedure assists taxpayers and practitioners in determining eligibility for automatic relief.

Relief for S Corporation & QSub Elections Without PLR (Rev. Proc. 2022-19

NOTE - Rev. Proc. 2022-19 is effective October 11, 2022 and includes a transition rule for pending PLRs. This procedure amplifies Rev. Proc. 2013-30.

Background

This revenue procedure describes procedures that allow S corporations and their shareholders to resolve frequently encountered issues with certainty and often without requesting a private letter ruling (PLR). The IRS identified these issues as not affecting the validity or continuation of a corporation's election to be treated as an S corporation or to treat its corporate subsidiary as a qualified subchapter S subsidiary (QSub). The six key areas covered by this guidance are:

1. Agreements and arrangements with no principal purpose to circumvent one class of stock requirement
2. Governing provisions that provide for identical distribution and liquidation rights
3. Procedures for addressing missing shareholder consents, errors with regard to a permitted year, missing officer's signature, and other inadvertent errors and omissions
4. Procedures for verifying S elections or QSub elections
5. Procedures for addressing a Federal income tax return filing inconsistent with an S election or a QSub election
6. Procedures for retroactively correcting one or more non-identical governing provisions

S Corporation Shareholders Stock & Debt Basis

Purpose of a Shareholder's Stock Basis

The main reasons a shareholder must calculate their stock basis is to determine:

1. Any gain or loss on the sale of their stock (i.e., sales price less stock basis = gain or loss);
2. If any distributions from the S-corporation are taxable (i.e., distributions in excess of stock basis are taxed as capital gains); AND
3. If the shareholder may claim any losses or deductions allocated to them on their Form 1120S Schedule K-1 (i.e., losses and deductions are allowed to the extent of the shareholder's stock and debt basis).

Three Loss Limitations

Three separate limits apply to a shareholder's distributive share of loss and deductions from a S corporation. The limits determine the amount of loss each shareholder can deduct on his or her own income tax return. These limits are applied in the following order:

1. **Shareholder's stock basis & debt basis (§1366)**

> **NOTE –** Per schedule E instructions: "If you are claiming a deduction for your share of an aggregate loss (or you receive a distribution, dispose of stock, or receive a loan repayment from an S corporation), check the box on the appropriate line in Part II, column (e), and attach *Form 7203* to you return."

2. **At risk rules (§465)**

> **NOTE –** If a taxpayer is subject to the at-risk rules, use the *Form 6198 – At-Risk Limitations* to figure the amount of any deductible losses.

3. **Any other limitations at the individual level on the Form 1040 including**:
   a. Passive activity losses (§469),
   b. Capital losses,
   c. Charitable contributions,
   d. Investment interest expense,
   e. Portfolio deductions, and
   f. §179 expense.

Limitation on Losses & Deductions (§1.1366-2(a)(1))

The aggregate amount of losses and deductions taken into account by a shareholder for any taxable year of an S corporation cannot exceed the sum of:

1. The adjusted basis of the shareholder's stock in the corporation (i.e., **Stock Basis**); and
2. The adjusted basis of any indebtedness of the corporation to the shareholder (i.e., **Debt Basis**).

Carryover of Disallowed Losses & Deductions (§1.1366-2(a)(3))

A shareholder's aggregate amount of losses and deductions in excess of the shareholder's stock and debt basis is not allowed for the taxable year. However, any disallowed loss or deduction retains its character and is treated as incurred by the corporation in the corporation's first succeeding taxable year, and subsequent taxable years, with respect to the shareholder.

Basis Ordering Rules (§1.1367-1(f))

For any taxable year of a corporation beginning on or after August 18, 1998, the adjustments to basis of stock and indebtedness are made in the following order:

1. Increase for taxable and non-taxable income;
2. Decreased for property distributions (including cash) by the corporation;
3. Decreased for non-capital, nondeductible expenses, and the oil and gas depletion deductions; and
4. Decreased for deductible losses or deductions.

NOTE – The basis decrease by reason of a charitable contribution of property shall be the amount equal to the shareholder's pro rata share of the adjusted basis of such property (not fair market value).

Election to Modify the Ordering Rules (§1.1367-1(g))

A shareholder may elect to decrease basis by deductible losses or deductions prior to decreasing basis by non-capital, nondeductible expenses, and the oil and gas depletion deductions. As a result, after 1998 the adjustments to basis of stock and indebtedness are made in the following order:

1. Increase for taxable and non-taxable income;
2. Decreased for property distributions (including cash) by the corporation;
3. Decreased for deductible losses or deductions; and
4. Decreased for non-capital, nondeductible expenses, and the oil and gas depletion deductions.

Election Due Date

A shareholder makes the election under this paragraph by attaching a statement to the shareholder's timely filed original or amended return that states that the shareholder agrees to the carryover rule of the preceding sentence.

Irrevocable Election

Once a shareholder makes an election under this paragraph with respect to an S corporation, the shareholder must continue to use the rules of this paragraph for that S corporation in future taxable years unless the shareholder receives the permission of the Commissioner.

Final Regulations - Basis of indebtedness (§1.1366-2(a)(2))

EFFECTIVE DATE – The final regulations apply to indebtedness between an S corporation and its shareholder resulting from any transaction occurring on or after July 23, 2014.

General rule

The term basis of any indebtedness of the S corporation to the shareholder means the shareholder's adjusted basis (as defined in §1.1011-1 and as specifically provided in §1367(b)(2)) in any bona fide indebtedness of the S corporation that runs directly to the shareholder. Whether indebtedness is bona fide indebtedness to a shareholder is determined under general Federal tax principles and depends upon all of the facts and circumstances.

Guarantees

A shareholder does not obtain basis of indebtedness in the S corporation merely by guaranteeing a loan or acting as a surety, accommodation party, or in any similar capacity relating to a loan. When a shareholder makes a payment on bona fide indebtedness of the S corporation for which the shareholder has acted as guarantor or in a similar capacity, then the shareholder may increase the shareholder's basis of indebtedness to the extent of that payment.

S Corporation & Partnership Fringe Benefits Issues

Tax Treatment of Benefits Paid to Employees

Certain fringe benefits are excluded from an employee's gross income under §132 for in income tax purposes, income tax withholding and Federal Insurance Contributions Act (FICA) and Federal Unemployment Tax Act (FUTA) taxes.

NOTE – The advantage to the employer is that the fringe benefit is deductible and not subject to FICA or FUTA taxes. The advantage to the employee is that the fringe benefit is not includible in income.

If not specifically excluded under §132, the fringe benefit is includible in the recipient's gross income (under §61 and §83) and is includible in wages for withholding and other employment tax purposes. The amount includable in income is the excess of its fair market value over any amount paid by the employee for the benefit.

NOTE – This rule applies to employees of all business entities as well as shareholder's of C corporations.

Nondiscrimination Rules

In general, if an employer discriminates in favor of a highly compensated or key employee, the fringe benefit paid to the highly compensated or key employee must treated as compensation to that person.

OBSERVATION – If a C corporation does not discriminate in favor or a highly compensated or key employee with respect to fringe benefits, then all of the benefits paid by the C corporation will be excluded from the shareholder's compensation.

Fringe Benefits Paid to Partners in a Partnership

In general, a partner is not considered to be an employee with respect to certain fringe benefits. Thus, these fringe benefit paid to a partner in a partnership are not eligible for an exclusion from income UNLESS specifically excluded otherwise (i.e., the law treats a partner as an employee).

NOTE – If the law with respect to a particular fringe benefit treats a partner as an employee of the company, then the fringe benefit is not taxable to the partner. However, if the law with respect to a particular fringe benefit does NOT treat a partner as an employee of the company, then the fringe benefit is taxable to the partner as a guaranteed payment.

Fringe Benefits Paid to 2% S Corporation Shareholders

Partnership Rules Apply for Fringe Benefits Paid to 2% Shareholders (§1372(a))

For purposes of applying the provisions which relate to employee fringe benefits:

1. The S corporation shall be treated as a partnership AND
2. Any 2% shareholder of the S corporation shall be treated as a partner of such partnership.

NOTE – Thus, any fringe benefit paid on behalf of a 2% shareholder will be treated as compensation unless specifically excluded by the law. This follows the partnership rules with respect to fringe benefits.

2% Shareholder Defined (§1372(b))

The term "2% shareholder" means any person who owns directly or indirectly through family attributions rules under §318 on any day during the taxable year of the S corporation:

1. More than 2% of the outstanding stock of such corporation OR
2. Stock possessing more than 2% of the total combined voting power of all stock of such corporation.

Constructive Ownership of Stock (§318)(a)(1)(A))

An individual shall be considered as owning the stock owned, directly or indirectly, by or for his/her:

1. Spouse (other than a spouse who is legally separated),
2. Children,
3. Grandchildren, and
4. Parents.

Taxable Fringe Benefits (Treated as Compensation)

If the law does not treat a 2% shareholder or partner as an employee of the company with respect to a particular fringe benefit, then that benefit must be treated as compensation to the recipient (i.e., W-2 income for a 2% shareholder and guaranteed payment for a partner). The following are examples of fringe benefits that are treated as compensation to more than 2% shareholders and partners:

1. Premiums for accident and health insurance coverage for the shareholder, spouse, dependents & their children under age 27 (§106). Also see Rev. Rul. 91-26 & Notice 2008-1;
2. Medical reimbursement plans (MRP) for the shareholder, spouse, dependents & their children under age 27 (§105);
3. Disability insurance coverage (§105);
4. Qualified employee achievement award (§74(c));
5. Group term life insurance coverage of up to $50,000 per shareholder (§79);
6. Meals or lodging furnished for the convenience of the company (§119);
7. Cafeteria benefit plan (§125; Prop. Reg. §1.125-1(g)(2));
8. Qualified transportation fringes (§132(f));
9. Qualified moving expense reimbursements (§132(g));
10. Qualified adoption assistance program (§137(c)(2) & IRS Notice 97-9); and
11. Health savings accounts (HSAs) (§223 & Notice 2005-8).

Self-Employed Health Insurance Premiums – Deduction or Distribution (Rev. Rul. 91-26)

Premiums for health insurance paid by a partnership on behalf of a partner, for services as a partner, are treated as guaranteed payments. The partnership can deduct the payments as a business expense, and the partner must include them in gross income. However, if the partnership accounts for insurance paid for a partner as a reduction in distributions to the partner, the partnership cannot deduct the premiums.

Health Insurance FICA Tax Issue for 2% Shareholders (Announcement 92-16)

§3121(a)(2)(B) excludes from wages certain amounts paid by an employer to or on behalf of an employee (including amounts paid by an employer for insurance, annuities, or into a fund) for medical and hospitalization expenses in connection with sickness or accident disability. For this exclusion to apply, the payments must be made under a plan or system for employees and their dependents generally or for a class (or classes) of employees and their dependents.

NOTE – Whether amounts of this type are actually subject to social security or Medicare tax depends on whether in the particular case the taxpayer satisfies the requirements for the exclusion.

If the requirements for the exclusion under §3121(a)(2)(B) are satisfied, amounts paid by an S corporation for accident and health insurance covering a 2%-shareholder-employee are not wages for social security and Medicare tax purposes, even though the amounts must be included in wages for income tax withholding purposes on the 2% shareholder-employee's Form W-2.

CAUTION – If the requirements for an exclusion are not satisfied, amounts paid by an S corporation for accident and health insurance covering a 2% shareholder-employee must be included in wages for social security and Medicare tax purposes, as well as for income tax withholding purposes, and reported in the appropriate boxes on the 2% shareholder-employee's Form W-2.

Non-Taxable Fringe Benefits

If the law treats a 2% shareholder or partner as an employee of the company with respect to a particular fringe benefit, then that benefit is excludible from the recipient's income. The following are examples of fringe benefits that are treated as tax-free to more than 2% shareholders:

1. Qualified educational assistance program (§127);
2. Qualified dependent care assistance program (§129);
3. No-additional-cost services (§132(b) and §1.132-1(b)(1));
4. Qualified employee discounts (§132(c) and §1.132-1(b)(1));
5. Working condition fringe benefits (§132(d) and §1.132-1(b)(2)(ii));
6. De minimis fringe benefits (§132(e) and §1.132-1(b)(4));
7. On-premises athletic facilities (§132(j) and §1.132-1(b)(3)); and
8. Qualified retirement planning services (§132(m)).

2% S Corporation's Shareholder Health Insurance Deduction (Notice 2008-1)

Requirements for Deduction on Form 1040 (Schedule 1)

A 2% shareholder-employee in an S corporation, who otherwise meets the requirements of §162(l), is eligible for the deduction if the plan providing medical care coverage for the 2% shareholder-employee is established by the S corporation. A plan providing medical care coverage for the 2% shareholder-employee in an S corporation is established by the S corporation if:

1. the S corporation makes the premium payments for the accident and health insurance policy covering the 2% shareholder-employee (and his or her spouse or dependents, if applicable) in the current taxable year;

   OR

2. the 2% shareholder makes the premium payments and furnishes proof of premium payment to the S corporation and then the S corporation reimburses the 2% shareholder-employee for the premium payments in the current taxable year.

NOTE 1 – If the accident and health insurance premiums are not paid or reimbursed by the S corporation and included in the 2% shareholder-employee's gross income, a plan providing medical care coverage for the 2% shareholder-employee is not established by the S corporation and the 2% shareholder-employee in an S corporation is NOT allowed the deduction under §162(l).

NOTE 2 – In order for the 2% shareholder-employee to deduct the amount of the accident and health insurance premiums, the S corporation must report the accident and health insurance premiums paid or reimbursed as wages on the 2% shareholder-employee's Form W-2 in that same year. In addition, the shareholder must report the premium payments or reimbursements from the S corporation as gross income on his or her Form 1040, U.S. Individual Income Tax Return.

2 - 71

2% S-Corp Shareholder Family Member Health Insurance (CCA 201912001)

Facts

An individual owns 100% of an S corporation, which employs the individual's family member. The family member is considered to be a 2% shareholder pursuant to the attribution of ownership rules under §318. The S corporation provides a group health plan for all employees, and the amounts paid by the S corporation under such group health plan are included in the family member's gross income.

Issue

Whether an individual who is a 2% shareholder of an S corporation pursuant to the attribution of ownership rules under IRC §318 is entitled to the deduction under §162(l) for amounts that are paid by the S corporation under a group health plan for all employees and included in the individual's gross income, if the individual otherwise meets the requirements of §162(l).

Conclusion

An individual who is a 2% shareholder of an S corporation pursuant to the attribution of ownership rules under §318 is entitled to the deduction under §162(l) for amounts that are paid by the S corporation under a group health plan for all employees and included in the individual's gross income, if the individual otherwise meets the requirements of §162(l).

Schedules K-2 & K-3 - Reporting of International Tax Matters by Pass-Through Entities

Purpose of the New Schedules K-2 & K-3 (Forms 1065, 1120-S, and 8865)

The new schedules K-2 and K-3 were created to provide consistency in the reporting to partners and shareholders. Prior versions of schedules K and K-1 did not require any specific format to provide international information, resulting in what could be a confusing array of statements attached to the schedules K and K-1. The new schedules K-2 and K-3 provide greater certainty and consistency, helping partners and shareholders to voluntarily comply with their filing and reporting obligations. The greater certainty also enables the IRS to verify that partnership and S corporation items are properly reported on partners' and shareholders' returns. This should reduce the burden on both taxpayers and the IRS by reducing unnecessary inquiries and examinations that may arise due to inconsistent reporting of partnership and S corporation items.

Links to Forms & Additional Guidance

- Form 1065 Schedule K-2 - Partners' Distributive Share Items—International
- Form 1065 Schedule K-3 - Partner's Share of Income, Deductions, Credits, etc.—International
- Partnership Instructions for Schedules K-2 and K-3 (Form 1065)
- Form 1120-S Schedule K-2 - Shareholders' Pro Rata Share Items—International
- Form 1120-S Schedule K-3 - Shareholder's Share of Income, Deductions, Credits, etc.—International Partnerships
- S Corporation Instructions for Schedules K-2 and K-3 (Form 1120-S)
- IRS Draft Tax Forms

Overview of Adjustments to Partner's Outside Basis (§705(a))

The partner's initial or prior year basis will be adjusted at the end of the year for their distributive share of the following partnership items.

Increases to Basis

1. Contributions
    a. Cash
    b. Property = adjusted basis plus any gain recognized,
    c. Services taxable to the partner, and
    d. Liabilities the partner assumes and increases in the partner's share of partnership liabilities.
2. Taxable income of the partnership including capital gains,
3. Tax-exempt income of the partnership, and
4. The excess of the deductions for depletion over the basis of the depletable property, unless the property is an oil or gas property the basis of which has been allocated to partners under §613A(c)(7)(D).

Decreases to Basis (Cannot bring basis below zero)

1. Distributions
    a. Non-liquidating distributions of cash,
    b. Non-liquidating distributions of other property,
    c. Liabilities of the partner assumed by the partnership and decreases in the partner's share of partnership liabilities.

    AND
2. The sum of the partner's distributive share for the taxable year and prior taxable years of:
    a. Non-deductible partnership expenses which are not capital expenditures,
    b. Deductible partnership expenses and losses (including capital losses), and
    c. The partner's deduction for depletion allowable for any partnership oil and gas property to the extent the deduction does not exceed the proportionate share of adjusted basis of the property allocated to the partner under §613A(c)(7)(D).

NOTE 1 – Rev. Rul. 66-94 states that distributions are taken into consideration before losses in computing a partner's adjusted basis for his partnership interest under §705(a).

NOTE 2 – If the losses & deductions (i.e., items 2a through 2c) exceed the partner's basis, the allowed losses must be allocated pro-rata to the partner's distributive share of each such loss.

Basis of partner's interest - property donated by partnership (Rev. Rul. 96-11)

If a partnership makes a charitable contribution of property, the basis of each partner's interest in the partnership is decreased (but not below zero) by the partner's share of the partnership's basis in the property contributed.

Effect of Liabilities on a Partner's Basis (§752)

Increase in Partner's Liabilities (§752(a) & §1.752-1(b))

Any increase in a partner's share of partnership liabilities, or any increase in a partner's individual liabilities by reason of the partner's assumption of partnership liabilities, is treated as a contribution of money by that partner to the partnership.

Decrease in Partner's Liabilities (§752(b) & §1.752-1(c))
Any decrease in a partner's share of partnership liabilities, or any decrease in a partner's individual liabilities by reason of the partnership's assumption of the individual liabilities of the partner, is treated as a distribution of money by the partnership to that partner.

Definitions (§1.752-1(a))

Recourse Liability Defined (§1.752-1(a)(1))
A partner's share of a recourse partnership liability equals the portion of that liability, if any, for which the partner or related person bears the economic risk of loss.

NOTE – The determination of the extent to which a partner bears the economic risk of loss for a partnership liability is made under regulation §1.752-2 using the constructive liquidation.

Nonrecourse Liability Defined (§1.752-1(a)(2))
A partnership liability is a nonrecourse liability to the extent that no partner or related person bears economic risk of loss for that liability under §1.752-2. Under Reg. §1.752-3, a partner's share of nonrecourse liabilities of a partnership equals the sum of:

1. The partner's share of partnership minimum gain determined in accordance with the rules of §704(b) and the regulations thereunder;

2. The amount of any taxable gain that would be allocated to the partner under §704(c) (or in the same manner as §704(c) in connection with a revaluation of partnership property) if the partnership disposed of (in a taxable transaction) all partnership property subject to one or more nonrecourse liabilities of the partnership in full satisfaction of the liabilities and for no other consideration;

   AND

3. The partner's share of the excess nonrecourse liabilities (those not allocated under (1) and (2) above) of the partnership as determined in accordance with the partner's share of partnership profits.

Related Person (§1.752-1(a)(3))
Related person means a person having a relationship to a partner that is described in §1.752-4(b).

Liability Defined (§1.752-1(a)(4)(i))
An obligation is a liability for purposes of §752 and the regulations only if, when, and to the extent that incurring the obligation:

1. Creates or increases the basis of any of the obligor's assets (including cash);
2. Gives rise to an immediate deduction to the obligor; or
3. Gives rise to an expense that is not deductible in computing the obligor's taxable income and is not properly chargeable to capital.

Rev. Rul. 88-77 Holding – For purposes of computing the adjusted basis of a partner's interest in a cash basis partnership, accrued but unpaid expenses and accounts payable are not liabilities of a partnership" or "partnership liabilities" within the meaning of IRC §752.

Obligation Defined (§1.752-1(a)(4)(ii))
An obligation is any fixed or contingent obligation to make payment without regard to whether the obligation is otherwise taken into account for purposes of the Internal Revenue Code. Obligations include, but are not limited to, debt obligations, environmental obligations, tort obligations, contract obligations, pension obligations, obligations under a short sale, and obligations under derivative financial instruments such as options, forward contracts, futures contracts, and swaps.

§754 Election & Revocation

§754 Election Background

An election under §754 allows an adjustment to the basis of partnership property when partnership interests are transferred (i.e. via sale or death) and when the partnership makes a distribution of property. If a partnership files an election under §754, it triggers the operational rules of both:

1. §743(b) in the case of a transfer of a partnership interest; and
2. §734(b) in the case of a distribution of property.

NOTE - These adjustments can only be made if the partnership has made an election under §754.

Written Statement

An election under §754 must be made in a written statement filed with the partnership return for the taxable year during which the distribution or transfer occurs. The statement must:

1. Set forth the name and address of the partnership making the election,
2. Be signed by any one of the partners AND
3. Contain a declaration that the partnership elects under §754 to apply the provisions of §734(b) and §743(b).

NOTE – The IRS issued final regulations (TD 9963) under §1.754-1 (on August 5, 2022) removing the signature requirement under number 2 above for timely filed partnership returns.

Revoking the Section 754 Election (Form 15254)

A partnership wishing to revoke the election should file a request using newly published ***Form 15254, Request for Section 754 Revocation*** no later than 30 days after the close of the partnership year for which the revocation is intended to take effect. The request must be signed by one of the partners.

NOTE – The IRS has FAQs for the §754 election and revocation at their website.

Must state reason for revocation

Treasury Regulation section 1.754-1(c) provides examples of situations which may warrant approving an application for revocation. These examples include situations where the §754 election results in an administrative burden, such as:

1. a change in the nature of the partnership's business,
2. a substantial increase in the partnership's assets,
3. a change in the character of the partnership's assets, or
4. an increased frequency of retirements or shifts of partnership interests.

CAUTION - No application for revocation of an election shall be approved when the purpose of the revocation is primarily to avoid a reduction in the basis of partnership assets upon a transfer or distribution.

Additional documentation must be submitted

The partnership must provide all information relating to the reasons for the revocation request and a statement of whether the election, if not revoked, would result in a reduction in the basis of the partnership's property under §734(b) or §743(b).

Form 8308 - Report of a Sale or Exchange of Certain Partnership Interests

Background

Generally, §6050K and §1.6050K-1 require a partnership with §751 property to provide information to each transferor and transferee that are parties to a sale or exchange of an interest in the partnership (or portion thereof) in which any money or other property received by a transferor from a transferee in exchange for all or part of the transferor's interest in the partnership is attributable to §751 property (i.e., §751(a) exchange). Section 1.6050K-1(a)(2) provides that partnerships are required to report each §751(a) exchange on Form 8308. Generally, §1.6050K-1(f)(1) provides that a partnership is required to file Form 8308 as an attachment to its Form 1065, U.S. Return of Partnership Income, for the taxable year of the partnership that includes the last day of the calendar year in which the §751(a) exchange took place. Form 8308 is due at the time for filing the partnership return, including extensions.

Deadline

In addition, §1.6050K-1(c)(1) provides that each partnership that is required to file a Form 8308 must furnish a statement to the transferor and transferee by the later of

1. January 31 of the year following the calendar year in which the §751(a) exchange occurred, or
2. 30 days after the partnership has received notice of the exchange as specified under §6050K and §1.6050K-1.

Form 8308

A partnership must use a copy of the completed Form 8308 - Report of a Sale or Exchange of Certain Partnership Interests as the required statement unless the Form 8308 contains information for more than one §751(a) exchange. Section 1.6050K-1(c)(1) provides that if the partnership does not use the Form 8308 as the required statement, the partnership must furnish a statement that includes the information required to be shown on the Form 8308 with respect to the §751(a) exchange to which the person to whom the statement is furnished is a party.

Penalties

§6722 imposes a penalty for failure to furnish correct payee statements on or before the required date, and for any failure to include all of the information required to be shown on the statement or the inclusion of incorrect information. For these purposes, payee statements include statements required to be furnished to transferors and transferees under §6050K. §6724 provides an exception to the imposition of a penalty under §6722 if it is shown that the failure is due to reasonable cause and not to willful neglect.

Relief Provided by (Notice 2025-2)

For §751(a) exchanges occurring in 2024, the IRS grants safe harbor from §6722 penalties (failure to furnish correct payee statements), if the partnership:

1. Timely furnishes Forms 8308 or equivalent copies of Parts I, II and III to the transferors and transferees by January 31, 2025 (or 30 days post-notice), and
2. Furnishes the complete Form 8308 (including Part IV) to those individuals by the partnership's Form 1065 due date (with extensions), or within 30 days of notice.

NOTE - IRS Notice 2024-19 provided late filing penalty relief for 2023 sales.

IRS Releases New Form 7217 - Partners Report of Property Distributed by a Partnership

Form 7217

Form 7217 - Partner's Report of Property Distributed by a Partnership is filed by any partner receiving a distribution of property from a partnership in a non-liquidating or liquidating distribution to report the basis of the distributed property, including any basis adjustment to such property as required by §732(a)(2) or (b).

Who Must File

File with your annual tax return a separate Form 7217 for each date during the tax year that you received distributed property subject to §732. If you received distributed properties subject to §732 on different days during the tax year, even if part of the same transaction, file a separate Form 7217 for each date that you received the properties. Do not file Form 7217 if the distribution consisted only of money or marketable securities treated as money under §731(c). Also, do not file Form 7217 for payments to you for services other than in your capacity as a partner under §707(a)(1) or for transfers that are treated as disguised sales under §707(a)(2)(B).

Example – Current (Nonliquidating) Partnership Distribution

Facts

Jim Beam has an outside basis in his partnership interest of $50,000. He receives a current (nonliquidating) distribution from the partnership consisting of:

Asset Distributed	Inside Basis	FMV
Cash	$35,000	$35,000
Accounts Receivable	$0	$30,000
Land	$40,000	$100,000

Assuming the accounts receivable is a proportionate distribution, so there are no §751 hot asset complications, and there is no §754 election in effect, Jim's outside basis would be zero after the distribution, he would not recognize any gain or loss and would take basis in the accounts receivable of $30,000 and land of $15,000 as follows:

	Tax basis	FMV	Basis of Asset Received
Beginning outside basis	$50,000		
1. Cash	(35,000)	$35,000	$35,000
	15,000		
2. Accounts receivable	(0)	30,000	0
	15,000		
3. Land	(40,000)	100,000	15,000 (40,000 – 25,000)
Ending basis	0		

Form **7217** (December 2024) Department of the Treasury Internal Revenue Service

Partner's Report of Property Distributed by a Partnership

Attach to your tax return.
Go to *www.irs.gov/Form7217* for instructions and the latest information.

OMB No. 1545-0123
Attachment Sequence No. **217**

Partner's name	Partner's TIN
Jim Beam	
Distributing partnership's name	Distributing partnership's EIN

Date property was distributed to partner

Part I **Aggregate Basis of Distributed Property on Distribution Date.** File a separate form for each date a partner received distributed property.

1	Was this distribution in complete liquidation of the partner's interest in the partnership?		☐ Yes ☑ No
2	Was any part of the distribution treated as a sale or exchange under section 751(b)?		☐ Yes ☑ No
3	Partnership's aggregate basis in distributed property (taking into account any basis adjustments under section 732(d), 734(b), or 743(b)) immediately before the distribution. This line should equal the total of Part II, line B, column (b)		$ 40,000
4	Adjusted basis of the partner's interest in the partnership immediately before the distribution		$ 50,000
5a	Cash received in the distribution	$ 35.000	
b	Fair market value of marketable securities (as defined in section 731(c)) received in the distribution	$	
c	Add lines 5a and 5b		$ 35,000
6	Enter the smaller of line 4 or line 5c		$ 35,000
7	Gain recognized. Subtract line 6 from line 5c. If zero, enter -0- and go to line 9		$ 0
8	Is U.S. tax required to be paid on the gain entered on line 7?		☑ Yes ☐ No
9	Partner's basis in partnership interest reduced by cash received in the distribution. Subtract line 5a from line 4. If zero or less, enter -0-. See instructions if you recognized gain under section 737 as a result of the distribution		$ 15,000
10	Aggregate basis to be allocated to the distributed property. For a non-liquidating distribution, enter the smaller of line 3 or line 9. For a liquidating distribution, enter the amount from line 9. Line 10 should equal the total of Part II, line B, column (e)		$ 15,000

For Paperwork Reduction Act Notice, see the Instructions for Form 1065. Cat. No. 94479B Form **7217** (12-2024)

Form 7217 (12-2024) Page **2**

Part II **Allocation of Basis of Distributed Property**

	(a) Description of distributed property (If applicable, include property code. See Pub. 946, Appendix B.)	(b) Partnership's basis in distributed property immediately before the distribution	(c) (i) 732(d)	(c) (ii) 732(f)	(c) (iii) 734(b)	(c) (iv) 743(b)	(c) (v) Reserved for future use	(d) FMV of distributed property	(e) Partner's basis in distributed property after application of section 732
1	Accounts receivable	$ 0	☑	☐	☐	☐	☐	$ 30,000	$ 0
2	Land	$ 40,000	☑	☐	☐	☐	☐	$ 100,000	$ 15,000
27		$	☐	☐	☐	☐	☐	$	$
28		$	☐	☐	☐	☐	☐	$	$
29		$	☐	☐	☐	☐	☐	$	$
30		$	☐	☐	☐	☐	☐	$	$
A	If applicable, enter any totals from any attached Parts II. See instructions	$						$	$
B	Totals for all items	$ 40,000						$ 130,000	$ 15,000

Form **7217** (12-2024)

Partnership Self-Employment Tax Issues

Net Earnings from Self-Employment (§1402(a))

The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss from any trade or business carried on by a partnership of which he is a member.

Rental Real Estate Exception (§1402(a)(1))

There shall be excluded rentals from real estate and from personal property leased with the real estate (including such rentals paid in crop shares, and including payments under section 1233(a)(2) of the Food Security Act of 1985 (16 U.S.C. 3833(a)(2)) to individuals receiving benefits under section 202 or 223 of the Social Security Act) together with the deductions attributable thereto, unless such rentals are received in the course of a trade or business as a real estate dealer …

Services rendered for occupants (§1.1402(a)-4(c)(2))

Payments for the use or occupancy of rooms or other space where services are also rendered to the occupant, such as for the use or occupancy of rooms or other quarters in hotels, boarding houses, or apartment houses furnishing hotel services, or in tourist camps or tourist homes, or payments for the use or occupancy of space in parking lots, warehouses, or storage garages, do not constitute rentals from real estate; consequently, such payments are included in determining net earnings from self-employment. Generally, services are considered rendered to the occupant if they are primarily for his convenience and are other than those usually or customarily rendered in connection with the rental of rooms or other space for occupancy only. The supplying of maid service, for example, constitutes such service; whereas the furnishing of heat and light, the cleaning of public entrances, exits, stairways and lobbies, the collection of trash, and so forth, are not considered as services rendered to the occupant.

Limited Partner Exception (§1402(a)(13))

IRC §1402(a)(13) provides that in computing gros income and deductions and such distributive share of partnership ordinary income or loss, there shall be excluded the distributive share of any item of income or loss of a limited partner, as such, other than guaranteed payments (described in §707(c)) to that partner for services actually rendered to or on behalf of the partnership to the extent that those payments are established to be in the nature of remuneration for those services.

Renkemeyer, Campbell & Weaver LLP (TC-2011)

The Tax Court ruled that three attorney partners were subject to self-employment tax on their distributive share of partnership income. The court also discussed the legislative history of §1402(a)(13) quoted above, and concluded that "The insight provided reveals that the intent of §1402(a)(13) was to ensure that individuals who merely invested in a partnership and who were not actively participating in the partnership's business operations (which was the archetype of limited partners at the time) would not receive credits toward Social Security coverage. The legislative history of §1402(a)(13) does not support a holding that Congress contemplated excluding partners who performed services for a partnership in their capacity as partners (i.e., acting in the manner of self-employed persons), from liability for self-employment taxes."

CCA 201436049

The IRS concluded that partners of a management company were not "limited partners" within the meaning of §1402(a)(13) and were subject to self-employment tax on their distributive shares from the management company.

CCA 201640014

The IRS concluded that the Franchisee, the Operating Manager, President, and Chief Executive Officer of a partnership which operates restaurants is not a "limited partner" within the meaning of §1402(a)(13) and is subject to self-employment tax on his distributive share from Partnership.

Castigliola (TC Memo 2017-62)

The Tax Court held that members of a PLLC were not treated as limited partners for self-employment tax purposes. All of the members testified that they participated equally in all decisions and had substantially identical relationships with the PLLC. There was no PLLC operating agreement or other evidence to suggest otherwise. Since at least one of the members must have occupied a role analogous to that of a general partner in a limited partnership, and because all of the members had the same rights and responsibilities, they must all have had positions analogous to those of general partners in a limited partnership. This conclusion was affirmed by the history of the PLLC: Before the members organized the PLLC, they operated as a general partnership; and there is no evidence that organizing as a PLLC was accompanied by any change in the way they managed the business.

Self-Employment Tax Treatment of Partners in a Partnership That Owns a Disregarded Entity - Final Regulation §301.7701-2 (TD 9869)

UPDATE – The Treasury finalized the Temporary regulations with no change effect July 2, 2019.

Reg. §301.7701-2(c)(2)(iv)(C) (2) applies to taxes imposed on self-employment income and states: Thus, an entity that is treated in the same manner as a sole proprietorship under §301.7701-2(a) (i.e., disregarded entity) is not treated as a corporation for purposes of employing its owner; instead, the entity is disregarded as an entity separate from its owner for this purpose and is not the employer of its owner. The owner will be subject to self-employment tax on self-employment income with respect to the entity's activities. Also, if a partnership is the owner of an entity that is disregarded as an entity separate from its owner for any purpose under §301.7701-2, the entity is not treated as a corporation for purposes of employing a partner of the partnership that owns the entity; instead, the entity is disregarded as an entity separate from the partnership for this purpose and is not the employer of any partner of the partnership that owns the entity. A partner of a partnership that owns an entity that is disregarded as an entity separate from its owner for any purpose under §301.7701-2 is subject to the same self-employment tax rules as a partner of a partnership that does not own an entity that is disregarded as an entity separate from its owner for any purpose under §301.7701-2.

Basis Loss Limitation and the At-Risk Loss Limitation Apply in Determining a General Partner's SE Tax (CCA 202009024)

Issue

Whether the basis loss limitation under §704(d) and the at-risk loss limitation under §465 apply to determining a general partner's net earnings from self-employment (NESE) under §1402 for Self-Employment Contributions Act (SECA) tax purposes.

Conclusion

Unless a specific exclusion applies under §1402(a) to the facts of a case, the basis loss limitation under §704(d) and the at-risk loss limitation under §465 apply in determining a general partner's NESE under §1402 for SECA tax purposes.

Functional Test to Deem Partners Limited 'In Name Only' (Soroban Capital Partners LP, TC Memo 2025-52).

NOTE - The Tax Court has once again used the functional test to determine that three partnership members were not limited partners based on their day-to-day functions, making them subject to self-employment (SE) tax.

- Soroban Capital Partners LP, a Delaware investment management limited partnership, allocated its ordinary business income to its general and limited partners during 2016 and 2017.
- It reported only the limited partners' guaranteed payments as self-employment income, excluding their distributive shares under §1402(a)(13).
- The IRS contested this, arguing that those partners were active participants despite their titles and therefore ineligible for the "limited partner" exclusion.
- Previously in Soroban (161 TC 310 (2023)), the court ruled that a **"functional analysis test"** is necessary to "determine whether a partner in a state law limited partnership is a 'limited partner'" under IRC Sec. 1402(a)(13).
- In 2022, the IRS issued Notices of Final Partnership Administrative Adjustment for tax years 2016 and 2017, claiming Soroban mischaracterized income allocated to three limited partners.
- The IRS's adjustments treated this income as SE net earnings, increasing Soroban's SE income for those years.
- On 05-28-25, the Tax Court sided with the IRS, finding that the partners were limited partners "in name only" and did not qualify for the §1402(a)(13) exception, noting the partners were essential to Soroban's operations and their earnings were not "of an investment nature."

NOTE - The Tax Court reaffirmed that the label assigned under state law isn't determinative for § 1402(a)(13). Instead, it applies a functional analysis—examining each partner's actual duties and impact on income generation.

Key Factors Considered

The court evaluated multiple aspects to gauge each partner's role:

1. **Income Generation**: The partners' judgment, skills, and decision-making were essential to Soroban's success.
2. **Management Authority**: They served on key committees and influenced personnel, trading, and operational choices.
3. **Time Commitment**: Each worked full-time roughly 2,300–2,500 hours annually.
4. **Public Profile**: They were marketed as indispensable "founders"—their presence was even central to key-man provisions.
5. **Capital Contributions**: Their personal capital investments were minimal compared to their income share, signaling compensation rather than investment returns.

Court's Ruling

The court concluded that although the partners held "limited partner" titles, their active involvement meant they did not qualify for the § 1402(a)(13) exemption. As a result, their distributive shares were includable in net earnings subject to self-employment tax.

Overview of Various Partnership Regulations Issued

Partnership Varying Interest Rules (Final Reg. §1.706-4)

Final Regulations Issued (TD 9728)

The IRS and Treasury Department issued final regulations regarding the determination of a partner's distributive share of partnership items of income, gain, loss, deduction, and credit when a partner's interest varies during a partnership taxable year. The final regulations also modify the existing regulations regarding the required taxable year of a partnership.

NOTE – In general, these regulations are effective on August 3, 2015.

Proposed Regulations Issued (REG-109370-10)

The IRS and Treasury Department also issued proposed regulations regarding the determination of a partner's distributive share of certain allocable cash basis items and items attributable to an interest in a lower-tier partnership during a partnership taxable year in which a partner's interest changes.

NOTE – The proposed regulations are effective for tax years beginning on or after the date they are finalized. However, publicly traded partnerships may rely on these proposed rules with respect to the treatment of the new extraordinary item relating to income that is subject to withholding.

Partner's share of recourse & nonrecourse liabilities & disguised sale regulations

- On October 5, 2016, the IRS issued temporary (TD 9788), final (TD 9787) and proposed (Reg-122855-15) regulations with guidance on partnership disguised sales under §707 and allocation of liabilities under §752.
- On 06-18-18, the IRS 1) withdrew the 2016 proposed regulations issued under §707, 2) removed the 2016 temporary regulations issued under §707, and 3) reinstated the prior rules under former Reg. §1.707-5(a)(2), as previously in effect. The 2016 proposed regulations under §752 and the 2016 final and temporary regulations regarding "bottom dollar" guarantees, still remain in effect.
- On October 4, 2019, the IRS issued final regulations (TD 9877) on when partnership liabilities are treated as recourse liabilities under §752 (i.e., **bottom dollar payment obligations**) and expanded them to certain obligations to restore a deficit balance in a partner's capital account.
- On October 4, 2019, the IRS issued final regulations (TD 9876) adopting the 2018 Proposed Regulations proposing to withdraw the §707 Temporary Regulations and reinstated the prior §707 regulations without change (except the applicability date).

Final Centralized Partnership Audit Regime Regulations (TD 9969)

On December 9, 2022, the IRS issued final centralized partnership audit regime regulations. The final regulations overall follow the November 2020 proposed regulations, with a few revisions made in response to public comments.

NOTE – Click here for IRS information on the BBA centralized partnership audit regime.

Business Entity Classification Issues

Background – Default Eligible Entity Classification

A business entity that is not classified as a corporation (i.e., **eligible entity**) can elect its classification for federal tax purposes. Unless the entity elects (on a Form 8832) otherwise, a domestic eligible entity by default is:

1. A partnership if it has two or more members; or
2. Disregarded as an entity separate from its owner if it has a single owner.

2 or More Owner Eligible Entity Options

A business entity with two or more members is classified for federal tax purposes as either a:

1. Partnership (by default) or
2. Corporation (by election on Form 8832 for a C corporation and Form 2553 for a S corporation).

One Owner Eligible Entity Options

A business entity with only one owner is classified as either a:

1. Disregarded entity (by default) or
2. Corporation (by election on Form 8832 for a C corporation and Form 2553 for a S corporation).

NOTE – If the entity is disregarded, its activities are treated in the same manner as a sole proprietorship, branch, or division of the owner.

Form 8832 Election

Form 8832 – *Entity Classification Elections* are necessary only when an eligible entity chooses to be classified initially as an entity other than its default classification or when an eligible entity chooses to change its classification. An entity whose classification is determined under the default classification retains that classification until the entity makes an election to change that classification.

NOTE – Rev. Proc. 2009-41 provides relief for filing a late election (Form 8832).

Form 2553 S Corporation Election

An entity must file *Form 2553* - *Election by a Small Business Corporation* if making an election under §1362(a) to be an S corporation. An eligible entity that timely files Form 2553 to elect classification as an S corporation and meets all other requirements to qualify as an S corporation is deemed to have made an election under Reg. §301.7701-3(c)(v) to be classified as an association taxable as a corporation.

Pass Through Entity (PTE) Income Tax Payments

Revenue Ruling 58-25

This ruling held that a Cincinnati, Ohio tax imposed upon and paid by a partnership on the net profits of the partnership's business conducted in Cincinnati was deductible in computing the taxable income or loss of the partnership. The ruling holds that "any tax imposed upon and paid by a partnership on the net profits of its business conducted in Cincinnati is deductible in computing the taxable income of the partnership and the partners are not precluded from claiming the standard deduction." Thus, the partners' distributive shares of the net profits tax were not separately stated and the partners' distributive shares of the partnership's non-separately stated income or loss, which reflects a deduction for the tax paid by the partnership, could be taken into account by the partners in computing adjusted gross income under §62, not as itemized deductions.

Notice 2020-75

This notice announces that the Treasury Department) and the IRS intend to issue proposed regulations to clarify that State and local income taxes imposed on and paid by a partnership or an S corporation on its income are allowed as a deduction by the partnership or S corporation in computing its non-separately stated taxable income or loss for the taxable year of payment.

Purpose and scope

The Treasury Department and the IRS intend to issue proposed regulations to provide certainty to individual owners of partnerships and S corporations in calculating their SALT deduction limitations. Based on the statutory and administrative authorities described in section 2 of this notice, the forthcoming proposed regulations will clarify that Specified Income Tax Payments are deductible by partnerships and S corporations in computing their non-separately stated income or loss.

Definition of Specified Income Tax Payment

The term "Specified Income Tax Payment" means any amount paid by a partnership or an S corporation to a State, a political subdivision of a State, or the District of Columbia (Domestic Jurisdiction) to satisfy its liability for income taxes imposed by the Domestic Jurisdiction on the partnership or the S corporation. This definition does not include income taxes imposed by U.S. territories or their political subdivisions. Thus, this definition solely includes income taxes described in §164(b)(2) for which a deduction by a partnership is not disallowed under §703(a)(2)(B), and such income taxes for which a deduction by an S corporation is not disallowed under §1363(b)(2). For this purpose, a Specified Income Tax Payment includes any amount paid by a partnership or an S corporation to a Domestic Jurisdiction pursuant to a direct imposition of income tax by the Domestic Jurisdiction on the partnership or S corporation, without regard to whether the imposition of and liability for the income tax is the result of an election by the entity or whether the partners or shareholders receive a partial or full deduction, exclusion, credit, or other tax benefit that is based on their share of the amount paid by the partnership or S corporation to satisfy its income tax liability under the Domestic Jurisdiction's tax law and which reduces the partners' or shareholders' own individual income tax liabilities under the Domestic Jurisdiction's tax law.

Deductibility of Specified Income Tax Payments

If a partnership or an S corporation makes a Specified Income Tax Payment during a taxable year, the partnership or S corporation is allowed a deduction for the Specified Income Tax Payment in computing its taxable income for the taxable year in which the payment is made.

Specified Income Tax Payments not separately taken into account

Any Specified Income Tax Payment made by a partnership or an S corporation during a taxable year does not constitute an item of deduction that a partner or an S corporation shareholder takes into account separately under §702 or §1366 in determining the partner's or S corporation shareholder's own Federal income tax liability for the taxable year. Instead, Specified Income Tax Payments will be reflected in a partner's or an S corporation shareholder's distributive or pro-rata share of non-separately stated income or loss reported on a Schedule K-1 (or similar form).

Specified Income Tax Payments not taken into account for SALT deduction limitation

Any Specified Income Tax Payment made by a partnership or an S corporation is not taken into account in applying the SALT deduction limitation to any individual who is a partner in the partnership or a shareholder of the S corporation.

Applicable Date

The proposed regulations will apply to Specified Income Tax Payments made on or after November 9, 2020. The proposed regulations will also permit taxpayers to apply the rules in a taxable year of the partnership or S corporation ending after December 31, 2017, and made before November 9, 2020, provided that the Specified Income Tax Payment is made to satisfy the liability for income tax imposed on the partnership or S corporation pursuant to a law enacted prior to November 9, 2020. Prior to the issuance of the proposed regulations, taxpayers may rely on the provisions of this notice with respect to Specified Income Tax Payments.

NOTE – Click here for AICPA State & Local Tax Advocacy Resources.

Federal Income Tax Issues

There are numerous federal income tax issues to consider, such as:

- In which tax year can an electing PTE deduct the state taxes under federal tax rules?
- Is an owner's state tax refund attributable to the PTE tax credit considered taxable income (and if so, to what extent)?
- How is the state tax expense of an investment partnership treated? Is the PTE tax expense treated as a §212 investment expense subject to applicable limitations on deductibility?
- Can a partnership specially allocate the PTE's state tax expense only to those partners whose income was included in the PTE's state tax base? Does the partnership operating agreement need to be amended to comply with the substantial economic effect rules?

State Income Tax Issues

- When must the election be made?
- Is the election binding, made annually and/or revocable?
- How do you make the election?
- Who is authorized to make the election on behalf of the PTE?
- Can tiered partnerships or PTEs with non-individual members make the election?
- Are electing PTEs still required to comply with withholding or composite requirements?
- Are nonresident members of electing PTEs still required to file returns?
- What is the tax rate?
- What is the electing PTE's tax base?
- How do members of the electing PTE report their share of income?
- How do members of the electing PTE calculate their credit?
- Can non-individual members take a credit? If so, is it refundable?
- Are non-residents allowed to take an "other state tax credit" on their resident state income tax return for elective PTE taxes paid in another state?

Depreciation

Real Property Depreciation

Real Estate – Recovery Periods (§168(e)(2))

Residential Real Estate – 27 ½ Years

The term "residential rental property" means any building or structure if 80% or more of the gross rental income from such building or structure for the taxable year is rental income from dwelling units. The term "dwelling unit" means a house or apartment used to provide living accommodations in a building or structure, but does not include a unit in a hotel, motel, or other establishment more than:

1. ½ of the units which are used on a transient basis AND
2. if any portion of the building or structure is occupied by the taxpayer, the gross rental income from such building or structure includes the rental value of the portion so occupied.

NOTE 1 – Residential real property is depreciated over 27.5 years using S/L depreciation.

NOTE 2 – The alternative depreciation system (ADS) recovery period is 30 years for residential real property placed in service by the taxpayer after December 31, 2017, and is 40 years for property placed in service by the taxpayer before January 1, 2018.

Nonresidential Real Property – 39 Years

The term "nonresidential real property" means §1250 property that is NOT:

1. residential rental property AND
2. property with a class life of less than 27.5 years.

NOTE 1 – Non-residential real property is depreciated over 39 years using S/L depreciation.

NOTE 2 – The ADS recovery period is 40 years for non-residential real property.

Optional 30-year ADS depreciation table

Rev. Proc 2019-08 provides and optional depreciation table for residential rental property placed in service by the taxpayer after December 31, 2017, and depreciated by the taxpayer under the ADS of §168(g) using the straight-line method, a 30-year recovery period, and the mid-month convention.

Year	Month placed in service											
	1	2	3	4	5	6	7	8	9	10	11	12
1	3.204%	2.926%	2.649%	2.371%	2.093%	1.815%	1.528%	1.250%	0.972%	0.694%	0.417%	0.139%
2 - 30	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%	3.333%
31	0.139%	0.417%	0.694%	0.972%	1.250%	1.528%	1.815%	2.093%	2.371%	2.649%	2.926%	3.204%

Depreciation of Leasehold Improvements

Depreciation allowances for improvements made on leased property are determined under MACRS, even if the MACRS recovery period assigned to the property is longer than the term of the lease (i.e., they are depreciated over the property life NOT the lease life). This rule applies regardless of whether the lessor or the lessee places the leasehold improvements in service. If a leasehold improvement constitutes an addition or improvement to nonresidential real property already placed in service, the improvement is depreciated using the straight-line method over a 39-year recovery period, beginning in the month the addition or improvement was placed in service. For residential improvements are depreciated over 27 ½ -years.

Treatment of Dispositions of Leasehold Improvements
A lessor of leased property that disposes of a leasehold improvement that was made by the lessor for the lessee of the property may take the adjusted basis of the improvement into account for purposes of determining gain or loss if the improvement is irrevocably disposed of or abandoned by the lessor at the termination of the lease.

NOTE – This rule conforms the treatment of lessors and lessees with respect to leasehold improvements disposed of at the end of a term of lease.

Leasehold improvements placed in service prior to 2018
A 15-year recovery period applied to the following placed in service after December 31, 2005 and prior to January 1, 2018:
1. qualified leasehold improvement,
2. qualified restaurant and
3. qualified retail improvement property.

NOTE – §168(e)(6) was modified for property placed in service after December 31, 2017. The separate definitions of qualified leasehold improvement, qualified restaurant, and qualified retail improvement property were eliminated and replaced with a new uniform definition for qualified improvement property.

Qualified Improvement Property – 15-Year Recovery (§168(e)(6))
The term qualified improvement property means any improvement to an interior portion of a building which is nonresidential real property if such improvement is placed in service after the date such building was first placed in service.

Certain improvements not included
Such term shall not include any improvement for which the expenditure is attributable to:
1. the enlargement of the building,
2. any elevator or escalator, or
3. the internal structural framework of the building.

§179 Expense Limitations & Modifications

Maximum Expense Election (§179)

The maximum amount a taxpayer can elect to expense under §179 is limited to the year the property is purchased and placed in service.

If the taxable year begins in:	The maximum §179 is
2024	$1,220,000
2025	$2,500,000
2026	$2,560,000

Reduction in Limitation

The §179 expense limitation for any taxable year will be reduced dollar for dollar (but not below zero) by the amount by which the cost of §179 property placed in service during such taxable year exceeds the acquisition limitation below.

If the taxable year begins in:	The acquisition limit
2024	$3,050,000
2025	$4,000,000
2026	$4,090,000

2025 EXAMPLE – Mary purchases $4,200,000 of qualifying §179 property. Since her acquisitions of exceed the $4,000,000 threshold by $200,000 she must reduce the $2,500,000 maximum by this amount. Thus, she can elect to expense $2,300,000 under §179.

SUV §179 Expense Limitation (§179(a)(5))

The cost of any sport utility vehicle (SUV) for any taxable year that may be taken into account under §179 to shall not exceed the following amounts:

If the taxable year begins in:	SUV limit
2024	$30,500
2025	$31,300
2026	$32,000

SUV Defined

The term "sport utility vehicle" means any 4-wheeled vehicle:

1. which is primarily designed or which can be used to carry passengers over public streets, roads, or highways (except any vehicle operated exclusively on a rail or rails),
2. which is not subject to §280F and
3. which is rated at not more than 14,000 pounds gross vehicle weight.

NOTE – This affects the SUVs weighing more than 6,000 pounds unloaded gross vehicle weight and are not subject to the §280F auto depreciation limitations.

Excluded from the SUV Definition

For this purpose, a sport utility vehicle is defined to exclude any vehicle that:

1. Is designed for more than nine individuals in seating rearward of the driver's seat;
2. Is equipped with an open cargo area, or a covered box not readily accessible from the passenger compartment, of at least six feet in interior length; OR
3. Has an integral enclosure, fully enclosing the driver compartment and load carrying device, does not have seating rearward of the driver's seat, and has no body section protruding more than 30 inches ahead of the leading edge of the windshield.

179 Property Defined (§179(d)(1))

The term §179 property means property:

1. which is:
    a. tangible property to which §168 applies (i.e., of a character subject to an allowance for depreciation), or
    b. computer software (as defined in §197(e)(3)(B)) which is described in §197(e)(3)(A)(i) and to which §167 applies,
2. which is:
    a. §1245 property (as defined in §1245(a)(3)), or
    b. at the election of the taxpayer, qualified real property (as defined in §179(f)), and
3. which is acquired by purchase for use in the active conduct of a trade or business.

Certain property not eligible

§179 shall not include any property described in §50(b) (other than 50(b)(2)). This includes:

1. property used outside the U.S.,
2. property used by certain tax-exempt organizations and
3. property used by governmental units or foreign persons or entities.

UPDATE – After 2017, property used predominantly to furnish lodging or in connection with furnishing lodging is no longer excluded. This includes, e.g., beds and other furniture, refrigerators, ranges, and other equipment used in the living quarters of a lodging facility such as an apartment house, dormitory, or any other facility (or part of a facility) where sleeping accommodations are provided and let. See Treas. Reg. §1.48-1(h).

Qualified real property defined – After 2017

NOTE – The TCJA of 2017 modified §179(f) for property placed in service in tax years beginning after December 31, 2017. Prior to 2018, "qualified real property" meant qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property.

The term "qualified real property" means:

1. any qualified improvement property described in §168(e)(6), and
2. any of the following improvements to nonresidential real property placed in service after the date such property was first placed in service:
    a. Roofs
    b. Heating, ventilation, and air-conditioning property
    c. Fire protection and alarm systems
    d. Security systems.

Additional First Year Depreciation (AFYD)

UPDATE - The OBBB permanently sets bonus depreciation at 100%. It does not change the types of property eligible under §168(k), aside from updating certain date references. A limited transitional election allows taxpayers to apply the pre-OBBB phase-down rates (40% or 60%) for property placed in service during the first taxable year ending after January 19, 2025. This provision applies to property acquired after January 19, 2025.

Special allowance for certain property – Bonus Depreciation (§168(k))

Taxpayers are required to take an additional first year special depreciation allowance for certain qualified property (defined below). The allowance is a percentage of the property's depreciable basis.

NOTE – The deduction is calculated after any §179 deduction and before figuring any regular depreciation deduction.

	Bonus Depreciation Percentage	
Placed in service year	**Qualified Property**	**Longer Production Period Property* & Certain Aircraft**
September 28, 2017 to December 31, 2022	100%	100%
2023	80%	100%
2024	60%	80%
01-01-25 to 01-19-25	40%	60%
After 01-19-25	100%	100%

***NOTE -** An extension of the placed in-service date of one year was provided for certain property with a recovery period of 10 years or longer and certain transportation property (§168(k)(2)(B)) and certain aircraft (§168(k)(2)(C)).

Transition Rule

A transition rule provides that, for a taxpayer's first taxable year ending after January 1, 2025, the taxpayer may elect to apply:

- 40% bonus depreciation for standard qualified property
- 60% for longer production period property, certain aircraft and specified plants

Deduction allowed in computing AMT

Even though a taxpayer elects out of bonus depreciation for a class of property (after 2015), the property retains its status as "qualified property" under §168(k) and is not subject to AMT depreciation adjustment. Thus, for property placed in service after 2015, there is no AMT adjustment not just in the year of purchase but for the life of the asset.

NOTE – This rule did not apply to property placed in service before 2016 for which an election out was made.

Electing Out of Bonus Depreciation

If the taxpayer meets the requirements for bonus depreciation, then bonus depreciation is automatic. If the taxpayer does not wish to take bonus depreciation, then an election to not claim bonus depreciation must be made (§1.168(k)-1(e)(1)).

NOTE – This is just the opposite of §179. To get the §179 deduction, the taxpayer must elect §179.

This election out of bonus depreciation must be made by the due date (including extensions) of the tax return.

NOTE – The election out is NOT made on an asset-by-asset basis. It is made on an asset class basis (i.e., 5-year property, 7-year property, 10-year property, etc.).

Increase in AFYD for §280F Passenger Autos (§168(f)(2)(F))

The first-year depreciation deduction on passenger automobiles (§280F) is increased by $8,000 for vehicles that are qualifying for the AFYD.

Passenger Defined

The term "passenger automobile" includes any 4-wheeled vehicle that is:

1. Manufactured primarily for use on public streets, roads, and highways AND
2. Rated at 6,000 pounds gross vehicle weight or less.

NOTE – In the case of a truck or van, the above 6,000 pounds weight test is applied to the truck's or van's gross vehicle weight rather than its unloaded gross vehicle weight.

§280F Auto Depreciation Limits on Passenger Automobiles			
	2026	**2025**	**2024**
Auto Depreciation Limits			
First Year – not §168(k) qualified property		$12,200	$12,400
– is §168(k) qualified property		$20,200	$20,400
Second Year		$19,600	$19,800
Third Year		$11,800	$11,900
Fourth Year & Thereafter		$7,060	$7,160

Qualifying Property Acquired After to 09-27-17 (§168(k)(2))

Qualifying Property Defined – Property Acquired After to 09-27-17

The term "qualified property" means property:

1. the **property must be:**
   a. property to which MACRS applies with an applicable recovery period of 20 years or less;
   b. computer software other than computer software covered by §197;
   c. water utility property (as defined in §168(e)(5)); or
   d. which is a qualified film or television production (as defined in §181(d)) for which a deduction would have been allowable without regard to §181(a)(2) and (g) or this subsection, or
   e. which is a qualified live theatrical production (as defined in §181(e)) for which a deduction would have been allowable without regard to §181(a)(2) and (g) of such section or this subsection,
2. the original use of which begins with the taxpayer or the acquisition of which by the taxpayer meets the requirements of §168(k)(2)(E)(ii), and
3. which is placed in service by the taxpayer before January 1, 2027.

NOTE – Qualifying property also includes certain property having longer production periods (§168(k)(2)(B)) and certain aircraft (§168(k)(2)(C)). There are also special rules for certain plants bearing fruits and nuts (§168(k)(5)).

Acquisition requirements (§168(k)(2)(E)(ii))

An acquisition of property meets the requirements of this clause if:

1. such property was not used by the taxpayer at any time prior to such acquisition, and
2. the acquisition of such property meets the following §179 requirements:
   a. not acquired from a related person (§179(d)(2)(A)),
   b. the property is not acquired by one component member of a controlled group from another component member of the same controlled group (§179(d)(2)(B)),
   c. the basis of the property in the hands of the person acquiring it is not determined (i) in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired, or (ii) under §1014(a) (relating to property acquired from a decedent) (§179(d)(2)(C)), and
   d. the cost of property does not include so much of the basis of such property as is determined by reference to the basis of other property held at any time by the person acquiring such property (i.e., trade-in property) (§179(d)(3)).

Special Depreciation for Allowance for Qualified Production Property (§168(n))

General Rule (§168(n)(1))

In the case of any qualified production property of a taxpayer making an election under this subsection:

1. The depreciation deduction provided by §167(a) for the taxable year in which such property is placed in service shall include an allowance equal to 100% of the adjusted basis of the qualified production property, and
2. The adjusted basis of the qualified production property shall be reduced by the amount of such deduction before computing the amount otherwise allowable as a depreciation deduction under this chapter for such taxable year and any subsequent taxable year.

Qualified Production Property (§168(n)(2))

General rule (§168(n)(2)(A))

The term "qualified production property" means that portion of any nonresidential real property:

i. to which this section applies,
ii. which is used by the taxpayer as an integral part of a qualified production activity,
iii. which is placed in service in the United States or any possession of the United States,
iv. the original use of which commences with the taxpayer,
v. the construction of which begins after January 19, 2025, and before January 1, 2029,
vi. which is designated by the taxpayer in the election made under this subsection, and
vii. which is placed in service before January 1, 2031.

NOTE - For purposes of clause (ii), in the case of property with respect to which the taxpayer is a lessor, property used by a lessee shall not be considered to be used by the taxpayer as part of a qualified production activity.

Special Rule for Certain Property Not Previously Used in Qualified Production Activities (§168(n)(2)(B))

In the case of property acquired by the taxpayer during the period described in §168(n)(2)(A)(v), the requirements of clauses (iv) and (v) of subparagraph (A) shall be treated as satisfied if:

1. such property was not used in a qualified production activity (determined without regard to the second sentence of subparagraph (D)) by any person at any time during the period beginning on January 1, 2021, and ending on May 12, 2025,
2. such property was not used by the taxpayer at any time prior to such acquisition, and
3. the acquisition of such property meets the requirements of paragraphs (2)(A), (2)(B), (2)(C), and (3) of §179(d).

Written Binding Contracts - Such property shall be treated as acquired not later than the date on which the taxpayer enters into a written binding contract for such acquisition, and whether such property is acquired after such period, such property shall be treated as acquired not earlier than such date.

Exclusion of Office Space, Etc. (§168(n)(2)(C))

The term "qualified production property" shall not include that portion of any nonresidential real property which is used for offices, administrative services, lodging, parking, sales activities, research activities, software development or engineering activities, or other functions unrelated to the manufacturing, production, or refining of tangible personal property.

Qualified Production Activity (§168(n)(2)(D))
The term "qualified production activity" means the manufacturing, production, or refining of a qualified product. The activities of any taxpayer do not constitute manufacturing, production, or refining of a qualified product unless the activities of such taxpayer result in a substantial transformation of the property comprising the product.

Production (§168(n)(2)(E))
The term "production" shall not include activities other than agricultural production and chemical production.

Qualified Product (§168(n)(2)(F))
The term "qualified product" means any tangible personal property if such property is not a food or beverage prepared in the same building as a retail establishment in which such property is sold.

Syndication (§168(n)(2)(G))
For purposes of §168(n)(A)(iv), rules similar to the rules of §168(k)(2)(E)(iii) shall apply.
(H) Extension of Placed-in-Service Date Under Certain Circumstances. The Secretary may extend the date under subparagraph (A)(vii) with respect to any property that meets the requirements of clauses (i) through (vi) of subparagraph (A) if the Secretary determines that an act of God (as defined in section 101(1) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980) prevents the taxpayer from placing such property in service before such date.

Deduction Allowed in Computing Minimum Tax (§168(n)(3))
For purposes of determining alternative minimum taxable income under §55, the deduction under §167 for qualified production property shall be determined under this section without regard to any adjustment under §56.

Coordination with Certain Other Provisions (§168(n)(4))

Other Special Depreciation Allowances
For purposes of §168(k)(7) (election to accelerate or forgo bonus depreciation), §168(l)(3)(D) (election relating to qualified reuse and recycling property), and §168(m)(2)(B)(iii) (election for qualified disaster assistance property):

1. qualified production property shall be treated as a separate class of property, and
2. the taxpayer shall be treated as having made an election under such subsections with respect to such class.

Alternative Depreciation Property
The term "qualified production property" shall not include any property to which the alternative depreciation system under §168(g) applies. For purposes of §168(g)(7)(A), qualified production property to which this subsection applies shall be treated as separate nonresidential real property.

Recapture (§168(n)(5))
If, at any time during the 10-year period beginning on the date that any qualified production property is placed in service by the taxpayer, such property ceases to be used as a qualified production activity (described in §168(2)(A)(ii)), and is used by the taxpayer in a productive use not described in §168(2)(A)(ii), then:

1. **§1245 shall be applied -** the property is treated as if it were disposed of at the time of the change in use, and the amount subject to recapture is treated as not less than the full amount previously deducted under the special allowance, and
2. **Basis adjusted** - the taxpayer's basis and depreciation allowances for the property must then be adjusted to reflect the income recognized from the recapture.

Election (§168(n)(6))
Taxpayers may elect to apply the §168(n) special allowance for qualified production property by specifying the eligible nonresidential real property and the portion designated for the election. The election must be made on a timely filed return for the year the property is placed in service and in the manner prescribed by the Secretary through regulations or other guidance.

NOTE - Once made, the election is irrevocable except with the consent of the Secretary, which will be granted only in extraordinary circumstances.

Regulations (§168(n)(7))
The Secretary shall issue such regulations or other guidance as may be necessary or appropriate to carry out the purposes of this subsection, including regulations or other guidance:

1. Define what constitutes a substantial transformation of property, consistent with standards under §954(d), and
2. Provide recapture and transfer rules for situations where qualified production property changes use or is transferred in fully or partially tax-free transactions.

§168(n) – Special Allowance for Qualified Production Property (OBBB 2025)	
Purpose	Provides a **100% immediate deduction** (full expensing) for qualified production property (QPP) used in domestic manufacturing, refining, or chemical/agricultural production.
Eligibility	Available **only by election** for taxpayers that construct or acquire qualifying **nonresidential real property** used as an integral part of a production activity.
Qualified Property	That portion of **nonresidential real property** that: • Is used directly in a qualified production activity • Is constructed in the **United States or its possessions** • Original use begins with the taxpayer • Construction begins **after January 19, 2025** and before **January 1, 2029** • Placed in service **before January 1, 2031**
Qualified Production Activity	Includes **manufacturing, refining, agricultural, or chemical production** that results in a **substantial transformation** of tangible property. Excludes offices, administrative areas, research, software development, and sales functions.
Qualified Product	Tangible personal property other than food or beverages prepared and sold in the same retail building.
Amount of Deduction	100% of the property's **adjusted basis** in the year placed in service. Basis is reduced by the amount deducted before computing any further depreciation.
Election	Must be made **on a timely filed tax return** for the year the property is placed in service. Election is **irrevocable** without IRS consent (only allowed in extraordinary circumstances).
Coordination with Other Provisions	For purposes of: • **§168(k)(7)** (election to forgo bonus depreciation) • **§168(l)(3)(D)** (reuse and recycling property) • **§168(m)(2)(B)(iii)** (disaster assistance property) — QPP is treated as a **separate class of property** with its own election rules.
Alternative Depreciation System (ADS)	QPP is **not eligible** for ADS under §168(g). For classification purposes, it is treated as **separate nonresidential real property**.
Recapture	If the property **ceases to be used** in a qualified production activity within **10 years**, §1245 recapture applies. Property is treated as disposed of at the time of change, and previously deducted amounts are **recaptured as ordinary income**. Basis and depreciation must be adjusted accordingly.
AMT Treatment	The deduction is **fully allowed** for **alternative minimum tax** purposes (no §56 adjustment).
Regulations & Guidance	Treasury will issue regulations defining "substantial transformation" consistent with §954(d) and providing rules for recapture following tax-free transfers.
Effective Dates	Applies to property with construction beginning **after January 19, 2025**, and before **January 1, 2029**, that is **placed in service before January 1, 2031**.

Farm Depreciation Provisions

Shorter Recover Period – 5 Years

The TCJA of 2017 shortens the recovery period from 7 to 5 years for any machinery or equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) used in a farming business, the original use of which commences with the taxpayer and is placed in service after December 31, 2017.

200% DB Allowed for 3, 5, 7 or 10-Year Property

The Act also repeals the required use of the 150% declining balance method for property used in a farming business (i.e., for 3, 5, 7, and 10-year property). The 150% declining balance method will continue to apply to any 15-year or 20-year property used in the farming business to which the straight-line method does not apply, or to property for which the taxpayer elects the use of the 150% declining balance method.

Farming business defined

For these purposes, the term "farming business" means a farming business as defined in §263A(e)(4). Thus, the term ''farming business'' means a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity (e.g., the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than six years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals). A farming business includes processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural products. A farming business does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another taxpayer, or merely buying and reselling plants or animals grown or raised by another taxpayer.

EFFECTIVE DATE – The provision is effective for property placed in service after December 31, 2017, in taxable years ending after such date.

Use of ADS for Electing Farming Business

An electing farming business is required to use the alternative depreciation system (ADS) to depreciate any property used in the farming business with a recovery period of 10-years or more. See §168(g)(1)(G).

NOTE – An electing farming business is one that elects out of the interest deduction limitations under §163(j). See §163(j)(7)(C).

Accounting Method Changes

Cash Method

Background – Pre-2018 Rules & Other Definitions

Cash method

Taxpayers using the cash method generally recognize items of income when actually or constructively received and items of expense when paid. The cash method is administratively easy and provides the taxpayer flexibility in the timing of income recognition. It is the method generally used by most individual taxpayers, including farm and nonfarm sole proprietorships.

Accrual method

Taxpayers using an accrual method generally accrue items of income when all the events have occurred that fix the right to receive the income and the amount of the income can be determined with reasonable accuracy. Taxpayers using an accrual method of accounting generally may not deduct items of expense prior to when all events have occurred that fix the obligation to pay the liability, the amount of the liability can be determined with reasonable accuracy, and economic performance has occurred. Accrual methods of accounting generally result in a more accurate measure of economic income than does the cash method. The accrual method is often used by businesses for financial accounting purposes.

C corporations & partnership with C corporation partners

A C corporation, a partnership that has a C corporation as a partner, or a tax-exempt trust or corporation with unrelated business income generally may not use the cash method. Exceptions are made for farming businesses, qualified personal service corporations, and the aforementioned entities to the extent their average annual gross receipts do not exceed $5 million for all prior years (including the prior taxable years of any predecessor of the entity) (the "gross receipts test"). The cash method may not be used by any tax shelter.

NOTE – For this purpose, a tax shelter includes: (1) any enterprise (other than a C corporation) if at any time interests in such enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having the authority to regulate the offering of securities for sale; (2) any syndicate (within the meaning of §1256(e)(3)(B)); or (3) any tax shelter as defined in §6662(d)(2)(C)(ii). In the case of a farming trade or business, a tax shelter includes any tax shelter as defined in §6662(d)(2)(C)(ii) or any partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, (1) if at any time interests in such partnership or enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having authority to regulate the offering of securities for sale or (2) if more than 35% of the losses during any period are allocable to limited partners or limited entrepreneurs.

Purchase, production, or sale of merchandise is an income producing factor

In addition, the cash method generally may not be used if the purchase, production, or sale of merchandise is an income producing factor. Such taxpayers generally are required to keep inventories and use an accrual method with respect to inventory items.

Farming business defined

A farming business is defined as a trade or business of farming, including operating a nursery or sod farm, or the raising or harvesting of trees bearing fruit, nuts, or other crops, timber, or ornamental trees. Such farming businesses are not precluded from using the cash method regardless of whether they meet the gross receipts test. However, §447 generally requires a farming C corporation (and any farming partnership if a corporation is a partner in such partnership) to use an accrual method of accounting. §447 does not apply to nursery or sod farms, to the raising or harvesting of trees (other than fruit and nut trees), nor to farming C corporations meeting a gross receipts test with a $1 million threshold. For family farm C corporations, the threshold under the gross receipts test is $25 million.

Qualified personal service corporation defined

A qualified personal service corporation is a corporation:

1. substantially all of whose activities involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting, and
2. substantially all of the stock of which is owned by current or former employees performing such services, their estates, or heirs.

NOTE – Qualified personal service corporations are allowed to use the cash method without regard to whether they meet the gross receipts test.

Expansion of Cash Method of Accounting for Small Businesses (§448(b)(3))

EFFECTIVE DATE – Taxable years beginning after December 31, 2017.
NOTE – This is a change in the taxpayer's method of accounting for purposes of §481.

$25 Million Gross Receipts Test (§448(b), (c) & (d))

The cash method of accounting may be used by taxpayers, other than tax shelters, that satisfy the gross receipts test, regardless of whether the purchase, production, or sale of merchandise is an income-producing factor. The gross receipts test allows taxpayers with annual average gross receipts that do not exceed $25 million (indexed for inflation after 2018) for the 3-prior taxable-year period (i.e., the gross receipts test) to use the cash method.

NOTE – In the case of a sole proprietorship, the gross receipts test is applied as if the sole proprietorship is a corporation or partnership.

Farming C corporations (§447(c) & (d))

The TCJA expands the universe of farming C corporations (and farming partnerships with a C corporation partner) that may use the cash method to include any farming C corporation (or farming partnership with a C corporation partner) that meets the $25 million gross receipts test.

Personal service corporations & taxpayers other than C corporations (§448(b)(2))

The TCJA retains the exceptions from the required use of the accrual method for qualified personal service corporations and taxpayers other than C corporations. Thus, qualified personal service corporations, partnerships without C corporation partners, S corporations, and other pass-through entities are allowed to use the cash method without regard to whether they meet the $25 million gross receipts test, so long as the use of such method clearly reflects income.

NOTE – The cash method generally may not be used by taxpayers, other than those that meet the $25 million gross receipts test, if the purchase, production, or sale of merchandise is an income-producing factor. In addition, the cash method may not be used by a tax shelter.

Accounting for Inventories (§471)

Background

In general, for Federal income tax purposes, taxpayers must account for inventories if the production, purchase, or sale of merchandise is an income-producing factor to the taxpayer. Treasury regulations also provide that in any case in which the use of inventories is necessary to clearly reflect income, the accrual method must be used with regard to purchases and sales. However, an exception is provided for taxpayers whose average annual gross receipts do not exceed $1 million. A second exception is provided for taxpayers in certain industries whose average annual gross receipts do not exceed $10 million and that are not otherwise prohibited from using the cash method under §448. Such taxpayers may account for inventory as materials and supplies that are not incidental (i.e., "non-incidental materials and supplies").

In those circumstances in which a taxpayer is required to account for inventory, the taxpayer must maintain inventory records to determine the cost of goods sold during the taxable period. Cost of goods sold generally is determined by adding the taxpayer's inventory at the beginning of the period to the purchases made during the period and subtracting from that sum the taxpayer's inventory at the end of the period.

Because of the difficulty of accounting for inventory on an item-by-item basis, taxpayers often use conventions that assume certain item or cost flows. Among these conventions are the first-in, first-out ("FIFO") method, which assumes that the items in ending inventory are those most recently acquired by the taxpayer, and the last-in, first-out ("LIFO") method, which assumes that the items in ending inventory are those earliest acquired by the taxpayer.

Alternatives to Inventories for Small Businesses (§471(c))

EFFECTIVE DATE – Taxable years beginning after December 31, 2017.
NOTE – This is a change in the taxpayer's method of accounting for purposes of §481.

The TCJA exempts certain taxpayers from the requirement to keep inventories. Specifically, taxpayers that meet the $25 million gross receipts test (indexed for inflation after 2018) are not required to account for inventories under §471, but rather may use a method of accounting for inventories that either:

1. treats inventories as non-incidental materials and supplies, or
2. conforms to the taxpayer's financial accounting treatment of inventories.

NOTE 1 – A deduction is generally permitted for the cost of non-incidental materials and supplies in the taxable year in which they are first used or are consumed in the taxpayer's operations. See Reg. §1.162-3(a)(1).

NOTE 2 – The taxpayer's financial accounting treatment of inventories is determined by reference to the method of accounting used in the taxpayer's applicable financial statement or, if the taxpayer does not have an applicable financial statement, the method of accounting used in the taxpayer's book and records prepared in accordance with the taxpayer's accounting procedures.

Uniform Capitalization (§263A)

Background

The uniform capitalization rules require certain direct and indirect costs allocable to real or tangible personal property produced by the taxpayer to be included in either inventory or capitalized into the basis of such property, as applicable. For real or personal property acquired by the taxpayer for resale, §263A generally requires certain direct and indirect costs allocable to such property to be included in inventory.

§263A provides a number of exceptions to the general uniform capitalization requirements. One such exception exists for certain small taxpayers who acquire property for resale and have $10 million or less of average annual gross receipts; such taxpayers are not required to include additional §263A costs in inventory. Another exception exists for taxpayers who raise, harvest, or grow trees. Under this exception, §263A does not apply to trees raised, harvested, or grown by the taxpayer (other than trees bearing fruit, nuts, or other crops, or ornamental trees) and any real property underlying such trees. Similarly, the uniform capitalization rules do not apply to any plant having a preproductive period of two years or less or to any animal, which is produced by a taxpayer in a farming business (unless the taxpayer is required to use an accrual method of accounting under §447 or §448(a)(3)). Freelance authors, photographers, and artists also are exempt from §263A for any qualified creative expenses.

Exception from Uniform Capitalization Rules for Small Businesses (263A(i))

The TCJA expands the exception for small taxpayers from the uniform capitalization rules. Under the provision, any producer or reseller that meets the $25 million gross receipts test (indexed for inflation after 2018) is exempted from the application of §263A. The provision retains the exemptions from the uniform capitalization rules that are not based on a taxpayer's gross receipts.

EFFECTIVE DATE – Taxable years beginning after December 31, 2017.
NOTE – This is a change in the taxpayer's method of accounting for purposes of §481.

Accounting for Long-Term Contracts

Background

In general, in the case of a long-term contract, the taxable income from the contract is determined under the percentage-of-completion method. Under this method, the taxpayer must include in gross income for the taxable year an amount equal to the product of (1) the gross contract price and (2) the percentage of the contract completed during the taxable year. The percentage of the contract completed during the taxable year is determined by comparing costs allocated to the contract and incurred before the end of the taxable year with the estimated total contract costs. Costs allocated to the contract typically include all costs (including depreciation) that directly benefit or are incurred by reason of the taxpayer's long-term contract activities. The allocation of costs to a contract is made in accordance with regulations. Costs incurred with respect to the long-term contract are deductible in the year incurred, subject to general accrual method of accounting principles and limitations.

Exception for small construction contracts

An exception from the requirement to use the percentage-of-completion method is provided for certain construction contracts ("small construction contracts"). Contracts within this exception are those contracts for the construction or improvement of real property if the contract:

1. is expected (at the time such contract is entered into) to be completed within 2-years of commencement of the contract and
2. is performed by a taxpayer whose average annual gross receipts for the prior 3 taxable years do not exceed $10 million.

Thus, long-term contract income from small construction contracts must be reported consistently using the taxpayer's exempt contract method. Permissible exempt contract methods include the completed contract method, the exempt-contract percentage-of-completion method, the percentage-of-completion method, or any other permissible method.

Small Businesses Exception from Percentage of Completion Method (§460(e))

EFFECTIVE DATE – Contracts entered into after December 31, 2017, in taxable years ending after such date.

The TCJA expands the exception for small construction contracts from the requirement to use the percentage-of-completion method. Under the provision, contracts within this exception are those contracts for the construction or improvement of real property if the contract:

1. is expected (at the time such contract is entered into) to be completed within 2-years of commencement of the contract and
2. is performed by a taxpayer that (for the taxable year in which the contract was entered into) meets the $25 million gross receipts test (indexed for inflation after 2018).

NOTE – Application of the exception for small construction contracts from the requirement to use the percentage-of-completion method is applied on a cutoff basis for all similarly classified contracts (hence there is no adjustment under §481(a) for contracts entered into before January 1, 2018).

Taxable Year of Inclusion Modified (§451)

Background

Taxable year of inclusion (§451)

Under §61(a), gross income generally includes all income from whatever source derived, except as otherwise provided in the IRC. Thus, gross income generally includes income realized in any from, whether in money, property, or services, except to the extent provided in other sections of the Code. Once it is determined that an item of gross income is clearly realized for Federal income tax purposes, §451 and the regulations thereunder provide the general rules as to the timing of when such item is to be included in gross income.

A taxpayer generally is required to include an item in gross income no later than the time of its actual or constructive receipt, unless the item properly is accounted for in a different period under the taxpayer's method of accounting. If a taxpayer has an unrestricted right to demand the payment of an amount, the taxpayer is in constructive receipt of that amount whether or not the taxpayer makes the demand and actually receives the payment.

Cash basis

In general, for a cash basis taxpayer, an amount is included in gross income when actually or constructively received. For an accrual basis taxpayer, an amount is included in gross income when all the events have occurred that fix the right to receive such income and the amount thereof can be determined with reasonable accuracy (i.e., when the "all events test" is met), unless an exception permits deferral or exclusion, or a special method of accounting applies. A number of exceptions that exist to permit deferral of gross income relate to advance payments. An advance payment is when a taxpayer receives payment before the taxpayer provides goods or services to its customer. The exceptions often allow tax deferral to mirror financial accounting deferral (e.g., income is recognized as the goods are provided or the services are performed).

Interest income

A taxpayer generally must include in gross income the amount of interest received or accrued within the taxable year on indebtedness held by the taxpayer.

Original issue discount (OID)

The holder of a debt instrument with original issue discount ("OID") generally accrues and includes the OID in gross income as interest over the term of the instrument, regardless of when the stated interest (if any) is paid.

TCJA Modification to Taxable Year of Inclusion

Inclusion not later than for financial accounting purposes (§451(b)(1)(A))

The TCJA revises the rules associated with the timing of the recognition of income under §451. Specifically, the provision requires an accrual method taxpayer subject to the all events test for an item of gross income to recognize such income no later than the taxable year in which such income is taken into account as revenue:

1. in an applicable financial statement (defined under §451(b)(3)) or
2. another financial statement under rules specified by the Secretary.

NOTE – The all events test is met with respect to any item of gross income if all the events have occurred which fix the right to receive such income and the amount of such income can be determined with reasonable accuracy.

Exception (§451(b)(1)(B))

There are exceptions to the rules for:

1. taxpayers without an applicable or other specified financial statement and
2. any item of gross income in connection with a mortgage servicing contract.

NOTE – The Committee intended that the financial statement conformity requirement added to §451 not be construed as preventing the use of special methods of accounting provided elsewhere in the Code, other than part V of subchapter P (special rules for bonds and other debt instruments) excluding items of gross income in connection with a mortgage servicing contract. For example, it does not preclude the use of the installment method under §453 or the use of long-term contract methods under §460. See §451(b)(2).

Allocation of transaction price (§451(b)(4))

In the case of a contract which contains multiple performance obligations, the provision allows the taxpayer to allocate the transaction price in accordance with the allocation made in the taxpayer's applicable financial statement.

Mortgage servicing contracts

The provision provides an exception for any item of gross income in connection with a mortgage servicing contract. Thus, under the provision, income from mortgage servicing rights will continue to be recognized in accordance with the present law rules for such items of gross income (i.e., "normal" mortgage servicing rights will be included in income upon the earlier of earned or received under the all events test of §451 (i.e., not averaged over the life of the mortgage), and "excess" mortgage servicing rights will be treated as stripped coupons under §1286 and therefore subject to the original issue discount rules).

Advance payments codified (§451(c))

The provision also codifies the current deferral method of accounting for advance payments for goods, services, and other specified items provided by the IRS under Revenue Procedure 2004-34. That is, the provision allows accrual method taxpayers to elect to defer the inclusion of income associated with certain advance payments to the end of the tax year following the tax year of receipt if such income also is deferred for financial statement purposes. In the case of advance payments received for a combination of services, goods, or other specified items, the provision allows the taxpayer to allocate the transaction price in accordance with the allocation made in the taxpayer's applicable financial statement. The provision requires the inclusion in gross income of a deferred advance payment if the taxpayer ceases to exist.

Change in method of accounting

The application of these rules is a change in the taxpayer's method of accounting for purposes of §481. In the case of any taxpayer required by this provision to change its method of accounting for its first taxable year beginning after December 31, 2017, such change is treated as initiated by the taxpayer and made with the consent of the Secretary. In the case of income from a debt instrument having OID, the related §481(a) adjustment is taken into account over 6 taxable years.

EFFECTIVE DATE – The provision generally applies to taxable years beginning after December 31, 2017. In the case of income from a debt instrument having OID, the provision applies to taxable years beginning after December 31, 2018.

UPDATE – Final Regulations Issued

Final regulations (TD 9941) were issued 01-06-21 with respect to the timing of income inclusion by accrual method taxpayers that either have "applicable financial statement" or receive advance payments.

Updated List for Automatic Change in Accounting Methods

Scope and Updates

Rev. Proc 2025-23 provides the current list of accounting method changes eligible for automatic consent, superseding prior guidance. It removes obsolete sections (such as those for expired elections), clarifies the application of Sec. 481(a) adjustments, and streamlines rules for depreciation, interest capitalization, and inventory valuation. Some changes, like those under former Sec. 118(c), now require non-automatic procedures.

Eligibility

To qualify for automatic consent, the change must be listed in Rev. Proc. 2025-23 and the taxpayer must meet all specific requirements. Generally, the same change cannot have been made or requested for the same item in the prior five years (with some exceptions). The taxpayer must not be involved in a Sec. 381 transaction for the year of change, and the year of change must not be the final year of the trade or business unless an exception applies. Some rules are relaxed for small businesses and in certain transition situations.

Procedural Requirements

Taxpayers must file *Form 3115, Application for Change in Accounting Method*, unless a short form or statement is specifically permitted. The correct automatic change number must be entered on the form. For most changes, the application can be filed up to the extended due date of the return for the year of change, and no user fee is required. Transition rules allow certain pending non-automatic requests to be converted to automatic procedures if eligible. Reduced filing requirements or the ability to file a single Form 3115 for multiple changes may apply, especially for small businesses.

Miscellaneous Topics

Charitable Conservation Easement & Listed Transactions

NOTE – Click here for the IRS list of recognized abusive and listed transactions click here for additional information about abusive tax shelters and transactions.

Prop. Regs. – Certain CRATS are Listed Transactions (REG-108761-22)

On March 22, 2024, proposed regulations were issued to identify certain charitable remainder annuity trust (CRAT) transactions and substantially similar transactions as listed transactions, a type of reportable transaction. Material advisors and certain participants in these listed transactions would be required to file disclosures with the IRS and would be subject to penalties for failure to disclose. The proposed regulations would affect participants in these transactions as well as material advisors but provide that certain organizations whose only role or interest in the transaction is as a charitable remainderman will not be treated as participants in the transaction or as parties to a prohibited tax shelter transaction subject to excise taxes and disclosure requirements. This would be effective after the regulations are finalized.

Qualified Conservation Contributions Final Regulations (TD 9999)

This document contains final regulations concerning the statutory disallowance rule enacted by the SECURE 2.0 Act of 2022 to disallow a Federal income tax deduction for a qualified conservation contribution made by a partnership or an S corporation after December 29, 2022, if the amount of the contribution exceeds 2.5 times the sum of each partner's or S corporation shareholder's relevant basis. These final regulations provide guidance regarding this statutory disallowance rule, including definitions, appropriate methods to calculate the relevant basis of a partner or an S corporation shareholder, the three statutory exceptions to the statutory disallowance rule, and related reporting requirements. In addition, these final regulations provide reporting requirements for partners and S corporation shareholders that receive a distributive share or pro rata share of any noncash charitable contribution made by a partnership or S corporation, regardless of whether the contribution is a qualified conservation contribution (and regardless of whether the contribution is of real property or other noncash property). These final regulations affect partnerships and S corporations that claim qualified conservation contributions, and partners and S corporation shareholders that receive a distributive share or pro rata share, as applicable, of a noncash charitable contribution.

NOTE - These regulations are effective on June 28, 2024, and generally apply to contributions made after December 29, 2022.

IRS sent settlement offer letters to certain taxpayers who participated in Syndicated Conservation Easement transactions (IR-2024-174)

On June 26, 2024, the IRS announced (IR-2024-174) that it sent time-limited settlement offer letters in July to certain taxpayers who had participated in Syndicated Conservation Easement (SCE) transactions or substantially similar arrangements and were under audit. Eligible taxpayers were notified by letter, which outlined the terms and deadlines for the settlement. The settlement required substantial concession of the claimed tax benefits and the acceptance of penalties. Taxpayers who received a letter but chose not to participate remained subject to IRS enforcement, including the potential for full disallowance of the charitable contribution deduction and all applicable penalties. Taxpayers who did not receive a letter, or whose cases were pending in the

U.S. Tax Court, were not eligible for this settlement offer. The IRS continued enforcement actions against all ineligible or non-participating taxpayers.

Final Regulations Identifying Syndicated Conservation Easement Transactions as Abusive Tax Transactions (TD 10007)

On October 7, 2024, the Department of the Treasury and the IRS issued final regulations (TD 10007) identifying certain syndicated conservation easement transactions as listed transactions (i.e., abusive tax transactions that must be reported to the IRS).

NOTE - Syndicated conservation easements have been included in the IRS' annual list of Dirty Dozen tax schemes for many years.

In these transactions, investors typically acquire an interest in a partnership that owns land and then claim an inflated charitable contribution deduction based on a grossly overvalued appraisal. Going forward, participants and material advisors will need to report their participation in these transactions using *Form 8886 - Reportable Transaction Disclosure Statement* and *Form 8918 - Material Advisor Disclosure Statement*.

NOTE – Form more detailed IRS information on recognized abusive and listed transactions click here.

The IRS previously identified certain SCE transactions as listed transactions in Notice 2017-10. These final regulations, consistent with Notice 2017-10, identify certain SCE transactions as listed transactions.

CAUTION - The issuance of these final regulations clarifies that participants and material advisors must report these transactions, including any transactions that were completed in taxable years that are still open.

This listed transaction regulation is part of a multifaceted IRS approach that is succeeding in protecting the integrity of the tax system. On a related front, the IRS has enjoyed significant success in the courts resulting in a number of syndicated partnerships having their grossly inflated easement valuations reduced for tax purposes to what the actual market value was at the time of the donation, with the partners claiming the inflated deduction often incurring substantial penalties.

Chevron Case Overturned (Loper Bright Enterprises)

Chevron Deference Background

Chevron deference is a legal principle that originated from the 1984 Supreme Court case Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc. Under this doctrine, courts defer to a federal agency's interpretation of a law that it administers when the law is ambiguous, as long as the agency's interpretation is reasonable. The principle operates in two steps:

1. **Step One:** The court determines whether the statute is clear regarding the specific issue at hand. If the statute is clear, the court must follow that clear intent of Congress.
2. **Step Two:** If the statute is ambiguous or silent on the issue, the court does not impose its own interpretation but instead defers to the agency's interpretation, as long as it is reasonable.

NOTE - The rationale behind Chevron deference was that agencies, as experts in their respective fields, are better equipped to interpret and implement the complex and technical statutes they are charged with enforcing. This deference has allowed agencies significant flexibility in interpreting laws, which has played a key role in shaping federal regulations and policy.

Loper Bright Enterprises v. Raimondo (SC - 06-28-24 decision)

Background

- This case arose from the fishing industry's (i.e, Loper Bright Enterprises (petitioner)) challenge to a rule imposed by the National Marine Fisheries Service (NMFS), a federal agency under the Department of Commerce that manages and conserves marine fisheries in U.S. waters.
- The rule in question required certain fishing vessels to pay for government-mandated at-sea monitors.
- These monitors were placed on vessels to ensure compliance with various regulations, including those related to catch limits and bycatch reduction.

Legal Issue

- The key legal issue was whether the NMFS had the authority under the Magnuson-Stevens Fishery Conservation and Management Act to require fishing vessels to cover the costs of these at-sea monitors.
- The petitioners argued that the Act did not explicitly grant the agency this power and that such an imposition was unlawful.
- The petitioners further contended that the lower courts had improperly applied Chevron deference to uphold the NMFS's interpretation of the statute.
- They argued that the courts should not have deferred to the agency's interpretation, as it resulted in an undue financial burden on the fishing companies without clear congressional authorization.

Chevron Deference Challenge

- The lower court upheld the NMFS regulation, applying Chevron deference to interpret the statute.
- The petitioners asked the Supreme Court to reconsider or overturn the Chevron deference doctrine, which had been applied by lower courts to uphold the NMFS's authority.
- They argued that the judiciary should have the final say in interpreting ambiguous statutes, rather than deferring to the agency's interpretation.

Supreme Court Ruling - Loper Bright Enterprises v. Raimondo

- The Court, in a 6-3 decision (on 06-28-2024) authored by Chief Justice Roberts, emphasized that courts must exercise their independent judgment when determining whether an agency has acted within its statutory authority.
- The majority opinion underscored that it is the role of the judiciary, not administrative agencies, to interpret the law.
- This stance directly counters the Chevron doctrine, which allowed courts to defer to agencies' reasonable interpretations of ambiguous statutes.

NOTE - The decision restores and reinforces the judiciary's role as the primary interpreter of laws, asserting that courts must independently determine the best reading of a statute, regardless of the agency's expertise or policy preferences. This marks a significant limitation on the power and flexibility of administrative agencies in shaping the interpretation of federal statutes.

Incompatibility with the APA

- The Court's reasoning leaned heavily on the Administrative Procedure Act (APA), which mandates that "the reviewing court" must "decide all relevant questions of law" and "interpret statutory provisions."
- The Court found that this directive from the APA could not be reconciled with Chevron's requirement for courts to accept any "permissible" agency construction of an ambiguous statute. The Court argued that even when a statute is ambiguous, there is still a "best reading," which the court is obliged to identify and adopt.

Rejection of Agency Expertise as Determinative

- One of the core arguments in Chevron was that agencies possess the expertise necessary to interpret complex and technical statutes. However, the Court in Loper Bright rejected the notion that statutory ambiguities should be resolved by agencies based on their expertise or policy decisions.
- Instead, the Court argued that statutory interpretation is a "textual art" in which courts have "special competence." The decision reinforces that it is the judiciary's duty to determine the best reading of a statute, even in areas involving technical matters, based on legal principles and interpretive tools.

Historical and Constitutional Foundation

- The Court referenced Marbury v. Madison to bolster its rationale, quoting Chief Justice Marshall's declaration that "It is emphatically the province and duty of the judicial department to say what the law is."
- The majority opinion suggested that the framers of the Constitution anticipated that courts would often encounter statutory ambiguities and expected that courts, not agencies, would resolve them by exercising independent legal judgment.

Impact on Judicial Review

- The Court concluded that the APA's provisions for reviewing agency actions effectively codify the principle, dating back to Marbury v. Madison, that courts are responsible for deciding legal questions by applying their own judgment.
- This decision reinforces the idea that courts should not abdicate their responsibility to interpret the law, even in the face of statutory ambiguities involving administrative agencies.

Regulations Post Loper Bright Enterprises

NOTE – Click here to see a summary of understanding all IRS guidance.

Final Regulations

- Legally binding and have full force of law.
- Published in the Federal Register and eventually in the Code of Federal Regulations (CFR).
- Can be relied on indefinitely, unless amended or repealed.
- These are the IRS's official interpretation of the tax law.

NOTE - You can rely on final regulations when preparing returns or advising clients.

Proposed Regulations

- Issued for public comment before becoming final.
- Not binding on taxpayers or the IRS, unless the IRS says you can rely on them.
- Often contain a statement like: "Taxpayers may rely on these proposed regulations until final regulations are issued."

NOTE - You can rely on proposed regulations only if the IRS explicitly allows it in the preamble.

Temporary Regulations

- Issued to provide immediate guidance (often after a new law is passed).
- Have the same authority as final regulations while they're in effect.
- Valid for a maximum of 3 years from the date of issuance (under current law).
- Usually accompanied by proposed regulations, which will eventually become final.

NOTE - You can rely on temporary regs just like final regulations until they expire or are replaced.

Type of Regulation	Binding on Taxpayers?	Can You Rely on It?	Court Deference (Post-*Loper Bright*)	Notes
Final Regulations	☑ Yes	☑ Yes	⚖ Court will interpret statute **independently -** no automatic deference	Strongest form of IRS guidance, but more vulnerable to legal challenge
Temporary Regulations	☑ Yes	☑ Yes	⚖ Same as final - court decides if it matches the law	Valid for up to 3 years; often replaced by final regs
Proposed Regulations	✕ Not binding	⚠ Only if IRS says so	✕ No deference at all	Courts don't treat proposed regs as authoritative; IRS must state if you may rely on them
Interpretive (vs. Legislative)	? Depends on court	⚠ Usually, but not guaranteed	⚠ No special weight given anymore	Courts will scrutinize more than before

Rules & Regulations (§7805)

Authorization (§7805(a))

Except where such authority is expressly given by this title to any person other than an officer or employee of the Treasury Department, the Secretary shall prescribe all needful rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.

- §7805(a) is the foundation for most IRS regulations and guidance.
- It is not a grant of unlimited power - rules must still align with the statute and follow the Administrative Procedure Act (APA).
- Courts give less deference to rules issued under this general authority than those issued under specific Congressional direction (called "legislative regulations").

Two Types of IRS Regulations (Post-Loper Bright)

Legislative (Authorized) Regulations

- Issued under a direct grant of authority from the Internal Revenue Code.
- Example: IRC says, "The Secretary shall prescribe regulations to implement this section."
- These are meant to fill in the details of a statute.

NOTE – These still carry the most legal weight, but the Courts now review them independently—they don't defer to the IRS just because the regulation is reasonable. The IRS must now show that the regulation is the best interpretation, not just "a reasonable one."

Interpretive Regulations

- Issued where the Code is silent or ambiguous, and the IRS is interpreting the law on its own.
- The IRS isn't specifically told to issue these regulations, they're based on general authority (e.g., under IRC §7805(a)).

NOTE - Now carry less persuasive authority than before. Courts no longer give them automatic deference and may reject them more often. Especially vulnerable when the interpretation adds burdens, narrows taxpayer rights, or conflicts with plain language of the statute.

Type	Based On	Pre-2024 Deference	Post-2024 Deference	Still Reliable for Taxpayers?
Legislative Regs	Specific IRC authority to issue regs	✅ Strong (Chevron)	⚠️ No deference; court decides	✅ Yes (unless overruled by court)
Interpretive Regs	General authority (e.g., IRC § 7805(a))	⚠️ Some deference	❌ No deference	⚠️ Use with caution

Summary Tables & Recent Legislation

Table of Contents

Individual Income Tax Provision Summary Tables **3**
OBBB Individual Income Tax Provisions 3
Individual Provisions Expiring during or after 2025 12
Individual Provisions Expiring after 2026 13

Business Income Tax Provision Summary Tables **14**
OBBB Business Income Tax Provisions 14
OBBB Subchapter A – Termination of Green New Deal Subsidies 19
OBBB Subchapter B – Enhanced America-First Energy Policies 20
Business Provisions Expiring after 2025 21

Miscellaneous OBBB Provisions **22**
Premium Tax Credit (PTC) Limited to Certain Lawfully Present Noncitizens (Post 2026) 22
Trump Accounts (§530A) (Post 2025) 23
Trump Accounts Contribution Pilot Program (§6434) 29
Employer Contributions to Trump Accounts (§128) 30
Qualified Tuition Programs (QTP) – 529 Plans (§529) 31
Federal Scholarship Contribution Credit & Exclusion (Post 2026) 33

Individual Income Tax Provision Summary Tables

UPDATE – On July 4, 2025, President Trump signed the One Big Beautiful Bill (OBBB – HR-1) into law. The legislation permanently extends the 2017 Tax Cuts and Jobs Act (TCJA) and provides additional income tax relief for both individuals and businesses. Click here for the IRS summary of the OBBB provisions.

OBBB Individual Income Tax Provisions

Filing Status & Exemptions	IRC Section
Personal Exemption (Post 2017) - The personal exemption deduction is permanently eliminated.	151(d)(5)
Exclusions from Income	**IRC Section**
Student Loan Discharges **2021-2025 -** Broad exclusion of most federal, state, institutional, or private education student. **Post 2025 (OBBB) -** Gross income does not include student loan or private education loan discharges due to death or permanent disability of the borrower. Borrower must report Social Security Number on tax return.	108(f)(5)
Qualified education loans (After 03-27-20) - Qualified education loans (principal or interest) are excludable from employees gross income (up to $5,250). This applies to the employee only (but not spouse or dependents). The OBBB makes this permanent and will start adjusting the $5,250 for inflation after 2026.	127(c)(1)(B)
Employer-provided dependent care assistance (After 2025) - The OBBB increases the maximum annual exclusion for employer-provided dependent care assistance from $5,000 to $7,500 ($2,500 to $3,750 for married individuals filing separately) for tax years beginning after December 31, 2025.	129
Scholarships for Qualified Elementary or Secondary Education Expenses (Post 2026) - Gross income does not include scholarships received for qualified K–12 education expenses of an eligible student, if provided by a Scholarship Granting Organization (SGO). The terms "qualified expenses," "eligible student," and "SGO" are defined by reference to §25F(c).	§139K
529 Plan Qualified Higher Education Expenses (QHHE) (OBBB Post 07-04-25) - 529 plan qualified higher education expenses include **qualified postsecondary credentialing expenses**. These tax-free 529 distributions now cover tuition, fees, books, supplies, equipment, testing, and continuing education required to obtain or maintain a recognized postsecondary credential. Eligible programs must appear on certain approved lists, such as state Workforce Innovation and Opportunity Act lists, the VA's WEAMS directory, or be recognized as preparatory for credentialing exams. Credentials include industry-recognized certifications, registered	NEW 529(f)

apprenticeships, occupational/professional licenses, and those identified by the Secretary of Labor. Effective for distributions after 07-04-25.	
529 Plan Qualified Higher Education Expenses (QHHE) **OBBB (Post 07-04-25) -** 529 plan definition of qualified K–12 education expenses expanded to include a broader range of costs, such as tuition, curriculum materials, books, online resources, tutoring (under specific conditions), standardized testing fees, dual enrollment, and licensed educational therapies for students with disabilities. Effective for distributions after 07-04-25. **OBBB (Post 2025) -** The annual distribution limit for K–12 expenses is increased from $10,000 to $20,000 per beneficiary. Effective for tax years beginning after 2025.	529(c)(7)
ABLE Contributions (Post 2017) – The OBBB permanently extends the ability for employed individuals with disabilities to make additional contributions to their ABLE accounts, limited to the lesser of - (a) the federal poverty line for a one-person household, or (b) the beneficiary's compensation for the taxable year**.**	529A(b)
§529 rollover to ABLE (Post 2017) - The OBBB permanently allows tax-free rollovers from qualified tuition programs (529 accounts) to ABLE accounts, provided the ABLE account is owned by the designated beneficiary of the 529 account or a member of the beneficiary's family. Rolled-over amounts count toward the annual contribution limit for the ABLE account. Any amount that exceeds this limit is included in the distributee's gross income under the rules of §72.	529(c)(3)
Trump Accounts (Post 2025) The OBBB establishes a new tax-deferred investment account for children, called a "Trump Account." These accounts may receive contributions from parents, relatives, employers, taxable entities, nonprofits, and government agencies. Effective for tax years beginning after 2025. **Eligibility -** Available to U.S. citizen children with a Social Security number. If parents do not open an account, the IRS will establish one automatically unless they opt out. **Contributions -** Up to $5,000 per year may be contributed using after-tax dollars (indexed for inflation). Contributions may be made by parents, relatives, employers, taxable entities, nonprofits, or government agencies. Contributions from tax-exempt organizations (e.g., foundations) are not subject to the $5,000 annual limit if made to a broad group of children (such as by state, district, or school). No contributions are allowed after the child reaches age 18. **Investments -** Funds must be invested in a diversified index fund tracking U.S. equities, and earnings grow tax-deferred. **Distributions -** Withdrawals are generally prohibited until age 18, with limited exceptions. **Pilot Program (2025–2028 births) -** The federal government contributes $1,000 at birth for each eligible child.	530A, 128, 139J, & 6434

Qualified bicycle commuting reimbursements exclusion (Post 2017) - The OBBB permanently eliminates the $20 per month exclusion for qualified bicycle commuting reimbursements.	132(f)
Moving Expense Reimbursement Exclusion **2018–2025 (TCJA) -** The exclusion from gross income and wages for qualified moving expense reimbursements (§217) was suspended, except for U.S. Armed Forces members on active duty moving under military orders. **Post-2025 (OBBB) -** The suspension was made permanent, but eligibility is expanded to include employees and new appointees of the intelligence community (as defined in the National Security Act) when relocation is required by a change in assignment.	132(g)(2)
Trade or Business Income & Expenses	**IRC Section**
Qualified business income (QBI) deduction - **2018- 2025 (TCJA) -** For taxable years beginning after 2017 and before 2026, an individual taxpayer generally may deduct 20% percent of qualified business income (QBI) from a partnership, S corporation, or sole proprietorship, as well as 20% of aggregate qualified REIT dividends, qualified cooperative dividends, and qualified publicly traded partnership income. Special rules apply to specified agricultural or horticultural cooperatives. A limitation based on W-2 wages paid is phased in above a threshold amount of taxable income. A disallowance of the deduction with respect to specified service trades or businesses is also phased in above the threshold amount of taxable income. **Post 2025 (OBBB) -** Permanently extends the 20% deduction for QBI, REIT dividends, and PTP income. Adds a new inflation-adjusted minimum deduction of $400, available only if the taxpayer has at least $1,000 of QBI from one or more active trades or businesses in which the taxpayer materially participates (§469(h)). The wage/capital limitation phase-in threshold and SSTB phase-out threshold are increased to $75,000 ($150,000 married filing joint), indexed for inflation after 2026.	199A
Capital Gain & Losses	**IRC Section**
Small Business Stock Exclusion (Post stock acquired after July 4, 2025) OBBB modifies §1202 for stock acquired after July 4, 2025, phasing gain exclusion to 50% (3 years), 75% (4 years), 100% (5 years), raising the issuer asset test to $75M (inflation-adjusted), and increasing the per-issuer gain cap from $10M to $15M (inflation-adjusted), with AMT relief retained.	1202

Adjustments to Income	IRC Section
Moving expense deduction **2018–2025 (TCJA) -** The deduction for moving expenses was suspended for tax years 2018–2025, except for members of the Armed Forces (and their spouse or dependents) who move pursuant to a military order and permanent change of station. **Post-2025 (OBBB) -** OBBB permanently extends the suspension of the moving expense deduction. It also expands eligibility to allow the deduction for employees and new appointees of the intelligence community (as defined in the National Security Act) when the relocation is required due to a change in assignment.	217(k)
HSAs - Direct primary care (DPC) service arrangement is not a health plan for the "no other coverage" rule (Post 2025) - The OBBB permits participation in direct primary care (DPC) service arrangements without loss of HSA eligibility, provided certain requirements are met; DPC fees for these arrangements are now qualified medical expenses for HSA purposes, effective for months after December 31, 2025. **What counts -** Fixed periodic-fee primary care by primary care practitioners (SSA §1833(x)(2)(A)). **Excludes -** (i) procedures needing general anesthesia; (ii) prescription drugs (except vaccines); (iii) labs not typically done in an ambulatory primary-care setting. **Cap -** Per month ≤ $150 (single) / $300 (covers >1 individual); indexed for tax years after 2026 (base 2025).	223(c)(1)(E) 223(d)(2)(c)(v)
HSA telehealth & remote care services (Post 2024) - The OBBB permanently allows HDHPs to cover telehealth and remote care services before the deductible is met, without affecting HSA eligibility, effective retroactively for plan years beginning after 2024.	223(c)(2)(E)
HSA HDHP definition expanded (Post 2025) - The OBBB expands the definition of an HDHP to include any plan that is (i) sold as individual coverage on an Exchange, and (ii) classified as Bronze (§1302(d)(1)(A)) or Catastrophic (§1302(e)). Effective for months after 2025.	223(c)(2)(H)
Temporary deduction for seniors (2025-2028) – Taxpayers who are age 65 or older (and their spouses, if filing a joint return) may claim a $6,000 deduction per qualified individual. This is phased out at a rate of 6% of the amount by which the taxpayer's adjusted gross income exceeds $75,000 (or $150,000 for joint filers). Taxpayers must include the qualifying individual's Social Security number (SSN) on the return.	151(d)(5)(C)

No Tax on Tips (2025-2028) - The OBBB created new IRC §224 allowing a temporary above-the-line deduction of up to $25,000 for qualified tips received by employees and self-employed individuals. The deduction phases out for higher-income taxpayers, reduced by $100 for every $1,000 (or fraction thereof) of modified AGI above $150,000 (single/MFS) or $300,000 (MFJ). The provision includes enhanced reporting and anti-abuse safeguards.	224
No Tax on Overtime (2025–2028) - The OBBB created new IRC §225 allowing a temporary deduction for qualified overtime pay (as defined under FLSA rules). The deduction is up to $12,500 ($25,000 MFJ) and phases out by $100 per $1,000 of MAGI above $150,000 (single) or $300,000 (joint). It is available to all taxpayers (itemizers and non-itemizers) who meet filing requirements, with employers/payors subject to new information reporting. For overtime compensation earned before January 1, 2026, reporting entities may use reasonable methods to estimate and report qualifying amounts during the transition period.	225
Qualified passenger vehicle loan interest (2025-2028) - The OBBB temporarily (2025-2028) allows a "above-the-line" deduction of up to $10,000 for personal interest on qualified passenger vehicle loans. The deduction begins phasing out for taxpayers with modified adjusted gross income over $100,000 ($200,000 for joint filers). This applies only to new, U.S.-assembled vehicles purchased for personal use. Lease financing, used vehicles, and commercial/fleet loans are excluded.	163(h) & 63(b)
Standard & Itemized Deductions	**IRC Section**
Standard Deduction **2018-2025 (TCJA) -** – The basic deduction was increased to $24,000 for married individuals filing a joint return, $18,000 for head-of-household filers, and $12,000 for all other individuals. **Post 2024 (OBBB) -** The OBBB permanently extends the TCJA increases to the basic standard and further raises the amounts to $31,500 for married individuals filing a joint return (MFJ), $23,625 for head-of-household (HOH) filers, and $15,750 for all other individuals (single/MFS). The amount of the standard deduction is indexed for inflation using the C-CPI-U for taxable years beginning after December 31, 2018.	63(c)(7)
Itemized Deduction Limitation **2018–2025 (TCJA) -** Pease limitation suspended for high-income taxpayers. Pre-TCJA, Pease reduced itemized deductions by the lesser of 3% of AGI over a threshold or 80% of deductions; it was scheduled to return in 2026. **Post-2025 (OBBB) -** Permanently repeals Pease and replaces it with a 2/37 reduction on the lesser of itemized deductions or taxable income above the 37% bracket threshold, excluding the §199A QBI deduction.	68(f)

Miscellaneous itemized deductions **TCJA (2018–2025) -** All miscellaneous itemized deductions that were subject to the 2% AGI floor were suspended. **Post 2025 (OBBB) -** The OBBB makes the suspension of miscellaneous itemized deductions permanent other than those under IRC §67(b). The OBBB creates **a permanent exception for educator expenses** by adding them to the list of deductions not subject to §67 disallowance. §67(h) defines "educator expenses" more broadly than under current law. The revised definition expands allowable expenses to include those incurred by teachers, counselors, and also interscholastic sports administrators or coaches, and removes the prior exclusion for nonathletic health or PE supplies. Additionally, it replaces the limitation of being "in the classroom" with the broader phrase "as part of instructional activity."	67
State and Local Tax (SALT) Limitation **2018-2024 (TCJA) -** The individual SALT deduction was capped at $10,000 ($5,000 - 50% for MFS) through 2025. **2025-2029 (OBBB) -** For tax years beginning after 2024, the OBBB retroactively increases the SALT deduction cap to $40,000 for 2025 ($40,400 for 2026, and 1% annually thereafter through 2029). For taxpayers with MAGI above $500,000 in 2025 ($505,000 in 2026, increasing 1% annually thereafter), the cap is reduced by 30% of the excess over the threshold, but not below $10,000. These amounts are 50% for MFS. **Post 2029 (OBBB) -** The SALT cap reverts to $10,000 starting in 2030.	164(b)(7)
Qualified Residence Interest **2018–2025 (TCJA) -** Deductible interest limited to acquisition indebtedness up to $750,000 ($375,000 MFS). Home equity indebtedness interest is not deductible. Grandfathered debt - acquisition indebtedness incurred before 12-15-2017 retains the $1,000,000 ($500,000 MFS) cap. **Post-2025 (OBBB) -** Permanently extends the TCJA limits - $750,000 acquisition indebtedness cap ($375,000 MFS); home-equity interest remains nondeductible. Also restores deductibility of **qualified mortgage insurance premiums (PMI)** as qualified residence interest for tax years beginning after 2025. PMI is deductible subject to AGI phase-out - reduce by 10% for each $1,000 ($500 if MFS) of AGI over $100,000 ($50,000 MFS); fully phased out at $109,000 ($54,500 MFS). (Grandfathered pre-12-15-2017 acquisition debt remains under the $1,000,000/$500,000 caps.)	163(h)(3)(F)

Cash Charitable Contributions **Post 2017 (TCJA & OBBB) -** The OBBB permanently extends the TCJA rule under §170(b) that increased the 50% limitation for "cash" contributions to public charities and certain private foundations to 60% of the taxpayer's AGI. Excess contributions are to be carried forward for up to five years subject to the later year's ceiling. **Post 2025 (OBBB) -** The OBBB established a new 0.5% floor on charitable contribution deductions. Individuals who itemize deductions may deduct charitable contributions only to the extent their total giving exceeds 0.5% of their contribution base (essentially their AGI). Any amount below this threshold is permanently nondeductible unless the taxpayer's contributions exceed the applicable AGI limitation and qualify for a carryforward under §170(d). In effect, itemizers will not receive any charitable deduction until their aggregate donations surpass the 0.5% floor.	170(b)(1)(G) & 170(b)(1)(I)
Charitable Contribution Deduction for Non-itemizer **Post 2025 (OBBB) -** Non-itemizers may claim a "below-the-line" charitable deduction of up to $1,000 ($2,000 for joint filers). To qualify, contributions must be in cash, made to a public charity, and meet the requirements of IRC §170(p). The deduction is taken after adjusted gross income in computing taxable income under IRC §63(b)(4).	170(p) & 63(b)(4)
Individual personal casualty and theft losses **2018–2025 (TCJA) -** Deductible only if attributable to a federally declared disaster and subject to the $100-per-casualty reduction and 10% of AGI floor. **Post-2025 (OBBB) -** Permanently extends the TCJA limitation and adds state-declared disasters for tax years beginning after 2025.	165(h)(5)(A)
Casualty & Theft Losses for Non-itemizers **Post 07-04-25 (OBBB)** – Permanently extends the 2020 disaster tax relief rules, allowing victims of qualified natural disasters to claim personal casualty losses without itemizing by adding net disaster losses to the standard deduction. The per-casualty floor remains at $500, and losses must occur in a qualified disaster area beginning on or after the incident period.	165(h)
Wagering Loss Limitations **2018–2025 (TCJA) -** §165(d) was modified to provide that the term wagering losses includes any deduction otherwise allowable incurred in carrying on any wagering transaction. The provision is intended to clarify that the limitation on losses from wagering transactions applies not only to the actual costs of wagers incurred by an individual, but to other expenses incurred by the individual in connection with the conduct of that individual's gambling activity. **Post 2025 (OBBB) -** A taxpayer's deduction for losses from wagering transactions is limited to 90% of the total amount of wagering-related deductions for the year. Losses from wagering transactions include not only direct gambling losses but also any otherwise allowable deductions incurred in carrying on a wagering activity.	165(d)

Taxes, Penalties & Tax Return Filing Issues	IRC Section
Individual Income Tax Brackets (Post 2017) - The OBBB makes the TCJA tax rate reductions and bracket changes, marriage penalty fix, and capital gains/qualified income breakpoints permanent. Thus, the seven tax rates applicable for individuals (i.e., 10%, 12%, 22%, 24%, 32%, 35%, and 37%) will remain in effect and will not revert back to the pre-2018 rates (i.e., 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%).	1(j)
AMT Exemption & Phase-Out (Post 2017) - The OBBB makes permanent the higher individual AMT exemption amounts that were put in place by the TCJA. The act also resets the AMT exemption phase-out thresholds (the income levels at which the exemption starts to phase out) to $500,000 for single filers and $1,000,000 for joint filers, effective for tax years beginning after 2025, with annual inflation indexing beginning in 2026. The OBBB also increases the phase-out rate for higher-income taxpayers from 25% to 50%.	55(d)(4)
Excise Tax on Certain Remittance Transfers (Post 2025) - The OBBB imposes a 1% excise tax on remittance transfers made by U.S. senders to foreign recipients. The tax is collected and remitted quarterly by remittance providers (who are secondarily liable if unpaid). Applies only to cash, money orders, cashier's checks, or similar instruments. Excludes transfers from U.S. financial institution accounts or those funded with U.S.-issued debit/credit cards.	OBBB Act Sec. 70604
Individual Tax Credits	**IRC Section**
Dependent Care Credit (Post 2025) – The OBBB increases the maximum credit rate to 50%, reduced by one percentage point, but not below 35%, for each $2,000 or fraction thereof by which the taxpayer's AGI exceeds $15,000. For AGIs between $43,001 and $75,000 ($86,001 and $150,000, respectively, in the case of a joint return), the credit rate is 35%. This credit rate is further phased down to 20% for AGI between $75,001 and $105,000 ($150,001 and $210,000, respectively, in the case of a joint return).	21
Child Tax & Other Dependent Credits (2018-2025) - The child tax credit (CTC) was increased to $2,000 per qualifying child. The credit was further modified to temporarily provide for a $500 nonrefundable credit for qualifying dependents other than qualifying children. The maximum amount refundable may not exceed $1,400 per qualifying child (increased for inflation). The credit begins to phase out for taxpayers with AGI in excess of $400,000 (in the case of married taxpayers filing a joint return) and $200,000 (for all other taxpayers). These phase-out thresholds are not indexed for inflation. The taxpayer is eligible for a refundable credit (the additional child tax credit) equal to 15% of earned income in excess of a threshold dollar amount (the "earned income" formula). This was reduced to a $2,500 (from $3,000) earnings threshold. In order to receive the child tax credit (i.e., both the refundable and non-refundable portion), a taxpayer must include a Social Security number for each qualifying child for whom the credit is claimed on the tax return. For these purposes, a Social Security number must be issued before the due date for the filing of the return for the taxable year. This	24(h)

requirement does not apply to a non-child dependent for whom the $500 non-refundable credit is claimed. **CTC & ODC (Post 2025) -** The OBBB makes all the TCJA changes to the CTC permanent and for tax years after 2025, the OBBB adds - 1) an increase in the nonrefundable CTC to $2,200 per qualifying child, indexed for inflation using chained CPI with 2024 as the base year and 2) a requirement that the return include the taxpayer's SSN (or one spouse's SSN for joint filers) and the qualifying child's SSN to claim the credit.	
Adoption Credit (Post 2024) – The OBBB makes the adoption credit partially refundable, allowing up to $5,000 (indexed annually for inflation) to be refunded when the credit exceeds the taxpayer's federal income tax liability..	23
Education Credits (Post 2025) – The OBBB amends §25A to require that, beginning with tax years after December 31, 2025, taxpayers must include valid Social Security numbers (SSNs) for themselves and any student for whom the **American Opportunity Tax Credit (AOTC) or Lifetime Learning Credit (LLC)** is claimed. For the AOTC, taxpayers must also report the employer identification number (EIN) of the eligible educational institution receiving tuition payments. Failure to provide a valid SSN or EIN will be treated as a mathematical or clerical error, authorizing the IRS to automatically deny the credit. These requirements are intended to improve compliance and reduce improper education credit claims.	25A(g)
ABLE Contributions (Post 2017) - The OBBB permanently allows beneficiaries who make qualified contributions to their ABLE accounts to claim the Saver's Credit. It also provides an alternative calculation method for qualified retirement contributions, elective deferrals, and voluntary employee contributions made in tax years before 2027. Beginning in the 2027 tax year, the maximum credit amount increases to $2,100.	25B(d)(1)(D)
Credit for Contributions to Scholarship Granting Organizations (SGOs) (Post 2026) - This nonrefundable tax credit allows individuals to offset 100% of eligible contributions to qualifying SGOs, up to $1,700 annually, provided the SGO supports K–12 scholarships and the taxpayer hasn't claimed a state tax credit for the same contribution.	25F
Premium Tax Credit (PTC) Repayment Cap (Post 2025) - Under prior law, taxpayers with household income generally below 400% of the federal poverty level had a limit on the amount of excess advance premium tax credit (APTC) they had to repay. The OBBB eliminates this cap for tax years after 2025, allowing full repayment of any excess premium tax credit regardless of income level.	36B(f)(2)(B) repealed
PTC Disallowed for Certain Aliens Below Poverty Line (Post 2025) - Lawfully present aliens who are ineligible for Medicaid due to immigration status must meet the 100% federal poverty line threshold to qualify for the premium tax credit.	36B(c)(1)(B) repealed
PTC Disallowed for Certain SEP Coverage (Post 2025) - Beginning with plan years after Dec. 31, 2025, individuals who enroll in coverage through a special enrollment period (SEP) based solely on low income—not tied to a qualifying life event—will not be eligible for the premium tax credit (PTC).	36B(c)(3)(A)

PTC Limited to Certain Lawfully Present Noncitizens (Post 2026) - Under the OBBB Act §71301(a), amending §36B(e)(1)), the PTC is not available for premiums attributable to lawfully present individuals outside the three "eligible alien" categories - e.g., DACA recipients, TPS holders, and nonimmigrant visa holders (such as many work, student, or visitor visas).	36B(e)(1)
PTC Eligibility to Enroll in Qualified Health Plan (Post 2027) – The OBBB amends IRC §36B to require pre-enrollment and ongoing verification of eligibility by Exchanges before months qualify for the Premium Tax Credit. Applicants must verify income, household size, lawful presence, coverage status, and residence, and Exchanges must comply with federal verification regulations. Effective for tax years after 2027, the rule eliminates "attestation-only" enrollment for PTC purposes.	36B(c)(3)(A)
Installment Payment of Tax on Gain from Sale of Qualified Farmland to Qualified Farmers (Post 07-04-25) - The OBBB allows sellers of qualified farmland property to elect to pay capital gains tax in four equal annual installments. Qualified farmland must be real property located in the U.S. that was used substantially for farming purposes for at least 10 years before the sale and is subject to restrictions against non-farm use for at least 10 years after the sale. The property may also qualify if it was leased to a qualified farmer (as defined under the Food Security Act of 1986). The first installment is due with the return for the year of sale, with the next three due with returns for the following three tax years.	1062

Individual Provisions Expiring during or after 2025

Exclusions from Income	IRC Section
Cancellation of Debt (COD) – Qualified Principal Residence Indebtedness. The exclusion for qualified principal residence indebtedness under IRC §108 was not extended by the OBBB. For discharges after 2020, the maximum exclusion amount is $750,000 ($375,000 if MFS). This provision applies to discharges of indebtedness before January 1, 2026, or those made pursuant to a binding written agreement entered into before that date.	108(a)(1)(E)
Individual Tax Credits	**IRC Section**
Clean Vehicle Credit - The Inflation Reduction Act of 2022 Act Section 13401 amended the Qualified Plug-in Electric Drive Motor Vehicle Credit (§30D), now known as the Clean Vehicle Credit, and added a new requirement for final assembly in North America that took effect on August 17, 2022, with additional requirements taking place beginning January 1, 2023. No credit shall be allowed under this section with respect to any vehicle placed in service after December 31, 2032. Reported on Form 8936 (and Schedule A). The OBBB amends §30D(h) by significantly accelerating the termination date of the clean vehicle credit, so that it now ends for vehicles acquired after September 30, 2025. It also eliminates the provisions in §30D(e) that would have required increasing percentage thresholds of critical minerals and	30D

battery components manufactured or assembled in North America for vehicles placed in service after calendar year 2026.	
Previously-Owned Clean Vehicles - The IRA of 2022 Act Section 13402 creates a new tax credit under §25E for buyers of previously owned qualified clean (plug-in electric and fuel cell) vehicles. This provision shall apply to vehicles acquired after December 31, 2022. Reported on the Form 8936 (and Schedule A). The OBBB amends §25E(g) accelerates the termination date to vehicles acquired September 30, 2025.	25E
Alternative Fuel Refueling Property Credit. This provides a credit for taxpayers that install qualified refueling or recharging property (such as an electric vehicle (EV) charger) in an eligible location. Reported on Form 8911. The OBBB amends §30C(i) and terminates the credit for property placed in service after June 30, 2026.	§30C(i)
(PTC) Premium assistance credit enhancements **Pre 2022 & Post 2025 -** Individuals who received or have been approved to receive unemployment compensation for a week or more are eligible during the taxable year for PTC as if household income is 133% above the federal poverty level (FPL), essentially making the employee contribution for premiums zero for the second-lowest cost silver plan in the marketplace. **For 2021 through 2025**, the 400% above the FPL limit for PTC eligibility is removed, the amount of PTC is increased for eligible individuals on a sliding scale based on the percentage household income above the FPL, percentage of household income range is reduced from 2% to 9.5% (adjusted for inflation) to 0% to 8.5% (annual inflation adjustments are suspended).	36B(b)(3)(A)(iii) and (c)(1)(E)

Individual Provisions Expiring after 2026

Individual Tax Credits	IRC Section
After 2026 - The nonrefundable credit (i.e., matching 50% of up to $2,000 in contributions) for individuals who make contributions to IRAs, employer retirement plans (such as 401(k) plans), and ABLE accounts is repealed and replaced. It will be changed from a credit paid in cash as part of a tax refund into a federal matching contribution that must be deposited into a taxpayer's IRA or retirement plan.	25B

Business Income Tax Provision Summary Tables

UPDATE – On July 4, 2025, President Trump signed the One Big Beautiful Bill (OBBB) into law. The legislation permanently extends the 2017 Tax Cuts and Jobs Act (TCJA) and provides additional income tax relief for both individuals and businesses.

OBBB Business Income Tax Provisions

Business Deductions & Miscellaneous Provisions	IRC Section
Corporate Charitable Contributions (Post 2025) – The OBBB adds a 1% floor (nondeductible and not carried forward) to the existing 10% ceiling on corporate charitable contributions, with the 5-year carryforward unchanged.	170
Limitation on Excess Business Losses of Non-Corporate Taxpayers **Post 2020 (OBBB) -** The OBBB permanently extends the §461(l) limitation on excess business losses and renders §461(j) inapplicable to farm losses. Thus, for taxable years beginning after December 31, 2020, excess business losses of noncorporate taxpayers are disallowed for the year and carried forward as part of the taxpayer's NOL carryforward. An "excess business loss" is the excess of (i) aggregate deductions attributable to trades or businesses (without regard to the §461(l) limitation) over (ii) the sum of aggregate gross income or gain from such businesses plus a threshold amount. The threshold (indexed for inflation) was originally $250,000 ($500,000 for joint filers). The Act changes the inflation adjustment calculation for the $250,000 amount; "2024" (and not "2017") is substituted for the "2016". For partnerships and S corporations, the limitation is applied at the partner or shareholder level.	461(l) 461(j)
Qualified business income (QBI) deduction **2018- 2025 (TCJA) -** For taxable years beginning after 2017 and before 2026, an individual taxpayer generally may deduct 20% percent of qualified business income (QBI) from a partnership, S corporation, or sole proprietorship, as well as 20% of aggregate qualified REIT dividends, qualified cooperative dividends, and qualified publicly traded partnership income. Special rules apply to specified agricultural or horticultural cooperatives. A limitation based on W-2 wages paid is phased in above a threshold amount of taxable income. A disallowance of the deduction with respect to specified service trades or businesses is also phased in above the threshold amount of taxable income. **Post 2025 (OBBB) -** Permanently extends the 20% deduction for QBI, REIT dividends, and PTP income. Adds a new inflation-adjusted minimum deduction of $400, available only if the taxpayer has at least $1,000 of QBI from one or more active trades or businesses in which the taxpayer materially participates (§469(h)). The wage/capital limitation phase-in threshold and SSTB phase-out threshold are increased to $75,000 (single) / $150,000 (joint), indexed for inflation after 2026.	199A

Business Interest Limitation **Post 2024 -** The OBBB removes the sunset on the add-back for depreciation, amortization, and depletion in the calculation of adjusted taxable income (ATI). As a result, ATI will continue to be computed without regard to these items for all taxable years beginning after 2024. (Act Sec. 70303; amends §163(j)(8)(A)(v)). **Post 2025 -** Under the OBBB, the §163(j) limitation applies before interest capitalization, allowable interest is applied first to capitalized amounts, and any carryforward is treated solely as deductible interest. (Act Sec. 70341 amends §163(j)(10)). Also, ATI must also add back Subpart F income (§951(a)), net CFC tested income (formerly GILTI, §951A(a)), and §78 gross-up amounts, along with related deductions under §245A and §250, when applying the §163(j) business interest limit." (Act Sec. 70342 amends §163(j)(8)(A)(vi)).	163(j)
Meals provided at convenience of employer **Pre 2018 -** 100% deduction for the cost of - 1) Operating an employer-provided eating facility (as defined in §132(e)(2)), including the cost of food and beverages associated with that facility (whether subsidized or provided under §132(e)(1)); or 2) Meals provided for the convenience of the employer and excludable under §119(a) (e.g., meals furnished on the employer's premises for employees so they can work through meal periods). **2018 to 2025 (TCJA) -** Employer-provided meals (§119) and employer-operated cafeterias (§132) costs reduced from 100% to 50% deductible. **Post 2025 (JCJA) -** No deduction for employer-provided meals (§119) and employer-operated cafeterias (§132) costs. **Post 2025 (OBBB) -** Exceptions - The only carve-outs are for - 1) §274(e)(8) — food or beverages sold to customers in a bona fide transaction (e.g., a restaurant or catering business selling meals). 2) §274(n)(2)(C) — special OBBB exception for certain fishing vessels and fish processing facilities north of 50° latitude.	274(o)
Moving Expense Reimbursement Exclusion **2018–2025 (TCJA) -** The exclusion from gross income and wages for qualified moving expense reimbursements (§217) was suspended, except for U.S. Armed Forces members on active duty moving under military orders. **Post-2025 (OBBB) -** The suspension was made permanent, but eligibility is expanded to include employees and new appointees of the intelligence community (as defined in the National Security Act) when relocation is required by a change in assignment.	132(g)(2)

Domestic Research or Experimental Expenditures **2022-2024 (TCJA) -** No immediate expensing allowed. Mandatory 5-year amortization (beginning with the midpoint of the taxable year in which expenses are paid/incurred). 15-year amortization for specified R&E expenditures which are attributable to research that is conducted outside of the U.S. **Post 2025 (OBBB) -** The OBBB repeals the TCJA's mandatory amortization for U.S.-based research, restoring immediate expensing for domestic R&E (with an option to amortize over at least 60 months), while foreign R&E remains subject to 15-year amortization. **Transition rules permit special elections** - (i) eligible small businesses may apply the expensing rules retroactively to post-2021 expenditures (i.e., amend prior year returns to claim deductions), and (ii) taxpayers who capitalized domestic R&E in 2022–2024 may deduct any remaining unamortized balances beginning in 2025, either in full that year or ratably over 2025–2026.	174 NEW 174A
Excessive Employee Compensation (Post 2025) - The OBBB expands §162(m) so that the $1 million deduction limit for executive compensation applies across all members of a publicly held corporation's broader controlled group, including affiliated service groups under §414(b), (c), (m), and (o). Compensation paid to a "specified covered employee" is aggregated across the group, and any excess above $1 million must be prorated among the group members. This rule applies to tax years beginning after December 31, 2025.	162(m)
Transactions between partner and partnership (Post 07-04-25) - The OBBB amends §707(a)(2) by eliminating the requirement that recharacterization of disguised sales or service/property transfers be done under IRS regulations, allowing the IRS to recharacterize such transactions directly. This change applies to services performed or property transferred after July 4, 2025, and does not affect transactions occurring on or before that date.	707(a)(2)
Bonus Depreciation **09-28-2017 to 12-31-2026 (TCJA)** - Bonus depreciation under §168(k) was extended and modified. The rate increased from 50% to 100% for qualified property placed in service after September 27, 2017 and before January 1, 2023 (January 1, 2024 for longer-production-period property and certain aircraft). The phase-down rates applied as follows - 80% (2023), 60% (2024), 40% (2025), 20% (2026). Qualified property could be new or used, and the definition was expanded to include certain film, TV, and live theatrical productions placed in service before Jan. 1, 2027. A transition election allowed taxpayers to apply 50% instead of 100% in their first taxable year ending after Sept. 27, 2017. **Post-01-19-2025 (OBBB) -** The OBBB permanently sets bonus depreciation at 100% under §168(k) for qualified property acquired after January 19, 2025. Eligible property types remain unchanged, except for adjustments to date criteria. **Transition Rule (OBBB)** - For a taxpayer's first taxable year ending after January 1, 2025, an election may be made to apply reduced bonus rates (i.e., 40% for standard qualified property and 60% for longer-production-period property, certain aircraft, and specified plants) instead of 100%.	168(k)

100% Depreciation Election for Real Property Used for Producing Tangible Personal Property (> 01-19-2025 & < 01-01-2029) - Taxpayers may elect a 100% depreciation deduction for qualified production property (QPP) in the year it is placed in service. The basis is reduced by the amount deducted. QPP includes nonresidential real property used as an integral part of a qualified production activity (QPA), such as manufacturing, refining, or agricultural or chemical production. To qualify, the original use of the property must begin with the taxpayer, construction must begin after January 19, 2025, and before January 1, 2029, and the property must be placed in service in the United States (or a U.S. possession) before January 1, 2031. Portions of the property used for non-production functions are excluded from this treatment. **Excluded property -** QPP excludes property used for offices, sales, research, software development, lodging, or administrative functions, as well as ADS property and leased property. It must meet the original use requirement, with limited exceptions for unused, unrelated-party acquisitions. **Recapture -** A 10-year recapture period applies if the property ceases to be used in a QPA. Coordination rules apply for the AMT and other first-year depreciation elections.	168(n) 1245(a)(3)(G)
5-Year MACRS for Energy Property - The OBBB eliminates 5-year MACRS classification for energy property (e.g., solar, wind, geothermal, fuel cells, energy storage) for projects beginning after 12-31-24, ending accelerated cost recovery.	168(e)(B)(iv)
Information Reporting	**IRC Section**
Information Reporting at the Source (Post 2025) - Under pre-OBBB law, businesses were required to file information returns for payments of $600 or more in a calendar year for fixed or determinable income. The OBBB raises this threshold to $2,000 for payments made after December 31, 2025, and beginning in 2027 the amount will be indexed annually for inflation (rounded to the nearest $100).	§6041
Information Reporting for Services and Direct Sales (Post 2025) - Originally enacted in 1982, §6041A required information reporting for payments for services and certain government or tax-exempt payors, using the same $600 threshold as §6041. The OBBB now ties its threshold directly to §6041, so service payments (including subcontractor payments in rental real estate) will also be subject to the new $2,000, inflation-indexed limit beginning in 2027.	§6041A
Information Reporting for Payment Card & Third Party Network Transactions (Post 2024) - The OBBB reinstates the pre-ARPA de minimis exception, so Form 1099-K reporting is required only if aggregate payments exceed $20,000 and the number of transactions exceeds 200 in a calendar year (§6050W(e)). The same $20,000/200 threshold now applies for backup withholding under §3406, meaning payments through third-party networks are reportable only if both tests are met.	§6050W

Business Credits & Investment Provisions	
Employee Retention Tax Credit (ERTC) - The OBBB cracks down on questionable ERTC claims by (i) imposing $1,000 per-failure penalties on "promoters" who fail due diligence, (ii) barring all new ERTC claims after Jan. 31, 2024, (iii) giving IRS 6 years to audit ERTC claims, and (iv) broadening the erroneous refund penalty to cover employment taxes.	OBBB Act Sec. 70605
New markets tax credit (NMTC) - The OBBB makes the NMTC permanent by amending §45D(f)(1)(H) to authorize allocations for every year after 2019. The NMTC provides a credit for qualified equity investments in qualified community development entities (CDEs) that invest in low-income communities (claimed on Form 8874). Unused allocation authority may be carried forward for up to five years; any excess from years before 2026 is treated as arising in 2025. Effective for calendar years beginning after December 31, 2025.	45D
New Energy Efficient Home Credit (Form 8908) - The OBBB amends §45L(h) to accelerate the expiration of the credit. This credit applied to eligible contractors for the construction or manufacture of energy-efficient new homes. Builders and developers may not claim the credit for homes acquired after June 30, 2026.	45L
Paid family and medical leave credit (Form 8994) - The OBBB made §45S a permanent general business credit beginning in 2026. Employers with a qualifying written policy may claim a 12.5%–25% credit for up to 12 weeks of paid family and medical leave, based on wages or qualifying insurance premiums. Employees must meet service, hours, and wage limits; state-mandated leave counts toward eligibility but not for the credit. Employers must reduce deductions for wages or premiums by the credit amount.	45S i
Advanced Manufacturing Investment (CHIPS) Credit **Pre-2026 -** Eligible taxpayers may claim a 25% credit for qualified investments in advanced manufacturing facilities whose primary purpose is the manufacture of semiconductors or semiconductor manufacturing equipment, provided the property is placed in service before January 1, 2027. **Post 2025 (OBBB) -** Beginning with property placed in service after December 31, 2025, the OBBB increases the credit rate to 35%. The eligibility rules and the January 1, 2027 cutoff remain unchanged.	48D
Opportunity Zones – The OBBB Act Section 70421 makes Opportunity Zones permanent, with redesignations every 10 years and stricter eligibility rules. It replaces the 2026 sunset with rolling 5-year deferrals, adds a 10% basis step-up (30% for rural funds), maintains the 10-year gain exclusion with a 30-year cap, and eases rural improvement tests. The law also imposes strong reporting and penalties, with Treasury required to publish annual and semi-decennial impact reports.	1400Z-1 1400Z-2 i

OBBB Subchapter A – Termination of Green New Deal Subsidies

OBBB	IRC	Credit / Deduction	OBBB Change	Effective Date
§70501	§25E	Previously-Owned Clean Vehicle Credit	Sunset accelerated	September 30, 2025
§70502	§30D	Clean Vehicle Credit (new EVs)	Sunset accelerated; conforming amendments	September 30, 2025
§70503	§45W	Qualified Commercial Clean Vehicles Credit	Sunset accelerated	September 30, 2025
§70504	§30C	Alternative Fuel Vehicle Refueling Property Credit	Sunset accelerated	June 30, 2026
§70505	§25C	Energy Efficient Home Improvement Credit	Sunset accelerated; furnace/boiler definition updated	December 31, 2025
§70506	§25D	Residential Clean Energy Credit (solar, wind, etc.)	Sunset accelerated; percentage table simplified	December 31, 2025
§70507	§179D	Energy Efficient Commercial Buildings Deduction	Sunset accelerated	Construction beginning after June 30, 2026
§70508	§45L	New Energy Efficient Home Credit	Sunset accelerated	June 30, 2026
§70509	§168	Cost Recovery for Energy Property	Accelerated repeal of bonus depreciation for certain energy property	Construction beginning after December 31, 2024
§70510	§45U	Zero-Emission Nuclear Power Production Credit	Denied to specified foreign entities (after July 4, 2025); denied to foreign-influenced entities (after July 4, 2027)	July 4, 2025 (enactment); phased restrictions through 2027
§70511	§45V	Clean Hydrogen Production Credit	Termination accelerated	January 1, 2028
§70512	§45Y	Clean Electricity Production Credit	Terminates for wind/solar after 12/31/2027; restrictions on foreign entities; special nuclear rules	Generally tax years after July 4, 2025; construction after December 31, 2025 (foreign entity rules)
§70513	§48E	Clean Electricity Investment Credit	Terminates for wind/solar after 12/31/2027; foreign entity restrictions; recapture rules; denial for leasing; domestic content changes; applies to fuel cells (30%)	Generally tax years after July 4, 2025; phase-ins 2025–2027
§70514	§45X	Advanced Manufacturing Production Credit	Modifies integrated component rules; phases out critical minerals (2031–2033);	Generally tax years after July 4, 2025;

			terminates wind components after 2027; metallurgical coal after 2029; adds metallurgical coal as a "critical mineral"; foreign entity restrictions	some rules apply 2026–2027
§70515	§48C	Advanced Energy Project Credit Program	Prohibits increases in allocation authority	July 4, 2025 (date of enactment)

OBBB Subchapter B – Enhanced America-First Energy Policies

OBBB	IRC	Credit / Deduction	OBBB Change	Effective Date
§70521	§45Z, §40A, §6426, §7701	Clean Fuel Production Credit & Agri-Biodiesel Credit	Extends §45Z credit through 2029; prohibits foreign feedstocks; no negative emission rates; excludes indirect land-use emissions; adds manure-specific rules; prevents double crediting; modifies SAF rules (no palm oil, eliminates special rate); terminates §6426(k) SAF credit Sept. 30, 2025; doubles agri-biodiesel small producer credit to $0.20/gal (through 2026); foreign entity restrictions	Effective for fuel produced/sold after December 31, 2025 (most); SAF coordination applies July 4, 2025; agri-biodiesel extension applies June 30, 2025
§70522	§45Q	Carbon Oxide Sequestration Credit	Restricts credit for prohibited foreign entities and foreign-influenced entities; harmonizes uses/utilizations (storage, EOR, utilization); adjusts credit rates ($17 base, indexed after 2026; $36 for storage/EOR)	Effective for facilities/equipment placed in service after July 4, 2025
§70523	§56A	Intangible Drilling & Development Costs (IDCs)	Allows tax deductions for IDCs to reduce AFI (book income) under corporate minimum tax; aligns treatment of depreciation, depletion, and IDC deductions	Effective for tax years after December 31, 2025
§70524	§7704	Publicly Traded Partnerships (Qualifying Income)	Expands qualifying PTP income to include hydrogen storage, carbon capture, advanced nuclear, hydropower, and geothermal	Effective for tax years after December 31, 2025
§70525	§6435	Dyed Fuel Payments	New provision allows refunds of excise tax previously paid on indelibly dyed diesel/kerosene improperly taxed; adds penalties for excessive claims	Effective 180 days after July 4, 2025

Business Provisions Expiring after 2025

Work opportunity tax credit (WOTC) - The WOTC is equal to 40% of up to $6,000 of wages paid to, or incurred on behalf of, an individual who 1) is in their first year of employment; 2) is certified as being a member of a targeted group; and 3) performs at least 400 hours of services for that employer. Thus, the maximum tax credit is generally $2,400. A 25% rate applies to wages for individuals who perform fewer than 400 but at least 120 hours of service for the employer. Up to $24,000 in wages may be taken into account in determining the WOTC for certain qualified veterans. An employer cannot claim the WOTC for employees who are rehired. Form 5884 & Form 8850	51(c)(4)
Empowerment zone tax incentives - This is a tax credit for employers who hire employees who live and work in an Empowerment Zone. Form 8844	1391 & 1394

Miscellaneous OBBB Provisions

Premium Tax Credit (PTC) Limited to Certain Lawfully Present Noncitizens (Post 2026)

PTC Background

Under Code §36B, an applicable taxpayer enrolled in a qualified health plan (QHP) through an Exchange may claim a refundable PTC. The credit is based in part on monthly premiums for one or more QHPs covering the taxpayer, spouse, and/or dependents enrolled through an Exchange. Premiums for individuals not lawfully present are not counted in computing the PTC under current law.

UPDATE - Under the OBBB Act §71301(a), amending §36B(e)(1), the PTC is not available for premiums attributable to lawfully present individuals outside the three "eligible alien" categories - e.g., DACA recipients, TPS holders, and nonimmigrant visa holders (such as many work, student, or visitor visas).

OBBB Act §71301 Changes

For individuals who are lawfully present, the OBBB creates a narrower class of "eligible aliens." Going forward, premiums attributable to lawfully present individuals who are not "eligible aliens" will not be taken into account in computing the PTC.

Who qualifies as an "eligible alien" (§36B(e)(2)):

A lawfully present individual who is, and is reasonably expected to be for the entire enrollment period for which the PTC is claimed, one of the following:

1. Lawful permanent resident under the INA (i.e., green-card holder);
2. Cuban/Haitian entrant as defined in REAA §501(e); or
3. A person lawfully residing in the U.S. under a Compact of Free Association (COFA) (FSM, RMI, Palau) per 8 U.S.C. §1612(b)(2)(G).

Exchange verification & conforming changes

ACA §1411/§1412 are amended to require attestation/verification of eligible-alien status when determining PTC eligibility and advance payments; related MEC terminology is aligned by amending §5000A(d)(3) to reference "eligible alien."

Effective dates

- PTC/MEC changes: Tax years beginning after December 31, 2026.
- Exchange verification/attestation changes: Plan years beginning on or after January 1, 2027.

Trump Accounts (§530A) (Post 2025)

UPDATE – The OBBB enacted new IRC §530A effective for taxable years beginning after 2025.

Trump Accounts (§530A(a) &(b))

NOTE - Except as provided in this section or under regulations or guidance established by the Secretary, a Trump account shall be treated for purposes of this title in the same manner as an individual retirement account under §408(a).

In general

The term "Trump account" means an individual retirement account (as defined in §408(a)) which is not designated as a Roth IRA and which meets the following requirements:

1. The account-
    a. is created or organized by the Secretary for the exclusive benefit of an eligible individual or such eligible individual's beneficiaries, or
    b. is-
        i. created or organized in the United States for the exclusive benefit of an individual who has not attained the age of 18 before the end of the calendar year, or such individual's beneficiaries, and
        ii. funded by a qualified rollover contribution.
2. The **account is designated** (in such manner as the Secretary shall prescribe) at the time of the establishment of the account **as a Trump account**.
3. The **written governing instrument** creating the account meets the following requirements:
    a. No contribution will be accepted-
        i. before the date that is 12 months after the date of the enactment (July 4, 2025) of this section, or
        ii. in the case of a contribution made in any calendar year before the calendar year in which the account beneficiary attains age 18, if such contribution would result in aggregate contributions (other than exempt contributions) for such calendar year in excess of the annual contribution limit.
    b. Except as provided in §530A(d), no distribution will be allowed before the first day of the calendar year in which the account beneficiary attains age 18.
    c. No part of the account funds will be invested in any asset other than an eligible investment during any period before the first day of the calendar year in which the account beneficiary attains age 18.

Eligible individual

The term "eligible individual" means any individual-

1. who has **not attained the age of 18** before the close of the calendar year in which the election under subparagraph 3 is made,
2. for whom a **social security number** (within the meaning of §24(h)(7)) has been issued before the date on which an election under subsection 3 is made, and
3. for whom an election is made –
    a. by the Secretary based on IRS data (if criteria met and no prior election), or
    b. by another person (e.g., parent/guardian) per IRS rules.

Eligible investment

The term "eligible investment" means any mutual fund or exchange traded fund which-

1. tracks the returns of a qualified index,
2. does not use leverage,
3. does not have annual fees and expenses of more than 0.1% of the balance of the investment in the fund, and
4. meets such other criteria as the Secretary determines appropriate for purposes of this section.

Qualified index

The term "qualified index" means:

1. the Standard and Poor's 500 stock market index, or
2. any other index-
    a. which is comprised of equity investments in primarily United States companies, and
    b. for which regulated futures contracts (as defined in §1256(g)(1)) are traded on a qualified board or exchange (as defined in §1256(g)(7)).

NOTE - Such term shall not include any industry or sector-specific index, but may include an index based on market capitalization.

Account beneficiary

The term "account beneficiary" means the individual on whose behalf the Trump account was established.

Treatment of contributions (§530A(c))

No deduction allowed

No deduction shall be allowed under §219 for any contribution which is made before the first day of the calendar year in which the account beneficiary attains age 18.

Contribution limit

In the case of any contribution made before the calendar year in which the account beneficiary attains age 18, the aggregate amount of contributions (other than exempt contributions) for such calendar year shall not exceed $5,000 (adjusted for inflation in $100 increments after 2027).

Exempt contribution

The term "exempt contribution" means-

1. a qualified rollover contribution,
2. any qualified general contribution, or
3. any contribution provided under §6434 (i.e., Federal government $1,000 contributions to Trump accounts under pilot program).

Timing of contributions

The §219(f)(3) rule allowing IRA contributions to be made up to the due date of the return (generally April 15 of the following year) shall not apply to any contribution made to a Trump account for any taxable year ending before the calendar year in which the account beneficiary attains age 18.

Certain Contributions to Trump Accounts (§139J)

Gross income of an account beneficiary shall not include any qualified general contribution to a Trump account of the account beneficiary.

NOTE - Any term used in this section which is used in §530A shall have the meaning given such term under §530A.

Distributions (§530A(d))

In general – No distribution before age 18

Except as otherwise provided in this subsection, no distribution shall be allowed before the first day of the calendar year in which the account beneficiary attains age 18.

Tax treatment of allowable distributions

For purposes of applying §72 to any amount distributed from a Trump account, the investment in the contract shall not include-

1. any qualified general contribution,
2. any contribution provided under §6434 (i.e., Federal government $1,000 contributions to Trump accounts under pilot program), and
3. the amount of any contribution which is excluded from gross income under §128 (i.e., employer contributions to Trump accounts).

Qualified rollover contributions

The no distribution before age 18 rule shall not apply to any distribution which is a qualified rollover contribution and the amount of such distribution shall not be included in the gross income of the beneficiary.

Qualified ABLE rollover contributions

The no distribution before age 18 rule shall not apply to any distribution which is a qualified ABLE rollover contribution and the amount of such distribution shall not be included in the gross income of the beneficiary. The term "qualified ABLE rollover contribution" means an amount which is paid during the calendar year in which the account beneficiary attains age 17 in a direct trustee-to-trustee transfer from a Trump account maintained for the benefit of the account beneficiary to an ABLE account (as defined in §529A(e)(6)) for the benefit of the such account beneficiary, but only if the amount of such payment is equal to the entire balance of the Trump account from which the payment is made.

Distributions of excess contributions

In the case of any contribution which is made before the calendar year in which the account beneficiary attains age 18 and which is in excess of the annual contribution limitation in effect for the calendar year:

1. The general restriction on early distributions does not apply to removing the excess amount.
2. The excess amount withdrawn is not included in the beneficiary's gross income.
3. The distributee's tax for the year of the distribution is increased by 100% of the net income attributable to the excess contribution (determined without regard to item 2 above).

NOTE - Withdraw the excess contribution (and its earnings) as soon as discovered to avoid the 100% tax on earnings.

Treatment of death of account beneficiary
If, by reason of the death of the account beneficiary before the first day of the calendar year in which the account beneficiary attains age 18, any person acquires the account beneficiary's interest in the Trump account-

1. The early distribution restriction does not apply.
2. Such account shall cease to be a Trump account as of the date of death, and
3. The fair market value of the account assets on the date of death, reduced by the investment in the contract, is taxable as follows:
    a. **If the recipient is not the beneficiary's estate:** The amount is included in the recipient's gross income for the tax year that includes the date of death.
    b. **If the recipient is the beneficiary's estate:** The amount is included in the beneficiary's gross income for their final tax year.

Qualified rollover contribution (§530A(e))
For purposes of this section, the term "qualified rollover contribution" means an amount which is paid in a direct trustee-to-trustee transfer from a Trump account maintained for the benefit of the account beneficiary to a Trump account maintained for such beneficiary, but only if the amount of such payment is equal to the entire balance of the Trump account from which the payment is made.

Qualified general contribution (§530A(f))

Definition
A qualified general contribution is a contribution that meets all of the following:

1. Made by the Secretary pursuant to a general funding contribution.
2. Directed to the Trump account of an account beneficiary who is part of the qualified class specified in the general funding contribution.
3. Amount per beneficiary equals:
   (Total general funding contribution) ÷ (Number of beneficiaries in the qualified class)

General funding contribution
A general funding contribution is a contribution that:

1. Is made by either:
    a. An entity described in §170(c)(1) (excluding U.S. possessions or their political subdivisions) or an Indian tribal government, or
    b. An organization described in §501(c)(3) and exempt under §501(a).
2. Specifies the qualified class of account beneficiaries to receive the contribution.

NOTE - Qualified general contributions to Trump accounts from tax-exempt entities, such as private foundations, are not subject to the $5,000 annual limit. These third-party contributions must be made to all eligible children within a qualified group (e.g., all children in a state, a specific school district, or an educational institution).

Qualified Class
A qualified class means any of the following groups:

1. All account beneficiaries under age 18 before the end of the calendar year in which the contribution is made.
2. All beneficiaries under age 18 and residing in one or more states or other qualified geographic areas specified in the general funding contribution.
3. All beneficiaries under age 18 and born in one or more calendar years specified in the general funding contribution.

NOTE - A qualified geographic area is a geographic area with at least 5,000 account beneficiaries, and designated as such by the Secretary.

Trustee selection (§530A(g))

In the case of any Trump account created or organized by the Secretary, the Secretary shall take into account the following criteria in selecting the trustee:

1. The history of reliability and regulatory compliance of the trustee.
2. The customer service experience of the trustee.
3. The costs imposed by the trustee on the account or the account beneficiary.

Other special rules and coordination with IRA rules (§530A(h))

- **Inapplicable IRA Provisions**: Certain IRA rules under §408 (subsections (k), (p), (d), and (i)) do not apply to Trump accounts until the year the beneficiary turns 18.
- **Custodial Account Definition:** §408(h) is modified so that "Trump account" replaces "IRA" in the custodial account definition.
- **Contribution Limits:** Before age 18, Trump account contributions are not counted toward contribution limits for any other IRA or retirement plan.
- **Separate Distribution Rules**: The IRA pro-rata distribution rules (§408(d)(2)) are applied separately for Trump accounts and other IRAs.
- **Excess Contributions:** For beneficiaries under 18, "excess contributions" means amounts exceeding the annual Trump account limit under §530A(c)(2), plus any carryover excess from the prior year, reduced by timely-distributed excesses under §530A(d)(5).

Reporting Requirements (§530A(i))

Annual Reporting

Trustees must report to both the IRS and the account beneficiary, including:

- Contributions (and the amount/source for any >$25 from a third party other than the Secretary, beneficiary, or parent/guardian).
- Distributions (including qualified rollovers).
- Fair market value of the account.
- Investment in the contract.
- Other information required by the IRS.

30-Day Rollover Reporting

For each qualified rollover contribution, trustees must report to the IRS within 30 days, including:

- Beneficiary's name, address, and SSN.
- Trustee's name and address.
- Account and routing numbers.
- Any other information required by the IRS.

End of Reporting Period

Reporting obligations cease after the calendar year in which the beneficiary turns 17.

§530A Trump Accounts		
Provision	**Summary**	**Key Details / Limits**
General Rule (§530A(a))	Trump accounts generally treated as traditional IRAs under §408(a) unless otherwise specified.	Subject to unique rules in §530A.
Definition (§530A(b)(1))	An IRA (non-Roth) created by the Secretary or privately for a minor under 18, funded by qualified rollover or contributions.	Must be designated a "Trump account" at setup; restrictions on contributions, distributions, and investments until age 18.
Eligible Individual (§530A(b)(2))	Individual under age 18 with SSN issued before election date; only one election allowed per person.	Election may be made by Secretary or other person as prescribed.
Eligible Investment (§530A(b)(3))	Certain low-cost index funds (S&P 500 or similar) meeting strict criteria.	≤0.1% annual expenses; no leverage; U.S. equity focus; no sector-specific indexes.
Contribution Rules (§530A(c))	No deduction allowed before age 18; annual limit $5,000 before age 18 (indexed after 2027).	Exempt contributions: qualified rollovers, qualified general contributions, §6434 contributions.
Timing (§530A(c)(3))	§219(f)(3) April 15 timing rule does not apply before age 18.	Contributions must be made in the same tax year.
Distributions (§530A(d))	Generally no distributions allowed before age 18.	Exceptions: qualified rollovers, ABLE rollovers at age 17, excess contributions, death of beneficiary.
Excess Contributions (§530A(d)(5))	Excess amounts returned tax-free; 100% penalty on earnings from excess.	Applies before age 18.
Death Before Age 18 (§530A(d)(6))	Account ceases to be a Trump account; FMV less investment in contract is taxable to inheritor or estate.	
Qualified Rollover Contribution (§530A(e))	Full trustee-to-trustee transfer of entire account balance to another Trump account for same beneficiary.	
Qualified General Contribution (§530A(f))	Funded by Secretary from certain governmental or charitable sources to a class of beneficiaries.	Class can be all minors, minors in a certain area, or minors born in certain years.
Trustee Selection (§530A(g))	Secretary must consider reliability, service, and cost.	Applies when Secretary creates the account.
Special Rules (§530A(h))	Certain IRA rules do not apply before age 18; contributions before age 18 don't count toward other IRA limits; distributions treated separately from other IRAs.	Excess contributions defined separately for pre-age-18 years.
Reporting (§530A(i))	Trustee must report contributions, distributions, FMV, contract investment, and other data annually to IRS and beneficiary.	30-day IRS report for rollovers; reporting ends after year beneficiary turns 17.

Trump Accounts Contribution Pilot Program (§6434)

General Rule (§6434(a))
In the case of an individual who makes an election under this section with respect to an eligible child of the individual, such eligible child shall be treated as making a payment against the tax imposed by subtitle A (for the taxable year for which the election was made) in an amount equal to $1,000.

Refund of payment (§6434(b))
The $1,000 amount is refunded by the IRS and deposited directly into the Trump account for which the child is the account beneficiary.

Eligible child (§6434(c))
The term "eligible child" means a qualifying child (as defined in §152(c)):
1. who is born after December 31, 2024, and before January 1, 2029,
2. with respect to whom no prior election has been made under this section by such individual or any other individual, and
3. who is a United States citizen.

Election (§6434(d))
An election under this section shall be made at such time and in such manner as the Secretary shall provide.

Social security number required (§6434(e))
This section shall not apply to any taxpayer unless such individual includes with the election made under this section the social security number (as defined in §24(h)(7)) of the eligible child with respect to whom the election is made.

Exception from reduction or offset (§6434(f))
Any payment made to any individual under this section shall not be-
1. subject to reduction or offset pursuant to §6402(c), (d), (e), or (f) or any similar authority permitting offset (i.e., pay child support, federal or state debts, or other obligations normally collected through IRS refund offsets), or
2. reduced or offset by other assessed Federal taxes that would otherwise be subject to levy or collection.

Special rule regarding interest (§6434(g))
The period determined under §6611(a) with respect to any payment under this section shall not begin before January 1, 2028. Thus, if the IRS owes interest on a Trump account payment under §6611(a), the clock for calculating that interest won't start until January 1, 2028, regardless of when the payment is processed.

Mirror code possessions (§6434(g))
In the case of any possession of the United States with a mirror code tax system (as defined in §24(k)), this section shall not be treated as part of the income tax laws of the United States for purposes of determining the income tax law of such possession unless such possession elects to have this section be so treated.

Definitions
For purposes of this section, the terms "Trump account" and "account beneficiary" have the meaning given such terms in §530A(b).

Employer Contributions to Trump Accounts (§128)

UPDATE – The OBBB enacted new IRC §128 effective for taxable years beginning after 2025.

General Rule

Gross income of an employee does not include amounts paid by the employer as a contribution to the Trump account of such employee or of any dependent of such employee if the amounts are paid or incurred pursuant to a Trump account contribution program (described in §128(c)).

Annual Limitation

The amount which may be excluded with respect to any employee shall not exceed $2,500.

NOTE – After 2027, the $2,500 amount will be increased in $100 increments for inflation.

Trump account contribution program

A Trump account contribution program is a separate written plan of an employer for the exclusive benefit of his employees to provide contributions to the Trump accounts of such employees or dependents of such employees which meets requirements similar to the requirements of a dependent care assistance program under §129(d)(2), (3), (6), (7), and (8).

§129(d) Requirements for Dependent Care Assistance Programs		
Subsection	**Rule**	**Requirement**
§129(d)(2)	Non-discrimination	Contributions or benefits must **not favor highly compensated employees** (per §414(q)).
§129(d)(3)	Eligibility	The plan must benefit employees who qualify under the employer's classification, **not biased toward highly compensated employees**.
§129(d)(6)	Notification	**Reasonable notice** of the program's availability and terms must be provided to eligible employees.
§129(d)(7)	Year-end Statement	Employers must provide a **written statement by January 31** detailing the dependent care assistance paid/incurred in the prior calendar year.
§129(d)(8)	Collective Bargaining Exception	Benefits are allowed for employees covered by bona fide **collective bargaining agreements**, if dependent care was subject to genuine negotiation.

Qualified Tuition Programs (QTP) – 529 Plans (§529)

529 Plans Background

A Qualified Tuition Program (QTP), also known as a 529 plan, is a program established and maintained by a state (or an agency or instrumentality of a state) or by an eligible educational institution to allow individuals to:

1. **Prepayment Plan** - allows people to prepay all or part of a designated beneficiary's qualified higher education expenses, usually limited to tuition;
2. **Savings Plan -** which allows people to make contributions to a special account established for the purpose of accumulating earnings that can later be withdrawn to pay a designated beneficiary's "qualified higher education expenses" (which are more broadly defined).

NOTE - Educational institutions may only offer prepaid tuition programs, while state-sponsored plans may offer account-based programs.

Contributions

- Contributions are not deductible for federal income tax purposes (some states may offer deductions or credits).
- Earnings grow tax-free while in the plan.
- Contributions to a 529 plan are treated as present interest gifts to the beneficiary subject to the annual gift tax exclusion under §2503(b).
- Under IRC §529(c)(2)(B) and Reg. §1.529-5(b)(2), donors may elect to treat a single 529 plan contribution as made ratably over five years for gift tax purposes.
- Contributions must not exceed what is reasonably necessary to cover anticipated education expenses.
- Each plan sets a maximum contribution limit per beneficiary - consult the plan administrator for details.

Distributions

- Distributions from a QTP will be reported on *Form 1099-Q - Payments from Qualified Education Programs (Under Sections 529 and 530)*.
- Qualified distributions are not subject to federal income tax.
- Nonqualified distributions - earnings portion is subject to income tax and generally a 10% penalty, unless an exception applies (e.g., death, disability, scholarship).

Special Roth IRA Rollover (Post 2023)

Under the SECURE 2.0 Act and as codified in §529(c)(3)(E), qualified rollovers from a QTP to a Roth IRA are permitted if:

1. the Roth IRA is in the name of the QTP beneficiary,
2. the QTP has been open for at least 15 years.
3. the rollover is completed via direct trustee-to-trustee transfer,
4. contributions and earnings distributed do not include amounts contributed in the last 5 years, and
5. the rollover is subject to the Roth IRA annual contribution limit and a $35,000 lifetime cap.

K–12 Education Expenses (§529(e)(3))

The definition of QHEEs for K–12 education includes:

- Tuition
- Curriculum and curricular materials
- Books or instructional materials
- Online educational materials
- Tutoring or supplemental instruction (subject to licensing or credentialing rules)
- Standardized testing and entrance exams (e.g., ACT, SAT, AP)
- Dual enrollment in higher ed institutions
- Educational therapies for students with disabilities

UPDATE – The OBBB increases the annual cap increased from $10,000 to $20,000 per beneficiary, effective tax years beginning after December 31, 2025.

Postsecondary Education Expenses (College and Beyond) (§529(e)(3))

The definition of QHEEs for postsecondary education includes:

- Tuition, fees, books, supplies, and equipment required for enrollment or attendance at an eligible postsecondary institution.
- Room and board (if enrolled at least half-time).
- Expenses for registered apprenticeship programs, including tools and equipment.
- Up to $10,000 per individual (lifetime) for qualified education loan repayments (for the beneficiary or a sibling).

Postsecondary Credentialing Expenses (NEW §529(f))

Under the OBBB new IRC §529(f), distributions after July 4, 2025 may also be used for qualified postsecondary credentialing expenses, defined as:

Covered Expenses

- Tuition, fees, books, supplies, and equipment required for participation in a recognized postsecondary credential program.
- Required testing fees to obtain or maintain such credentials.
- Required continuing education to maintain the credential.

Recognized Postsecondary Credential Program must meet at least one of the following:

- Listed on a state-approved list under the Workforce Innovation and Opportunity Act (WIOA)
- Included in the WEAMS directory (Veterans Benefits Administration)
- Prepares individuals for nationally recognized credentialing exams
- Identified by the Secretary of the Treasury (in consultation with the Secretary of Labor) as reputable

Recognized Postsecondary Credentials include:

- Credentials accredited by ICE, NCCA, or ANSI
- Programs in the DoD COOL directory
- Apprenticeship completion certificates registered with the U.S. Department of Labor
- Occupational or professional licenses, and associated certifications
- WIOA-defined postsecondary credentials

Federal Scholarship Contribution Credit & Exclusion (Post 2026)

UPDATE – The OBBB Act Section 70411 establishes a new federal income tax credit under §25F for individuals who contribute cash to eligible scholarship-granting organizations (SGOs). A related exclusion under §139K allows qualifying scholarship amounts received by eligible students to be excluded from gross income. Effective for tax years ending after December 31, 2026.

Credit for Contributions to SGOs (§25F)

Eligible individuals (U.S. citizens or residents) may claim a nonrefundable credit equal to the total amount of qualified cash contributions made to approved SGOs during the taxable year.

- **Annual Limit**: $1,700 per taxpayer.
- **Coordination with State Credits:** The federal credit is reduced by any state income tax credit claimed for the same contribution.
- **Carryforward Provision**: Unused credit amounts may be carried forward up to 5 years.
- **No Double Tax Benefit:** Contributions claimed for this credit cannot also be deducted under IRC §170 as charitable contributions.

Definition and Requirements for SGOs

To qualify, a scholarship-granting organization (SGO) must:

1. Be a 501(c)(3) public charity, but not a private foundation.
2. Maintain separate accounts for qualified contributions to prevent commingling with other funds.
3. Be included on a list of approved SGOs provided annually to the IRS by a participating state.
4. Provide scholarships to 10 or more students not all attending the same school.
5. Spend at least 90% of income on scholarships.
6. Fund only qualified elementary and secondary education expenses as defined in IRC §530(b)(3)(A).
7. Use an objective method for income verification and prioritize:
   a. Students previously awarded a scholarship.
   b. Siblings of previous recipients.
   c. Not earmark contributions for specific students.

NOTE – A SGO may not award a scholarship to any disqualified persons (defined under IRC §4946).

Eligible Students

To qualify for a scholarship:

1. The student must come from a household with income ≤ 300% of Area Median Gross Income (AMGI) (as defined under IRC §42).
2. The student must be eligible to enroll in a public elementary or secondary school.

State List of SGOs

Only states that voluntarily submit an annual, certified list of Scholarship Granting Organizations (SGOs) to the IRS will be treated as "covered states." The submission must come from the Governor or authorized designee, and the IRS will issue regulations to govern enforcement, recordkeeping, and reporting.

Exclusion for Scholarships (§139K)

Any scholarship amount received for qualified elementary or secondary education expenses from an eligible SGO is excluded from gross income. This applies to amounts received by the taxpayer or their dependent.

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Appendix TF – Tax Forms

NOTE – IRS releases draft versions of the forms, instructions & publications before finalizing them.
* Click here to see **Current** forms, instructions & publications.
* Click here to see **Draft** forms, instructions & publications.

Table of Contents

Individual Tax Forms 3
- Form 1040 - U.S. Individual Income Tax Return 3
- Schedule 1 (Form 1040) – Additional Income and Adjustments to Income 5
- Schedule 1-A (Form 1040) – Additional Deductions 7
- Schedule 2 (Form 1040) – Additional Taxes 9
- Schedule 3 (Form 1040) – Additional Credits and Payments 11

S Corporation Tax Forms 13
- Form 1120S – U.S. Income Tax Return for an S Corporation 13
- Schedule K-1 (Form 1120S) – Shareholder's Share of Income, Credits, Deductions, etc. 19
- Schedule K-1 (Form 1120S) – Instruction Codes 21

Partnership Tax Forms 23
- Form 1065 – U.S. Return of Partnership Income 23
- Schedule K-1 (Form 1065) – Partner's Share of Income, Deductions, Credits etc. 29
- Schedule K-1 (Form 1065) – Instruction Codes 31

Form **1040** Department of the Treasury—Internal Revenue Service
U.S. Individual Income Tax Return
TF-3 **2025** OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.

For the year Jan. 1–Dec. 31, 2025, or other tax year beginning , 2025, ending , 20 See separate instructions.

☐ Filed pursuant to section 301.9100-2 ☐ Combat zone ☐ Deceased MM / DD / YYYY Spouse MM / DD / YYYY

☐ Other

Your first name and middle initial	Last name	**Your social security number**
If joint return, spouse's first name and middle initial	Last name	**Spouse's social security number**

Home address (number and street). If you have a P.O. box, see instructions.	Apt. no.	Check here if your main home, and your spouse's if filing a joint return, was in the U.S. for more than half of 2025. ☐

City, town, or post office. If you have a foreign address, also complete spaces below.	State	ZIP code	**Presidential Election Campaign** Check here if you, or your spouse if filing jointly, want $3 to go to this fund. Checking a box below will not change your tax or refund. ☐ **You** ☐ **Spouse**
Foreign country name	Foreign province/state/county	Foreign postal code	

Filing Status

Check only one box.

☐ Single
☐ Married filing jointly (even if only one had income)
☐ Married filing separately (MFS). Enter spouse's SSN above and full name here:
☐ Head of household (HOH)
☐ Qualifying surviving spouse (QSS)
If you checked the HOH or QSS box, enter the child's name if the qualifying person is a child but not your dependent:

☐ If treating a nonresident alien or dual-status alien spouse as a U.S. resident for the entire tax year, check the box and enter their name (see instructions and attach statement if required):

Digital Assets

At any time during 2025, did you: (a) receive (as a reward, award, or payment for property or services); or (b) sell, exchange, or otherwise dispose of a digital asset (or a financial interest in a digital asset)? (See instructions.) . . ☐ **Yes** ☐ **No**

Dependents

(see instructions)

If more than four dependents, see instructions and check here . . ☐

	Dependent 1	Dependent 2	Dependent 3	Dependent 4
(1) First name				
(2) Last name				
(3) SSN				
(4) Relationship				
(5) Check if lived with you more than half of 2025	(a) ☐ Yes (b) ☐ And in the U.S.	(a) ☐ Yes (b) ☐ And in the U.S.	(a) ☐ Yes (b) ☐ And in the U.S.	(a) ☐ Yes (b) ☐ And in the U.S.
(6) Check if	☐ Full-time student ☐ Permanently and totally disabled	☐ Full-time student ☐ Permanently and totally disabled	☐ Full-time student ☐ Permanently and totally disabled	☐ Full-time student ☐ Permanently and totally disabled
(7) Credits	☐ Child tax credit ☐ Credit for other dependents	☐ Child tax credit ☐ Credit for other dependents	☐ Child tax credit ☐ Credit for other dependents	☐ Child tax credit ☐ Credit for other dependents

☐ Check if your filing status is MFS or HOH and you lived apart from your spouse for the last 6 months of 2025, or you are legally separated according to your state law under a written separation agreement or a decree of separate maintenance and you did not live in the same household as your spouse at the end of 2025.

Income

Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld.

If you did not get a Form W-2, see instructions.

Attach Sch. B if required.

1a	Total amount from Form(s) W-2, box 1 (see instructions)	1a	
b	Household employee wages not reported on Form(s) W-2	1b	
c	Tip income not reported on line 1a (see instructions)	1c	
d	Medicaid waiver payments not reported on Form(s) W-2 (see instructions)	1d	
e	Taxable dependent care benefits from Form 2441, line 26	1e	
f	Employer-provided adoption benefits from Form 8839, line 31	1f	
g	Wages from Form 8919, line 6	1g	
h	Other earned income (see instructions). Enter type and amount:	1h	
i	Nontaxable combat pay election (see instructions) . . . 1i		
z	Add lines 1a through 1h	1z	
2a	Tax-exempt interest . . . 2a ____ b Taxable interest	2b	
3a	Qualified dividends . . . 3a ____ b Ordinary dividends	3b	
c	Check if your child's dividends are included in 1 ☐ Line 3a 2 ☐ Line 3b		
4a	IRA distributions . . . 4a ____ b Taxable amount	4b	
c	Check if (see instructions) 1 ☐ Rollover 2 ☐ QCD 3 ☐		
5a	Pensions and annuities . . 5a ____ b Taxable amount	5b	
c	Check if (see instructions) 1 ☐ Rollover 2 ☐ PSO 3 ☐		
6a	Social security benefits . . 6a ____ b Taxable amount	6b	
c	If you elect to use the lump-sum election method, check here (see instructions) ☐		
d	If you are married filing separately and lived apart from your spouse the entire year (see inst.), check here ☐		
7a	Capital gain or (loss). Attach Schedule D if required	7a	
b	Check if: ☐ Schedule D not required ☐ Includes child's capital gain or (loss)		
8	Additional income from Schedule 1, line 10	8	
9	Add lines 1z, 2b, 3b, 4b, 5b, 6b, 7a, and 8. This is your **total income**	9	
10	Adjustments to income from Schedule 1, line 26	10	
11a	Subtract line 10 from line 9. This is your **adjusted gross income**	11a	

Tax and Credits

11b	Amount from line 11a (adjusted gross income)	11b	
12a	Someone can claim ☐ You as a dependent ☐ Your spouse as a dependent		
b	☐ Spouse itemizes on a separate return **c** ☐ You were a dual-status alien		
d	**You:** ☐ Were born before January 2, 1961 ☐ Are blind		
	Spouse: ☐ Was born before January 2, 1961 ☐ Is blind		
e	**Standard deduction or itemized deductions** (from Schedule A)	12e	
13a	Qualified business income deduction from Form 8995 or Form 8995-A	13a	
b	Additional deductions from Schedule 1-A, line 38	13b	
14	Add lines 12e, 13a, and 13b	14	
15	Subtract line 14 from line 11b. If zero or less, enter -0-. This is your **taxable income**	15	
16	**Tax** (see instructions). Check if any from Form(s): 1 ☐ 8814 2 ☐ 4972 3 ☐ ______	16	
17	Amount from Schedule 2, line 3	17	
18	Add lines 16 and 17	18	
19	Child tax credit or credit for other dependents from Schedule 8812	19	
20	Amount from Schedule 3, line 8	20	
21	Add lines 19 and 20	21	
22	Subtract line 21 from line 18. If zero or less, enter -0-	22	
23	Other taxes, including self-employment tax, from Schedule 2, line 21	23	
24	Add lines 22 and 23. This is your **total tax**	24	

Standard deduction for—
- Single or Married filing separately, $15,750
- Married filing jointly or Qualifying surviving spouse, $31,500
- Head of household, $23,625
- If you checked a box on line 12a, 12b, 12c, or 12d, see inst.

Payments and Refundable Credits

25	Federal income tax withheld from:				
a	Form(s) W-2	25a			
b	Form(s) 1099	25b			
c	Other forms (see instructions)	25c			
d	Add lines 25a through 25c			25d	
26	2025 estimated tax payments and amount applied from 2024 return			26	
	If you made estimated tax payments with your former spouse in 2025, enter their SSN (see instructions):				
27a	Earned income credit (EIC)	27a			
b	Clergy filing Schedule SE (see instructions) ☐				
c	If you do not want to claim the EIC, check here ☐				
28	Additional child tax credit (ACTC) from Schedule 8812. If you do not want to claim the ACTC, check here ☐	28			
29	American opportunity credit from Form 8863, line 8	29			
30	Refundable adoption credit from Form 8839, line 13	30			
31	Amount from Schedule 3, line 15	31			
32	Add lines 27a, 28, 29, 30, and 31. These are your **total other payments and refundable credits**			32	
33	Add lines 25d, 26, and 32. These are your **total payments**			33	

If you have a qualifying child, you may need to attach Sch. EIC.

Refund

34	If line 33 is more than line 24, subtract line 24 from line 33. This is the amount you **overpaid**	34	
35a	Amount of line 34 you want **refunded to you**. If Form 8888 is attached, check here ☐	35a	
b	Routing number **c** Type: ☐ Checking ☐ Savings		
d	Account number		
36	Amount of line 34 you want **applied to your 2026 estimated tax** — 36		

Direct deposit? See instructions.

Amount You Owe

37	Subtract line 33 from line 24. This is the **amount you owe**. For details on how to pay, go to *www.irs.gov/Payments* or see instructions	37	
38	Estimated tax penalty (see instructions) — 38		

Third Party Designee

Do you want to allow another person to discuss this return with the IRS? See instructions. ☐ **Yes.** Complete below. ☐ **No**

Designee's name | Phone no. | Personal identification number (PIN)

Sign Here

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature	Date	Your occupation	If the IRS sent you an Identity Protection PIN, enter it here (see inst.)
Spouse's signature. If a joint return, **both** must sign.	Date	Spouse's occupation	If the IRS sent your spouse an Identity Protection PIN, enter it here (see inst.)
Phone no.	Email address		

Joint return? See instructions. Keep a copy for your records.

Paid Preparer Use Only

Preparer's name	Preparer's signature	Date	PTIN	Check if: ☐ Self-employed
Firm's name			Phone no.	
Firm's address			Firm's EIN	

SCHEDULE 1 (Form 1040)

Department of the Treasury
Internal Revenue Service

Additional Income and Adjustments to Income

Attach to Form 1040, 1040-SR, or 1040-NR.

Go to *www.irs.gov/Form1040* for instructions and the latest information.

OMB No. 1545-0074

2025

Attachment Sequence No. **01**

Name(s) shown on Form 1040, 1040-SR, or 1040-NR | **Your social security number**

For 2025, enter the amount reported to you on Form(s) 1099-K that was included in error or for personal items sold at a loss . . . . ______

Note: The remaining amounts reported to you on Form(s) 1099-K should be reported elsewhere on your return depending on the nature of the transaction. See *www.irs.gov/1099k*.

Part I Additional Income

1	Taxable refunds, credits, or offsets of state and local income taxes			1	
2a	Alimony received			2a	
b	Date of original divorce or separation agreement (see instructions): Pre-2019 = income				
3	Business income or (loss). Attach Schedule C			3	
4	Other gains or (losses). Check if any from Form(s): ☐ 4797 ☐ 4684			4	
5	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E			5	
6	Farm income or (loss). Attach Schedule F			6	
7	Unemployment compensation. If you repaid a 2025 overpayment (see instructions), check here ☐ and enter amount repaid: ______			7	
8	Other income:				
a	Net operating loss	8a	( )		
b	Gambling	8b			
c	Cancellation of debt	8c			
d	Foreign earned income exclusion from Form 2555	8d	( )		
e	Income from Form 8853	8e			
f	Income from Form 8889	8f			
g	Alaska Permanent Fund dividends	8g			
h	Jury duty pay	8h			
i	Prizes and awards	8i			
j	Activity not engaged in for profit income	8j			
k	Stock options	8k			
l	Income from the rental of personal property if you engaged in the rental for profit but were not in the business of renting such property	8l			
m	Olympic and Paralympic medals and USOC prize money (see instructions)	8m			
n	Section 951(a) inclusion (see instructions)	8n			
o	Section 951A(a) inclusion (see instructions)	8o			
p	Section 461(l) excess business loss adjustment	8p			
q	Taxable distributions from an ABLE account (see instructions)	8q			
r	Scholarship and fellowship grants not reported on Form W-2	8r			
s	Nontaxable amount of Medicaid waiver payments included on Form 1040, line 1a or 1d	8s	( )		
t	Pension or annuity from a nonqualifed deferred compensation plan or a nongovernmental section 457 plan	8t			
u	Wages earned while incarcerated	8u			
v	Digital assets received as ordinary income not reported elsewhere. See instructions	8v			
z	Other income. List type and amount: ______	8z			
9	Total other income. Add lines 8a through 8z			9	
10	Combine lines 1 through 7 and 9. This is your **additional income**. Enter here and on Form 1040, 1040-SR, or 1040-NR, line 8			10	

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 71479F **Schedule 1 (Form 1040) 2025** Created 3/17/25

Part II Adjustments to Income

11	Educator expenses			11	
12	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106			12	
13	Health savings account deduction. Attach Form 8889			13	
14	Moving expenses for members of the Armed Forces. Attach Form 3903. If claiming only storage fees (see instructions), check here ☐			14	
15	Deductible part of self-employment tax. Attach Schedule SE			15	
16	Self-employed SEP, SIMPLE, and qualified plans			16	
17	Self-employed health insurance deduction			17	
18	Penalty on early withdrawal of savings			18	
19a	Alimony paid Pre-2019 = deductible			19a	
b	Recipient's SSN				
c	Date of original divorce or separation agreement (see instructions):				
20	IRA deduction. If you are married filing separately and lived apart from your spouse for the entire year (see instructions), check here ☐			20	
21	Student loan interest deduction			21	
22	Reserved for future use			22	
23	Archer MSA deduction			23	
24	Other adjustments:				
a	Jury duty pay (see instructions)	24a			
b	Deductible expenses related to income reported on line 8l from the rental of personal property engaged in for profit	24b			
c	Nontaxable amount of the value of Olympic and Paralympic medals and USOC prize money reported on line 8m	24c			
d	Reforestation amortization and expenses	24d			
e	Repayment of supplemental unemployment benefits under the Trade Act of 1974	24e			
f	Contributions to section 501(c)(18)(D) pension plans	24f			
g	Contributions by certain chaplains to section 403(b) plans	24g			
h	Attorney fees and court costs for actions involving certain unlawful discrimination claims (see instructions)	24h			
i	Attorney fees and court costs you paid in connection with an award from the IRS for information you provided that helped the IRS detect tax law violations	24i			
j	Housing deduction from Form 2555	24j			
k	Excess deductions of section 67(e) expenses from Schedule K-1 (Form 1041)	24k			
z	Other adjustments. List type and amount:	24z			
25	Total other adjustments. Add lines 24a through 24z			25	
26	Add lines 11 through 23 and 25. These are your **adjustments to income**. Enter here and on Form 1040, 1040-SR, or 1040-NR, line 10			26	

SCHEDULE 1-A (Form 1040)

Department of the Treasury
Internal Revenue Service

Additional Deductions

Attach to Form 1040, 1040-SR, or 1040-NR.
Go to *www.irs.gov/Form1040* for instructions and the latest information.

OMB No. 1545-0074
2025
Attachment Sequence No. 1A

Name(s) shown on Form 1040, 1040-SR, or 1040-NR | **Your social security number**

Part I Modified Adjusted Gross Income (MAGI) Amount

1	Enter the amount from Form 1040, 1040-SR, or 1040-NR, line 11b			1	
2a	Enter any income from Puerto Rico that you excluded	2a			
b	Enter the amount from Form 2555, line 45	2b			
c	Enter the amount from Form 2555, line 50	2c			
d	Enter the amount from Form 4563, line 15	2d			
e	Add lines 2a, 2b, 2c, and 2d			2e	
3	Add lines 1 and 2e			3	

Part II No Tax on Tips

Caution: Fill out Part II only if you received qualified tips. You and/or your spouse who received qualified tips must have a valid social security number to claim the deduction. If married, you must file jointly to claim this deduction. See instructions.

4	Qualified tips received as an employee.				
a	If Form W-2, box 5, is $176,100 or less, enter qualified tips included in Form W-2, box 7. Otherwise, see instructions	4a			
b	Qualified tips included on Form 4137, line 1(c). If Form 4137 is not filed, enter -0-	4b			
c	If you only received qualified tips from one employer, enter the larger of line 4a or line 4b. Otherwise, see instructions			4c	
5	Qualified tips received in the course of a trade or business. Qualified tip amount included in Form 1099-NEC, box 1; Form 1099-MISC, box 3; or Form 1099-K, box 1a. Do not enter more than the net profit from the trade or business. If you received qualified tips in the course of more than one trade or business, see instructions			5	
6	Add lines 4c and 5			6	
7	Enter the smaller of the amount on line 6 or $25,000			7	
8	Enter the amount from line 3			8	
9	Enter $150,000 ($300,000 if married filing jointly)			9	
10	Subtract line 9 from line 8. If zero or less, enter the amount from line 7 on line 13			10	
11	Divide line 10 by $1,000. If the resulting number isn't a whole number, decrease the result to the next lower whole number. (For example, decrease 1.5 to 1, and decrease 0.05 to 0.)			11	
12	Multiply line 11 by $100			12	
13	**Qualified tips deduction.** Subtract line 12 from line 7. If zero or less, enter -0-			13	

Part III No Tax on Overtime

Caution: Fill out Part III only if you received qualified overtime compensation. You and/or your spouse who received the qualified overtime compensation must have a valid social security number to claim this deduction. If married, you must file jointly to claim this deduction. See instructions.

14a	Qualified overtime compensation included on Form W-2, box 1 (see instructions)	14a			
b	Qualified overtime compensation included on Form 1099-NEC, box 1 or Form 1099-MISC, box 3 (see instructions)	14b			
c	Add lines 14a and 14b			14c	
15	Enter the smaller of the amount on line 14c or $12,500 ($25,000 if married filing jointly)			15	
16	Enter the amount from line 3			16	
17	Enter $150,000 ($300,000 if married filing jointly)			17	
18	Subtract line 17 from line 16. If zero or less, enter the amount from line 15 on line 21			18	
19	Divide line 18 by $1,000. If the resulting number isn't a whole number, decrease the result to the next lower whole number. (For example, decrease 1.5 to 1, and decrease 0.05 to 0.)			19	
20	Multiply line 19 by $100			20	
21	**Qualified overtime compensation deduction.** Subtract line 20 from line 15. If zero or less, enter -0-			21	

Part IV No Tax on Car Loan Interest

Caution: Fill out Part IV only if you paid or accrued qualified passenger vehicle loan interest. See instructions to learn more about what is an applicable passenger vehicle.

22 Applicable passenger vehicle (see instructions). If more than two VINs, see instructions.

	(i) Vehicle identification number (VIN)	Interest for this loan: (ii) Deducted on Schedule C, Schedule E, or Schedule F	(iii) Schedule 1-A
a			
b			

23	Add lines 22a and 22b, column (iii)	23	
24	Enter the smaller of the amount on line 23 or $10,000	24	
25	Enter the amount from line 3	25	
26	Enter $100,000 ($200,000 if married filing jointly)	26	
27	Subtract line 26 from line 25. If zero or less, enter the amount from line 24 on line 30	27	
28	Divide line 27 by $1,000. If the resulting number isn't a whole number, increase the result to the next higher whole number. (For example, increase 1.5 to 2, and increase 0.05 to 1.)	28	
29	Multiply line 28 by $200	29	
30	**Qualified car loan interest deduction.** Subtract line 29 from line 24. If zero or less, enter -0-	30	

Part V Enhanced Deduction for Seniors

Caution: You and/or your spouse must have a valid social security number. If married, you must file jointly to claim this deduction. See instructions.

31	Enter the amount from line 3	31	
32	Enter $75,000 ($150,000 if married filing jointly)	32	
33	Subtract line 32 from line 31. If zero or less, enter $6,000 on line 35	33	
34	Multiply line 33 by 6% (0.06)	34	
35	Subtract line 34 from $6,000. If zero or less, enter -0-	35	
36a	If you have a valid social security number (see instructions) and were born before January 2, 1961, enter the amount from line 35	36a	
b	If you are married filing jointly, your spouse has a valid social security number (see instructions), and your spouse was born before January 2, 1961, enter the amount from line 35	36b	
37	**Enhanced deduction for seniors.** Add lines 36a and 36b	37	

Part VI Total Additional Deductions

38	Add lines 13, 21, 30, and 37. Enter here and on Form 1040 or 1040-SR, line 13b, or on Form 1040-NR, line 13c	38	

SCHEDULE 2 (Form 1040)

Department of the Treasury
Internal Revenue Service

Additional Taxes

Attach to Form 1040, 1040-SR, or 1040-NR.

Go to *www.irs.gov/Form1040* for instructions and the latest information.

OMB No. 1545-0074

2025

Attachment Sequence No. **02**

Name(s) shown on Form 1040, 1040-SR, or 1040-NR | **Your social security number**

Part I Tax

1	Additions to tax:				
a	Excess advance premium tax credit repayment. Attach Form 8962	**1a**			
b	Repayment of new clean vehicle credit(s) transferred to a registered dealer from Schedule A (Form 8936), Part II. Attach Form 8936 and Schedule A (Form 8936)	**1b**			
c	Repayment of previously owned clean vehicle credit(s) transferred to a registered dealer from Schedule A (Form 8936), Part IV. Attach Form 8936 and Schedule A (Form 8936)	**1c**			
d	Recapture of net EPE from Form 4255, line 2a, column (l)	**1d**			
e	Excessive payments (EPs) on gross EPE from Form 4255. Check applicable box and enter amount. See instructions. **(i)** ☐ Line 1a **(ii)** ☐ Line 1c **(iii)** ☐ Line 1d **(iv)** ☐ Line 2a	**1e**			
f	20% EP from Form 4255. Check applicable box and enter amount. See instructions. **(i)** ☐ Line 1a **(ii)** ☐ Line 1c **(iii)** ☐ Line 1d **(iv)** ☐ Line 2a	**1f**			
y	Other additions to tax (see instructions): ____________	**1y**			
z	Add lines 1a through 1y			**1z**	
2	Alternative minimum tax. Attach Form 6251			**2**	
3	Add lines 1z and 2. Enter here and on Form 1040, 1040-SR, or 1040-NR, line 17			**3**	

Part II Other Taxes

4	Self-employment tax. Attach Schedule SE. Check if any exemption from (see instructions): **1** ☐ 4361 **2** ☐ 4029 **3** ☐ ____________			**4**	
5	Social security and Medicare tax on unreported tip income. Attach Form 4137	**5**			
6	Uncollected social security and Medicare tax on wages. Attach Form 8919	**6**			
7	Total additional social security and Medicare tax. Add lines 5 and 6			**7**	
8	Additional tax on IRAs or other tax-favored accounts. Attach Form 5329 if required. If not required, check here ☐			**8**	
9	Household employment taxes. Attach Schedule H			**9**	
10	Reserved for future use			**10**	
11	Additional Medicare Tax. Attach Form 8959			**11**	
12	Net investment income tax. Attach Form 8960			**12**	
13	Uncollected social security and Medicare or RRTA tax on tips or group-term life insurance from Form W-2, box 12			**13**	
14	Interest on tax due on installment income from the sale of certain residential lots and timeshares			**14**	
15	Interest on the deferred tax on gain from certain installment sales with a sales price over $150,000			**15**	
16	Recapture of low-income housing credit. Attach Form 8611			**16**	

(continued on page 2)

Part II **Other Taxes** *(continued)*

17	Other additional taxes:		
a	Recapture of other credits. List type, form number, and amount:	**17a**	
b	Recapture of federal mortgage subsidy. If you sold your home, see instructions	**17b**	
c	Additional tax on HSA distributions. Attach Form 8889	**17c**	
d	Additional tax on an HSA because you didn't remain an eligible individual. Attach Form 8889	**17d**	
e	Additional tax on Archer MSA distributions. Attach Form 8853	**17e**	
f	Additional tax on Medicare Advantage MSA distributions. Attach Form 8853	**17f**	
g	Recapture of a charitable contribution deduction related to a fractional interest in tangible personal property	**17g**	
h	Income you received from a nonqualified deferred compensation plan that fails to meet the requirements of section 409A	**17h**	
i	Compensation you received from a nonqualified deferred compensation plan described in section 457A	**17i**	
j	Section 72(m)(5) excess benefits tax	**17j**	
k	Golden parachute payments	**17k**	
l	Tax on accumulation distribution of trusts	**17l**	
m	Excise tax on insider stock compensation from an expatriated corporation .	**17m**	
n	Look-back interest under section 167(g) or 460(b) from Form 8697 or 8866 .	**17n**	
o	Tax on non-effectively connected income for any part of the year you were a nonresident alien from Form 1040-NR	**17o**	
p	Any interest from Form 8621, line 16f, relating to distributions from, and dispositions of, stock of a section 1291 fund	**17p**	
q	Any interest from Form 8621, line 24	**17q**	
z	Any other taxes. List type and amount:	**17z**	
18	Total additional taxes. Add lines 17a through 17z	**18**	
19	Recapture of net EPE from Form 4255, line 1d, column (l)	**19**	
20	Section 965 net tax liability installment from Form 965-A	**20**	
21	Add lines 4, 7 through 16, 18, and 19. These are your **total other taxes**. Enter here and on Form 1040 or 1040-SR, line 23; or Form 1040-NR, line 23b	**21**	

SCHEDULE 3 (Form 1040)

Department of the Treasury
Internal Revenue Service

Additional Credits and Payments

Attach to Form 1040, 1040-SR, or 1040-NR.
Go to *www.irs.gov/Form1040* for instructions and the latest information.

OMB No. 1545-0074
2025
Attachment Sequence No. 03

Name(s) shown on Form 1040, 1040-SR, or 1040-NR	**Your social security number**

Part I Nonrefundable Credits

1	Foreign tax credit. Attach Form 1116 if required			1	
2	Credit for child and dependent care expenses from Form 2441, line 11. Attach Form 2441			2	
3	Education credits from Form 8863, line 19			3	
4	Retirement savings contributions credit. Attach Form 8880			4	
5a	Residential clean energy credit from Form 5695, line 15			5a	
b	Energy efficient home improvement credit from Form 5695, line 32			5b	
6	Other nonrefundable credits:				
a	General business credit. Attach Form 3800	6a			
b	Credit for prior year minimum tax. Attach Form 8801	6b			
c	Adoption credit. Attach Form 8839	6c			
d	Credit for the elderly or disabled. Attach Schedule R	6d			
e	Reserved for future use	6e			
f	Clean vehicle credit. Attach Form 8936	6f			
g	Mortgage interest credit. Attach Form 8396	6g			
h	District of Columbia first-time homebuyer credit. Attach Form 8859	6h			
i	Qualified electric vehicle credit. Attach Form 8834	6i			
j	Alternative fuel vehicle refueling property credit. Attach Form 8911	6j			
k	Credit to holders of tax credit bonds. Attach Form 8912	6k			
l	Amount on Form 8978, line 14. See instructions	6l			
m	Credit for previously owned clean vehicles. Attach Form 8936	6m			
z	Other nonrefundable credits. List type and amount:	6z			
7	Total other nonrefundable credits. Add lines 6a through 6z			7	
8	Add lines 1 through 4, 5a, 5b, and 7. Enter here and on Form 1040, 1040-SR, or 1040-NR, line 20			8	

Part II Other Payments and Refundable Credits

9	Net premium tax credit. Attach Form 8962			9	
10	Amount paid with request for extension to file (see instructions)			10	
11	Excess social security and tier 1 RRTA tax withheld			11	
12	Credit for federal tax on fuels. Attach Form 4136			12	
13	Other payments or refundable credits:				
a	Form 2439	13a			
b	Section 1341 credit for repayment of amounts included in income from earlier years	13b			
c	Net elective payment election amount from Form 3800, Part III, line 6, column (j)	13c			
d	Deferred amount of net 965 tax liability (see instructions)	13d			
z	Other refundable credits (see instructions):	13z			
14	Total other payments or refundable credits. Add lines 13a through 13z			14	
15	Add lines 9 through 12 and 14. Enter here and on Form 1040, 1040-SR, or 1040-NR, line 31			15	

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 71480G **Schedule 3 (Form 1040) 2025**

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Form **1120-S**

Department of the Treasury
Internal Revenue Service

U.S. Income Tax Return for an S Corporation

Do not file this form unless the corporation has filed or is attaching Form 2553 to elect to be an S corporation.
Go to *www.irs.gov/Form1120S* for instructions and the latest information.

OMB No. 1545-0123

2025

For calendar year 2025 or tax year beginning , 2025, ending , 20

A S election effective date	Name				**D Employer identification number**
B Business activity code number (see instructions)	Number and street. If a P.O. box, see instructions.			Room or suite no.	**E** Date incorporated
C Check if Sch. M-3 attached ☐	City or town	State or province	Country	ZIP or foreign postal code	**F** Total assets (see instructions) $

G Is the corporation electing to be an S corporation beginning with this tax year? See instructions. ☐ Yes ☐ No

H Check if: **(1)** ☐ Final return **(2)** ☐ Name change **(3)** ☐ Address change **(4)** ☐ Amended return **(5)** ☐ S election termination

I Enter the number of shareholders who were shareholders during any part of the tax year . . . .

J Check if corporation: **(1)** ☐ Aggregated activities for section 465 at-risk purposes **(2)** ☐ Grouped activities for section 469 passive activity purposes

Caution: Include **only** trade or business income and expenses on lines 1a through 22. See the instructions for more information.

Income	1a	Gross receipts or sales ______ **b** Less returns and allowances ______ **c** Balance	1c	
	2	Cost of goods sold (attach Form 1125-A)	2	
	3	Gross profit. Subtract line 2 from line 1c	3	
	4	Net gain (loss) from Form 4797, Part II, line 17 (attach Form 4797)	4	
	5	Other income (loss) (see instructions—attach statement)	5	
	6	**Total income (loss).** Add lines 3 through 5	6	
Deductions (see instructions for limitations)	7	Compensation of officers (see instructions—attach Form 1125-E)	7	
	8	Salaries and wages (less employment credits)	8	
	9	Repairs and maintenance	9	
	10	Bad debts	10	
	11	Rents	11	
	12	Taxes and licenses	12	
	13	Interest (see instructions)	13	
	14	Depreciation from Form 4562 not claimed on Form 1125-A or elsewhere on return (attach Form 4562)	14	
	15	Depletion **(do not deduct oil and gas depletion)**	15	
	16	Advertising	16	
	17	Pension, profit-sharing, etc., plans	17	
	18	Employee benefit programs	18	
	19	Energy efficient commercial buildings deduction (attach Form 7205)	19	
	20	Other deductions (attach statement)	20	
	21	**Total deductions.** Add lines 7 through 20	21	
	22	**Ordinary business income (loss).** Subtract line 21 from line 6	22	
Tax and Payments	23a	Excess net passive income or LIFO recapture tax (see instructions) — 23a		
	b	Tax from Schedule D (Form 1120-S) — 23b		
	c	Add lines 23a and 23b (see instructions for additional taxes)	23c	
	24a	Current year's estimated tax payments and preceding year's overpayment credited to the current year — 24a		
	b	Tax deposited with Form 7004 — 24b		
	c	Credit for federal tax paid on fuels (attach Form 4136) — 24c		
	d	Elective payment election amount from Form 3800 — 24d		
	z	Add lines 24a through 24d	24z	
	25	Estimated tax penalty (see instructions). Check if Form 2220 is attached ☐	25	
	26	**Amount owed.** If line 24z is smaller than the total of lines 23c and 25, enter amount owed	26	
	27	**Overpayment.** If line 24z is larger than the total of lines 23c and 25, enter amount overpaid	27	
	28	Enter amount from line 27: **a Credited to 2026 estimated tax** **b Refunded**	28b	
		c Routing number **d** Type: ☐ Checking ☐ Savings		
		e Account number		

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Signature of officer | Date | Title

May the IRS discuss this return with the preparer shown below? See instructions. ☐ **Yes** ☐ **No**

Paid Preparer Use Only

Preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name			Firm's EIN	
Firm's address			Phone no.	

Schedule B Other Information (see instructions)

		Yes	No
1	Check accounting method: a ☐ Cash b ☐ Accrual c ☐ Other (specify)		
2	See the instructions and enter the: a Business activity b Product or service		
3	At any time during the tax year, was any shareholder of the corporation a disregarded entity, a trust, an estate, or a nominee or similar person? If "Yes," attach Schedule B-1, Information on Certain Shareholders of an S Corporation		
4	At the end of the tax year, did the corporation:		
a	Own directly 20% or more, or own, directly or indirectly, 50% or more of the total stock issued and outstanding of any foreign or domestic corporation? For rules of constructive ownership, see instructions. If "Yes," complete (i) through (v) below		

(i) Name of Corporation	**(ii)** Employer Identification Number (if any)	**(iii)** Country of Incorporation	**(iv)** Percentage of Stock Owned	**(v)** If Percentage in (iv) Is 100%, Enter the Date (if applicable) a Qualified Subchapter S Subsidiary Election Was Made

		Yes	No
b	Own directly an interest of 20% or more, or own, directly or indirectly, an interest of 50% or more in the profit, loss, or capital in any foreign or domestic partnership (including an entity treated as a partnership) or in the beneficial interest of a trust? For rules of constructive ownership, see instructions. If "Yes," complete (i) through (v) below		

(i) Name of Entity	**(ii)** Employer Identification Number (if any)	**(iii)** Type of Entity	**(iv)** Country of Organization	**(v)** Maximum Percentage Owned in Profit, Loss, or Capital

		Yes	No
5a	At the end of the tax year, did the corporation have any outstanding shares of restricted stock?		
	If "Yes," complete lines (i) and (ii) below.		
	(i) Total shares of restricted stock		
	(ii) Total shares of non-restricted stock		
b	At the end of the tax year, did the corporation have any outstanding stock options, warrants, or similar instruments?		
	If "Yes," complete lines (i) and (ii) below.		
	(i) Total shares of stock outstanding at the end of the tax year		
	(ii) Total shares of stock outstanding if all instruments were executed		
6	Has this corporation filed, or is it required to file, **Form 8918**, Material Advisor Disclosure Statement, to provide information on any reportable transaction?		
7	Check this box if the corporation issued publicly offered debt instruments with original issue discount ☐ If checked, the corporation may have to file **Form 8281**, Information Return for Publicly Offered Original Issue Discount Instruments.		
8	If the corporation (**a**) was a C corporation before it elected to be an S corporation **or** the corporation acquired an asset with a basis determined by reference to the basis of the asset (or the basis of any other property) in the hands of a C corporation, **and** (**b**) has net unrealized built-in gain in excess of the net recognized built-in gain from prior years, enter the net unrealized built-in gain reduced by net recognized built-in gain from prior years. See instructions $		
9	Did the corporation have an election under section 163(j) for any real property trade or business or any farming business in effect during the tax year? See instructions		
10	Does the corporation satisfy one or more of the following? See instructions		
a	The corporation owns a pass-through entity with current, or prior year carryover, excess business interest expense.		
b	The corporation's aggregate average annual gross receipts (determined under section 448(c)) for the 3 tax years preceding the current tax year are more than $31 million and the corporation has business interest expense.		
c	The corporation is a tax shelter and the corporation has business interest expense. If "Yes," complete and attach **Form 8990**, Limitation on Business Interest Expense Under Section 163(j).		
11	Does the corporation satisfy **both** of the following conditions?		
a	The corporation's total receipts (see instructions) for the tax year were less than $250,000.		
b	The corporation's total assets at the end of the tax year were less than $250,000. If "Yes," the corporation is not required to complete Schedules L and M-1.		

Schedule B Other Information (see instructions) *(continued)*

		Yes	No
12	During the tax year, did the corporation have any non-shareholder debt that was canceled, was forgiven, or had the terms modified so as to reduce the principal amount of the debt?		
	If "Yes," enter the amount of principal reduction . . . $		
13	During the tax year, was a qualified subchapter S subsidiary election terminated or revoked? If "Yes," see instructions		
14a	Did the corporation make any payments that would require it to file Form(s) 1099?		
b	If "Yes," did or will the corporation file required Form(s) 1099?		
15	Does the corporation intend to self-certify as a Qualified Opportunity Fund?		
	If "Yes," complete and attach Form 8996. Enter the amount (if any) from Form 8996, line 15 . . $		
16	At any time during the tax year, did the corporation: (a) receive (as a reward, award, or payment for property or services); or (b) sell, exchange, or otherwise dispose of a digital asset (or a financial interest in a digital asset)? See instructions		
17	Reserved for future use		

Schedule K Shareholders' Pro Rata Share Items

						Total amount
Income (Loss)	1	Ordinary business income (loss) (page 1, line 22)			1	
	2	Net rental real estate income (loss) (attach Form 8825)			2	
	3a	Other gross rental income (loss)	3a			
	b	Expenses from other rental activities (attach statement)	3b			
	c	Other net rental income (loss). Subtract line 3b from line 3a			3c	
	4	Interest income			4	
	5	Dividends: **a** Ordinary dividends			5a	
		b Qualified dividends	5b			
	6	Royalties			6	
	7	Net short-term capital gain (loss) (attach Schedule D (Form 1120-S))			7	
	8a	Net long-term capital gain (loss) (attach Schedule D (Form 1120-S))			8a	
	b	Collectibles (28%) gain (loss)	8b			
	c	Unrecaptured section 1250 gain (attach statement)	8c			
	9	Net section 1231 gain (loss) (attach Form 4797)			9	
	10	Other income (loss) (see instructions) . . . . Type:			10	
Deductions	11	Section 179 deduction (attach Form 4562)			11	
	12a	Cash charitable contributions			12a	
	b	Noncash charitable contributions			12b	
	c	Investment interest expense			12c	
	d	Section 59(e)(2) expenditures . . . . . . Type:			12d	
	e	Other deductions (see instructions) . . . . Type:			12e	
Credits	13a	Low-income housing credit (section 42(j)(5))			13a	
	b	Low-income housing credit (other)			13b	
	c	Qualified rehabilitation expenditures (rental real estate) (attach Form 3468, if applicable)			13c	
	d	Other rental real estate credits (see instructions) Type:			13d	
	e	Other rental credits (see instructions) . . . . Type:			13e	
	f	Biofuel producer credit (attach Form 6478)			13f	
	g	Other credits (see instructions) . . . . . . Type:			13g	
International	14a	Attach Schedule K-2 (Form 1120-S), Shareholders' Pro Rata Share Items—International, and check this box to indicate you are reporting items of international tax relevance ☐				
	b	Check this box if you qualified for an exception to filing Schedule K-2 (Form 1120-S) ☐				
Alternative Minimum Tax (AMT) Items	15a	Post-1986 depreciation adjustment			15a	
	b	Adjusted gain or loss			15b	
	c	Depletion (other than oil and gas)			15c	
	d	Oil, gas, and geothermal properties—gross income			15d	
	e	Oil, gas, and geothermal properties—deductions			15e	
	f	Other AMT items (attach statement)			15f	
Items Affecting Shareholder Basis	16a	Tax-exempt interest income			16a	
	b	Other tax-exempt income			16b	
	c	Nondeductible expenses			16c	
	d	Distributions (attach statement if required) (see instructions)			16d	
	e	Repayment of loans from shareholders			16e	
	f	Foreign taxes paid or accrued			16f	

Schedule K **Shareholders' Pro Rata Share Items** *(continued)*

				Total amount
Other Information	17a	Investment income	17a	
	b	Investment expenses	17b	
	c	Dividend distributions paid from accumulated earnings and profits	17c	
	d	Other items and amounts (attach statement)		
Recon-ciliation	18	**Income (loss) reconciliation.** Combine the total amounts on lines 1 through 10. From the result, subtract the sum of the amounts on lines 11 through 12e and 16f	18	

Schedule L **Balance Sheets per Books**

	Assets	Beginning of tax year (a)	(b)	End of tax year (c)	(d)
1	Cash				
2a	Trade notes and accounts receivable				
b	Less allowance for bad debts	( )		( )	
3	Inventories				
4	U.S. government obligations				
5	Tax-exempt securities (see instructions)				
6	Other current assets (attach statement)				
7	Loans to shareholders				
8	Mortgage and real estate loans				
9	Other investments (attach statement)				
10a	Buildings and other depreciable assets				
b	Less accumulated depreciation	( )		( )	
11a	Depletable assets				
b	Less accumulated depletion	( )		( )	
12	Land (net of any amortization)				
13a	Intangible assets (amortizable only)				
b	Less accumulated amortization	( )		( )	
14	Other assets (attach statement)				
15	Total assets				
	Liabilities and Shareholders' Equity				
16	Accounts payable				
17	Mortgages, notes, bonds payable in less than 1 year				
18	Other current liabilities (attach statement)				
19	Loans from shareholders				
20	Mortgages, notes, bonds payable in 1 year or more				
21	Other liabilities (attach statement)				
22	Capital stock				
23	Additional paid-in capital				
24	Retained earnings				
25	Adjustments to shareholders' equity (attach statement)				
26	Less cost of treasury stock		( )		( )
27	Total liabilities and shareholders' equity				

Schedule M-1 Reconciliation of Income (Loss) per Books With Income (Loss) per Return

Note: The corporation may be required to file Schedule M-3. See instructions.

1	Net income (loss) per books		5	Income recorded on books this year not included on Schedule K, lines 1 through 10 (itemize):	
2	Income included on Schedule K, lines 1, 2, 3c, 4, 5a, 6, 7, 8a, 9, and 10, not recorded on books this year (itemize):		a	Tax-exempt interest $	
3	Expenses recorded on books this year not included on Schedule K, lines 1 through 12e, and 16f (itemize):		6	Deductions included on Schedule K, lines 1 through 12e, and 16f, not charged against book income this year (itemize):	
a	Depreciation $		a	Depreciation $	
b	Travel and entertainment $		7	Add lines 5 and 6	
4	Add lines 1 through 3		8	Income (loss) (Schedule K, line 18). Subtract line 7 from line 4	

Schedule M-2 Analysis of Accumulated Adjustments Account, Shareholders' Undistributed Taxable Income Previously Taxed, Accumulated Earnings and Profits, and Other Adjustments Account

(see instructions)

		(a) Accumulated adjustments account	**(b)** Shareholders' undistributed taxable income previously taxed	**(c)** Accumulated earnings and profits	**(d)** Other adjustments account
1	Balance at beginning of tax year				
2	Ordinary income from page 1, line 22				
3	Other additions				
4	Loss from page 1, line 22	( )			
5	Other reductions	( )			( )
6	Combine lines 1 through 5				
7	Distributions				
8	Balance at end of tax year. Subtract line 7 from line 6				

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☐ Final K-1 ☐ Amended K-1 OMB No. 1545-0123

Schedule K-1 (Form 1120-S) **2025**

Department of the Treasury
Internal Revenue Service

For calendar year 2025, or tax year

beginning ___ / ___ / 2025 ending ___ / ___ / ___

Shareholder's Share of Income, Deductions, Credits, etc.

See separate instructions.

Part I Information About the Corporation

A Corporation's employer identification number

B Corporation's name, address, city, state, and ZIP code

C IRS Center where corporation filed return

D Corporation's total number of shares
Beginning of tax year . . . . . . ______
End of tax year . . . . ______

Part II Information About the Shareholder

E Shareholder's identifying number

F1 Shareholder's name, address, city, state, and ZIP code

F2 If the shareholder is a disregarded entity, a trust, an estate, or a nominee or similar person, enter the individual or entity responsible for reporting:
TIN ______ Name ______

F3 What type of entity is this shareholder? ______

G Current year allocation percentage . . . ______ %

H Shareholder's number of shares
Beginning of tax year . . . . . . ______
End of tax year . . . . ______

I Loans from shareholder
Beginning of tax year . . . . . . $ ______
End of tax year . . . . $ ______

For IRS Use Only

Part III Shareholder's Share of Current Year Income, Deductions, Credits, and Other Items

1	Ordinary business income (loss)	**13**	Credits
2	Net rental real estate income (loss)		
3	Other net rental income (loss)		
4	Interest income		
5a	Ordinary dividends		
5b	Qualified dividends	**14**	Schedule K-3 is attached if checked . . . . . ☐
6	Royalties	**15**	Alternative minimum tax (AMT) items
7	Net short-term capital gain (loss)		
8a	Net long-term capital gain (loss)		
8b	Collectibles (28%) gain (loss)		
8c	Unrecaptured section 1250 gain		
9	Net section 1231 gain (loss)	**16**	Items affecting shareholder basis
10	Other income (loss)		
		17	Other information
11	Section 179 deduction		
12	Other deductions		

18 ☐ More than one activity for at-risk purposes*
19 ☐ More than one activity for passive activity purposes*

* See attached statement for additional information.

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List of Codes

This list identifies the codes used on Schedule K-1 for all shareholders. For detailed reporting and filing information, see the specific line instructions, earlier, and the instructions for your income tax return.

Box 10. Other income (loss)

Code	
A	Other portfolio income (loss)
B	Involuntary conversions
C	Section 1256 contracts and straddles
D	Mining exploration costs recapture
E	Section 951A(a) income inclusions
F	Inclusions of subpart F income
G	Section 951(a)(1)(B) inclusions
H	Reserved for future use
I	Gain (loss) from disposition of oil, gas, geothermal, or other mineral properties
J	Recoveries of tax benefit items
K	Gambling gains and losses
L	Reserved for future use
M	Gain eligible for section 1045 rollover (replacement stock purchased by the corporation)
N	Gain eligible for section 1045 rollover (replacement stock not purchased by the corporation)
O	Sale or exchange of QSB stock with section 1202 exclusion
P – R	Reserved for future use
S	Non-portfolio capital gain (loss)
T – X	Reserved for future use
ZZ	Other income (loss)

Box 12. Other deductions

A	Cash contributions (60%)
B	Cash contributions (30%)
C	Noncash contributions (50%)
D	Noncash contributions (30%)
E	Capital gain property to a 50% limit organization (30%)
F	Capital gain property (20%)
G	Contributions (100%)
H	Investment interest expense
I	Deductions—Royalty income
J	Section 59(e)(2) expenditures
K	Reserved for future use
L	Deductions—Portfolio income (other)
M	Preproductive period expenses
N	Reserved for future use
O	Reforestation expense deduction
P – V	Reserved for future use
W	Soil and water conservation
X	Film, television, and theatrical production expenditures
Y	Expenditures for removal of barriers
Z	Itemized deductions
AA	Contributions to a capital construction fund (CCF)
AB	Penalty on early withdrawal of savings
AC	Interest expense allocated to debt financed distributions
AD – AJ	Reserved for future use
ZZ	Other deductions

Box 13. Credits

A	Zero-emission nuclear power production credit
B	Credit for production from advanced nuclear power facilities
C	Low-income housing credit (section 42(j)(5)) from post-2007 buildings
D	Low-income housing credit (other) from post-2007 buildings
E	Qualified rehabilitation expenditures (rental real estate)
F	Other rental real estate credits
G	Other rental credits
H	Undistributed capital gains credit
I	Biofuel producer credit
J	Work opportunity credit
K	Disabled access credit
L	Empowerment zone employment credit
M	Credit for increasing research activities
N	Credit for employer social security and Medicare taxes
O	Backup withholding
P	Unused investment credit from the qualifying advanced coal project credit or qualifying gasification project credit allocated from cooperatives
Q	Unused investment credit from the qualifying advanced energy project credit allocated from cooperatives
R	Unused investment credit from the advanced manufacturing investment credit allocated from cooperatives
S	Unused investment credit from clean electricity credit allocated from cooperatives
T	Unused investment credit from the energy credit allocated from cooperatives
U	Unused investment credit from the rehabilitation credit allocated from cooperatives
V	Advanced manufacturing production credit
W	Clean electricity production credit
X	Clean fuel production credit
Y	Clean hydrogen production credit
Z	Orphan drug credit
AA	Enhanced oil recovery credit
AB	Renewable electricity production credit
AC	Biodiesel, renewable diesel, or sustainable aviation fuels credit
AD	New markets credit
AE	Credit for small employer pension plan startup costs
AF	Credit for small employer auto-enrollment
AG	Credit for military spouse participation
AH	Credit for employer-provided childcare facilities and services
AI	Low sulfur diesel fuel production credit
AJ	Qualified railroad track maintenance credit
AK	Credit for oil and gas production from marginal wells
AL	Distilled spirits credit
AM	Energy efficient home credit
AN	Reserved for future use
AO	Alternative fuel vehicle refueling property credit
AP	Clean renewable energy bond credit
AQ	New clean renewable energy bond credit
AR	Qualified energy conservation bond credit
AS	Qualified zone academy bond credit

AT	Qualified school construction bond credit
AU	Build America bond credit
AV	Credit for employer differential wage payments
AW	Carbon oxide sequestration credit
AX	Carbon oxide sequestration credit recapture
AY	New clean vehicle credit
AZ	Qualified commercial clean vehicle credit
BA	Credit for small employer health insurance premiums
BB	Employer credit for paid family and medical leave
BC	Eligible credits from transferor(s) under section 6418
BD – BG	Reserved for future use
ZZ	Other credits

Box 15. Alternative minimum tax (AMT) items

A	Post-1986 depreciation adjustment
B	Adjusted gain or loss
C	Depletion (other than oil & gas)
D	Oil, gas, & geothermal—Gross income
E	Oil, gas, & geothermal—Deductions
F	Other AMT items

Box 16. Items affecting shareholder basis

A	Tax-exempt interest income
B	Other tax-exempt income
C	Nondeductible expenses
D	Distributions
E	Repayment of loans from shareholders
F	Foreign taxes paid or accrued

Box 17. Other information

A	Investment income
B	Investment expenses
C	Qualified rehabilitation expenditures (other than rental real estate)
D	Basis of energy property
E	Recapture of low-income housing credit (section 42(j)(5))
F	Recapture of low-income housing credit (other)
G	Recapture of investment credit
H	Recapture of other credits
I	Look-back interest—Completed long-term contracts
J	Look-back interest—Income forecast method
K	Dispositions of property with section 179 deductions
L	Recapture of section 179 deduction
M	Section 453(l)(3) information
N	Section 453A(c) information
O	Section 1260(b) information
P	Interest allocable to production expenditures
Q	Capital construction fund (CCF) nonqualified withdrawals
R	Depletion information—Oil and gas
S – T	Reserved for future use
U	Net investment income
V	Section 199A information
W – Z	Reserved for future use
AA	Excess taxable income
AB	Excess business interest income
AC	Gross receipts for section 448(c)
AD – AI	Reserved for future use
AJ	Excess business loss limitation
AK – AM	Reserved for future use
AN	Farming and fishing income
AO	Reserved for future use
AP	Inversion gain
AQ – AR	Reserved for future use
AS	Qualifying advanced coal project property and qualifying gasification project property
AT	Qualifying advanced energy project property
AU	Advanced manufacturing investment property
AV	Clean electricity investment property
AW	Reportable transactions
AX – BD	Reserved for future use
ZZ	Other information

Form **1065**

Department of the Treasury
Internal Revenue Service

U.S. Return of Partnership Income

For calendar year 2025, or tax year beginning ____________, 2025, ending ____________, 20 ___ .

Go to *www.irs.gov/Form1065* for instructions and the latest information.

OMB No. 1545-0123

2025

A Principal business activity	Name of partnership				**D Employer identification number**
B Principal product or service	Number and street			Room or suite no.	**E** Date business started
C Business code number	City or town	State or province	Country	ZIP or foreign postal code	**F** Total assets (see instructions) $

G Check applicable boxes: **(1)** ☐ Initial return **(2)** ☐ Final return **(3)** ☐ Name change **(4)** ☐ Address change **(5)** ☐ Amended return

H Check accounting method: **(1)** ☐ Cash **(2)** ☐ Accrual **(3)** ☐ Other (specify): ____________

I Number of Schedules K-1. Attach one for each person who was a partner at any time during the tax year: ______

J Check if Schedules C and M-3 are attached . . . ☐

K Check if partnership: **(1)** ☐ Aggregated activities for section 465 at-risk purposes **(2)** ☐ Grouped activities for section 469 passive activity purposes

Caution: Include **only** trade or business income and expenses on lines 1a through 23 below. See instructions for more information.

Income	1a	Gross receipts or sales ______ **b** Less returns and allowances ______ **c** Balance	1c	
	2	Cost of goods sold (attach Form 1125-A)	2	
	3	Gross profit. Subtract line 2 from line 1c	3	
	4	Ordinary income (loss) from other partnerships, estates, and trusts (attach statement)	4	
	5	Net farm profit (loss) (attach Schedule F (Form 1040))	5	
	6	Net gain (loss) from Form 4797, Part II, line 17 (attach Form 4797)	6	
	7	Other income (loss) (attach statement)	7	
	8	**Total income (loss).** Combine lines 3 through 7	8	
Deductions (see instructions for limitations)	9	Salaries and wages (other than to partners) (less employment credits)	9	
	10	Guaranteed payments to partners	10	
	11	Repairs and maintenance	11	
	12	Bad debts	12	
	13	Rent	13	
	14	Taxes and licenses	14	
	15	Interest (see instructions)	15	
	16a	Depreciation (if required, attach Form 4562) — 16a		
	b	Less depreciation reported on Form 1125-A and elsewhere on return — 16b	16c	
	17	Depletion **(Do not deduct oil and gas depletion.)**	17	
	18	Retirement plans, etc.	18	
	19	Employee benefit programs	19	
	20	Energy efficient commercial buildings deduction (attach Form 7205)	20	
	21	Other deductions (attach statement)	21	
	22	**Total deductions.** Add the amounts shown in the far right column for lines 9 through 21	22	
	23	**Ordinary business income (loss).** Subtract line 22 from line 8	23	
Tax and Payment	24	Interest due under the look-back method—completed long-term contracts (attach Form 8697)	24	
	25	Interest due under the look-back method—income forecast method (attach Form 8866)	25	
	26	BBA AAR imputed underpayment (see instructions)	26	
	27	Other taxes (see instructions)	27	
	28	**Total balance due.** Add lines 24 through 27	28	
	29	Elective payment election amount from Form 3800	29	
	30	Payment (see instructions)	30	
	31	**Amount owed.** If the sum of line 29 and line 30 is smaller than line 28, enter amount owed	31	
	32a	**Overpayment.** If the sum of line 29 and line 30 is larger than line 28, enter overpayment	32a	
	b	Routing number ______ **c** Type: ☐ Checking ☐ Savings		
	d	Account number ______		

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than partner or limited liability company member) is based on all information of which preparer has any knowledge.

Signature of partner or limited liability company member — Date

May the IRS discuss this return with the preparer shown below? See instructions. ☐ **Yes** ☐ **No**

Paid Preparer Use Only

Enter preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name			Firm's EIN	
Firm's address			Phone no.	

Schedule B **Other Information**

		Yes	No
1	What type of entity is filing this return? Check the applicable box: a ☐ Domestic general partnership b ☐ Domestic limited partnership c ☐ Domestic limited liability company d ☐ Domestic limited liability partnership e ☐ Foreign partnership f ☐ Other:		
2	At the end of the tax year:		
a	Did any foreign or domestic corporation, partnership (including any entity treated as a partnership), trust, or tax-exempt organization, or any foreign government own, directly or indirectly, an interest of 50% or more in the profit, loss, or capital of the partnership? For rules of constructive ownership, see instructions. If "Yes," attach Schedule B-1, Information on Partners Owning 50% or More of the Partnership		
b	Did any individual or estate own, directly or indirectly, an interest of 50% or more in the profit, loss, or capital of the partnership? For rules of constructive ownership, see instructions. If "Yes," attach Schedule B-1		
3	At the end of the tax year, did the partnership:		
a	Own directly 20% or more, or own, directly or indirectly, 50% or more, of the total voting power of all classes of stock entitled to vote of any foreign or domestic corporation? For rules of constructive ownership, see instructions. If "Yes," complete (i) through (iv) below		

(i) Name of corporation	**(ii)** Employer identification number (if any)	**(iii)** Country of incorporation	**(iv)** Percentage owned in voting stock

		Yes	No
b	Own directly an interest of 20% or more, or own, directly or indirectly, an interest of 50% or more, in the profit, loss, or capital in any foreign or domestic partnership (including an entity treated as a partnership) or in the beneficial interest of a trust? For rules of constructive ownership, see instructions. If "Yes," complete (i) through (v) below		

(i) Name of entity	**(ii)** Employer identification number (if any)	**(iii)** Type of entity	**(iv)** Country of organization	**(v)** Maximum percentage owned in profit, loss, or capital

		Yes	No
4	Does the partnership satisfy **all four** of the following conditions?		
a	The partnership's total receipts for the tax year were less than $250,000.		
b	The partnership's total assets at the end of the tax year were less than $1 million.		
c	Schedules K-1 are filed with the return and furnished to the partners on or before the due date (including extensions) for the partnership return.		
d	The partnership is not filing and is not required to file Schedule M-3		
	If "Yes," the partnership is not required to complete Schedules L, M-1, and M-2; item F on page 1 of Form 1065; or item L on Schedule K-1.		
5	Is this partnership a publicly traded partnership, as defined in section 469(k)(2)?		
6	During the tax year, did the partnership have any debt that was canceled, was forgiven, or had the terms modified so as to reduce the principal amount of the debt?		
7	Has this partnership filed, or is it required to file, Form 8918, Material Advisor Disclosure Statement, to provide information on any reportable transaction?		
8	At any time during calendar year 2025, did the partnership have an interest in or a signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account)? See instructions for exceptions and filing requirements for FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR). If "Yes," enter the name of the foreign country		
9	At any time during the tax year, did the partnership receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the partnership may have to file Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts. See instructions		
10a	Is the partnership making, or had it previously made (and not revoked), a section 754 election? If "Yes," enter the effective date of the election See instructions for details regarding a section 754 election.		
b	For this tax year, did the partnership make an optional basis adjustment under section 743(b)? If "Yes," enter the total aggregate net positive amount $ ________ and the total aggregate net negative amount $(________) of such section 743(b) adjustments for all partners made in the tax year. The partnership must also attach a statement showing the computation and allocation of each basis adjustment. See instructions		

Schedule B **Other Information** *(continued)*

		Yes	No
c	For this tax year, did the partnership make an optional basis adjustment under section 734(b)? If "Yes," enter the total aggregate net positive amount $ ____________ and the total aggregate net negative amount $(____________) of such section 734(b) adjustments for all partnership property made in the tax year. The partnership must also attach a statement showing the computation and allocation of each basis adjustment. See instructions . . .		
d	For this tax year, is the partnership required to adjust the basis of partnership property under section 743(b) or 734(b) because of a substantial built-in loss (as defined under section 743(d)) or substantial basis reduction (as defined under section 734(d))? If "Yes," enter the total aggregate amount of such section 743(b) adjustments and/or section 734(b) adjustments for all partners and/or partnership property made in the tax year $ ____________ . The partnership must also attach a statement showing the computation and allocation of the basis adjustment. See instructions . .		
e	Reserved for future use . . .		
11	Check this box if, during the current or prior tax year, the partnership distributed any property received in a like-kind exchange or contributed such property to another entity (other than disregarded entities wholly owned by the partnership throughout the tax year) . . . ☐		
12	At any time during the tax year, did the partnership distribute to any partner a tenancy-in-common or other undivided interest in partnership property? . . .		
13a	If the partnership is required to file Form 8858, Information Return of U.S. Persons With Respect to Foreign Disregarded Entities (FDEs) and Foreign Branches (FBs), enter the number of Forms 8858 attached. See instructions . . . ____________		
b	The owner of a qualified business unit (QBU) as defined in section 989(a) with a functional currency different from its owner (including a foreign disregarded entity, foreign branch, or foreign partnership) is required to file Form 8964, Information Return of U.S. Persons With Respect to Certain Qualified Business Units, and related schedules. Enter the number of Forms 8964 attached to this Form 1065 ____________; to Forms 5471 for controlled foreign corporations owned by the partnership ____________; and to Forms 8865 for controlled foreign partnerships owned by the partnership ____________ .		
14	Does the partnership have any foreign partners? If "Yes," enter the number of Forms 8805, Foreign Partner's Information Statement of Section 1446 Withholding Tax, filed for this partnership . . . ____________		
15	Enter the number of Forms 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships, attached to this return . . . ____________		
16a	Did you make any payments in 2025 that would require you to file Form(s) 1099? See instructions . . .		
b	If "Yes," did you or will you file required Form(s) 1099? . . .		
17	Enter the number of Forms 5471, Information Return of U.S. Persons With Respect to Certain Foreign Corporations, attached to this return . . . ____________		
18	Enter the number of partners that are foreign governments under section 892 . . . ____________		
19	During the partnership's tax year, did the partnership make any payments, or receive any payments allocable to foreign partners, that would require it to file Forms 1042 and 1042-S under chapter 3 (sections 1441 through 1464) or chapter 4 (sections 1471 through 1474)? . . .		
20	Was the partnership a specified domestic entity required to file Form 8938 for the tax year? See the Instructions for Form 8938 . . .		
21	Is the partnership a section 721(c) partnership, as defined in Regulations section 1.721(c)-1(b)(14)? . . .		
22	During the tax year, did the partnership pay or accrue any interest or royalty for which one or more partners are not allowed a deduction under section 267A? See instructions . . .		
	If "Yes," enter the total amount of the disallowed deductions . . . $ ____________		
23	Did the partnership have an election under section 163(j) for any real property trade or business or any farming business in effect during the tax year? See instructions . . .		
24	Does the partnership satisfy one or more of the following? See instructions . . .		
a	The partnership owns a pass-through entity with current, or prior year carryover, excess business interest expense.		
b	The partnership's aggregate average annual gross receipts (determined under section 448(c)) for the 3 tax years preceding the current tax year are more than $31 million and the partnership has business interest expense.		
c	The partnership is a tax shelter (see instructions) and the partnership has business interest expense. If "Yes" to any, complete and attach Form 8990.		
25	Does the partnership intend to self-certify as a qualified opportunity fund? . . .		
	If "Yes," complete and attach Form 8996, Qualified Opportunity Fund, and enter the amount (if any) from Form 8996, line 15 . . . $ ____________		
26	Enter the number of foreign partners subject to section 864(c)(8) as a result of transferring all or a portion of an interest in the partnership or of receiving a distribution from the partnership . . . ____________ Complete Schedule K-3 (Form 1065), Part XIII, for each foreign partner subject to section 864(c)(8) on a transfer or distribution.		
27	At any time during the tax year, were there any transfers between the partnership and its partners subject to the disclosure requirements of Regulations section 1.707-8? . . .		

Schedule B **Other Information** *(continued)*

		Yes	No
28	Since December 22, 2017, did a foreign corporation directly or indirectly acquire substantially all of the properties constituting a trade or business of your partnership, and was the ownership percentage (by vote or value) for purposes of section 7874 greater than 50% (for example, the partners held more than 50% of the stock of the foreign corporation)? If "Yes," list the ownership percentage by vote and by value. See instructions. Percentage: By vote: ________ By value: ________		
29	Is the partnership required to file Form 7208, Excise Tax on Repurchase of Corporate Stock (see instructions):		
a	Under the applicable foreign corporation rules?		
b	Under the covered surrogate foreign corporation rules?		
	If "Yes" to either (a) or (b), complete Form 7208. See the Instructions for Form 7208.		
30	At any time during this tax year, did the partnership (a) receive (as a reward, award, or payment for property or services); or (b) sell, exchange, or otherwise dispose of a digital asset (or financial interest in a digital asset)? See instructions		
31	Reserved for future use		
32	Check this box if an election out of subchapter K under section 761 is being made. See instructions . . . . ☐		
33	Is the partnership electing out of the centralized partnership audit regime under section 6221(b)? See instructions		
	If "Yes," the partnership must complete Schedule B-2 (Form 1065). Enter the total from Schedule B-2, Part III, line 3 . . . . . ________		
	If "No," complete Designation of Partnership Representative below.		

Designation of Partnership Representative (see instructions)

Enter below the information for the partnership representative (PR) for the tax year covered by this return.

First name of PR (or entity name)		Last name of PR			
U.S. address of PR	Street	City	State	ZIP code	U.S. phone number of PR

Name of designated individual (DI) if PR is an entity

First name of DI		Last name of DI			
U.S. address of DI	Street	City	State	ZIP code	U.S. phone number of DI

Schedule K Partners' Distributive Share Items

				Total amount
Income (Loss)	1	Ordinary business income (loss) (page 1, line 23)	1	
	2	Net rental real estate income (loss) (attach Form 8825)	2	
	3a	Other gross rental income (loss) — 3a		
	b	Expenses from other rental activities (attach statement) — 3b		
	c	Other net rental income (loss). Subtract line 3b from line 3a	3c	
	4	Guaranteed payments: a Services 4a — b Capital 4b		
		c Total. Add lines 4a and 4b	4c	
	5	Interest income	5	
	6	Dividends and dividend equivalents: a Ordinary dividends	6a	
		b Qualified dividends 6b — c Dividend equivalents 6c		
	7	Royalties	7	
	8	Net short-term capital gain (loss) (attach Schedule D (Form 1065))	8	
	9a	Net long-term capital gain (loss) (attach Schedule D (Form 1065))	9a	
	b	Collectibles (28%) gain (loss) — 9b		
	c	Unrecaptured section 1250 gain (attach statement) — 9c		
	10	Net section 1231 gain (loss) (attach Form 4797)	10	
	11	Other income (loss) (see instructions) Type:	11	
Deductions	12	Section 179 deduction (attach Form 4562)	12	
	13a	Cash contributions	13a	
	b	Noncash contributions	13b	
	c	Investment interest expense	13c	
	d	Section 59(e)(2) expenditures: (1) Type: (2) Amount:	13d(2)	
	e	Other deductions (see instructions) Type:	13e	
Self-Employment	14a	Net earnings (loss) from self-employment	14a	
	b	Gross farming or fishing income	14b	
	c	Gross nonfarm income	14c	
Credits	15a	Low-income housing credit (section 42(j)(5))	15a	
	b	Low-income housing credit (other)	15b	
	c	Qualified rehabilitation expenditures (rental real estate) (attach Form 3468, if applicable)	15c	
	d	Other rental real estate credits (see instructions) Type:	15d	
	e	Other rental credits (see instructions) Type:	15e	
	f	Other credits (see instructions) Type:	15f	
International	16a	Attach Schedule K-2 (Form 1065), Partners' Distributive Share Items—International, and check this box to indicate that you are reporting items of international tax relevance ☐		
	b	Check this box if you qualified for an exception to filing Schedule K-2 (Form 1065) ☐		
Alternative Minimum Tax (AMT) Items	17a	Post-1986 depreciation adjustment	17a	
	b	Adjusted gain or loss	17b	
	c	Depletion (other than oil and gas)	17c	
	d	Oil, gas, and geothermal properties—gross income	17d	
	e	Oil, gas, and geothermal properties—deductions	17e	
	f	Other AMT items (attach statement)	17f	
Other Information	18a	Tax-exempt interest income	18a	
	b	Other tax-exempt income	18b	
	c	Nondeductible expenses	18c	
	19a	Distributions of cash and marketable securities	19a	
	b	Distributions of other property	19b	
	20a	Investment income	20a	
	b	Investment expenses	20b	
	c	Other items and amounts (attach statement)		
	21	Total foreign taxes paid or accrued	21	

Analysis of Net Income (Loss) per Return

1	Net income (loss). Combine Schedule K, lines 1 through 11. From the result, subtract the sum of Schedule K, lines 12 through 13e, and 21					1	
2	Analysis by partner type:	(i) Corporate	(ii) Individual (active)	(iii) Individual (passive)	(iv) Partnership	(v) Exempt organization	(vi) Nominee/Other
a	General partners						
b	Limited partners						

Schedule L Balance Sheets per Books

		Beginning of tax year		End of tax year	
	Assets	**(a)**	**(b)**	**(c)**	**(d)**
1	Cash				
2a	Trade notes and accounts receivable				
b	Less allowance for bad debts				
3	Inventories				
4	U.S. Government obligations				
5	Tax-exempt securities				
6	Other current assets (attach statement)				
7a	Loans to partners (or persons related to partners)				
b	Mortgage and real estate loans				
8	Other investments (attach statement)				
9a	Buildings and other depreciable assets				
b	Less accumulated depreciation				
10a	Depletable assets				
b	Less accumulated depletion				
11	Land (net of any amortization)				
12a	Intangible assets (amortizable only)				
b	Less accumulated amortization				
13	Other assets (attach statement)				
14	Total assets				
	Liabilities and Capital				
15	Accounts payable				
16	Mortgages, notes, bonds payable in less than 1 year				
17	Other current liabilities (attach statement)				
18	All nonrecourse loans				
19a	Loans from partners (or persons related to partners)				
b	Mortgages, notes, bonds payable in 1 year or more				
20	Other liabilities (attach statement)				
21	Partners' capital accounts				
22	Total liabilities and capital				

Schedule M-1 Reconciliation of Income (Loss) per Books With Analysis of Net Income (Loss) per Return

Note: The partnership may be required to file Schedule M-3. See instructions.

1	Net income (loss) per books		6	Income recorded on books this year not included on Schedule K, lines 1 through 11 (itemize):	
2	Income included on Schedule K, lines 1, 2, 3c, 5, 6a, 7, 8, 9a, 10, and 11, not recorded on books this year (itemize):		a	Tax-exempt interest $	
3	Guaranteed payments (other than health insurance)		7	Deductions included on Schedule K, lines 1 through 13e, and 21, not charged against book income this year (itemize):	
4	Expenses recorded on books this year not included on Schedule K, lines 1 through 13e, and 21 (itemize):		a	Depreciation $	
a	Depreciation $		8	Add lines 6 and 7	
b	Travel and entertainment $		9	Income (loss) (*Analysis of Net Income (Loss) per Return*, line 1). Subtract line 8 from line 5	
5	Add lines 1 through 4				

Schedule M-2 Analysis of Partners' Capital Accounts

1	Balance at beginning of year		6	Distributions: **a** Cash	
2	Capital contributed: **a** Cash			**b** Property	
	b Property		7	Other decreases (itemize):	
3	Net income (loss) (see instructions)				
4	Other increases (itemize):		8	Add lines 6 and 7	
5	Add lines 1 through 4		9	Balance at end of year. Subtract line 8 from line 5	

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☐ Final K-1 ☐ Amended K-1

OMB No. 1545-0123

Schedule K-1 (Form 1065)

Department of the Treasury
Internal Revenue Service

2025

For calendar year 2025, or tax year

beginning / / 2025 ending / /

Partner's Share of Income, Deductions, Credits, etc.

See separate instructions.

Part I Information About the Partnership

A Partnership's employer identification number

B Partnership's name, address, city, state, and ZIP code

C IRS center where partnership filed return:

D ☐ Check if this is a publicly traded partnership (PTP)

Part II Information About the Partner

E Partner's SSN or TIN (Do not use TIN of a disregarded entity. See instructions.)

F Name, address, city, state, and ZIP code for partner entered in E. See instructions.

G ☐ General partner or LLC member-manager ☐ Limited partner or other LLC member

H1 ☐ Domestic partner ☐ Foreign partner

H2 ☐ If the partner is a disregarded entity (DE), enter the partner's:

TIN ______ Name

I1 What type of entity is this partner? ______

I2 If this partner is a retirement plan (IRA/SEP/Keogh/etc.), check here . ☐

J Partner's share of profit, loss, and capital (see instructions):

	Beginning	Ending
Profit	%	%
Loss	%	%
Capital	%	%

Check if decrease is due to:

☐ Sale or ☐ Exchange of partnership interest. See instructions.

K1 Partner's share of liabilities:

	Beginning	Ending
Nonrecourse . .	$	$
Qualified nonrecourse financing . . .	$	$
Recourse . . .	$	$

K2 Check this box if item K1 includes liability amounts from lower-tier partnerships ☐

K3 Check if any of the above liability is subject to guarantees or other payment obligations by the partner. See instructions . . . . . ☐

L **Partner's Capital Account Analysis**

Beginning capital account . . . $

Capital contributed during the year . . $

Current year net income (loss) . . . $

Other increase (decrease) (attach explanation) $

Withdrawals and distributions . . . $ ( )

Ending capital account . . . . $

M Did the partner contribute property with a built-in gain (loss)?

☐ **Yes** ☐ **No** If "Yes," attach statement. See instructions.

N **Partner's Share of Net Unrecognized Section 704(c) Gain or (Loss)**

Beginning . . . . $

Ending . . . . $

Part III Partner's Share of Current Year Income, Deductions, Credits, and Other Items

1	Ordinary business income (loss)	14	Self-employment earnings (loss)
2	Net rental real estate income (loss)		
3	Other net rental income (loss)	15	Credits
4a	Guaranteed payments for services		
4b	Guaranteed payments for capital	16	Schedule K-3 is attached if checked . . . . . ☐
4c	Total guaranteed payments	17	Alternative minimum tax (AMT) items
5	Interest income		
6a	Ordinary dividends		
6b	Qualified dividends	18	Tax-exempt income and nondeductible expenses
6c	Dividend equivalents		
7	Royalties		
8	Net short-term capital gain (loss)	19	Distributions
9a	Net long-term capital gain (loss)		
9b	Collectibles (28%) gain (loss)	20	Other information
9c	Unrecaptured section 1250 gain		
10	Net section 1231 gain (loss)		
11	Other income (loss)		
12	Section 179 deduction	21	Foreign taxes paid or accrued
13	Other deductions		

22 ☐ More than one activity for at-risk purposes*

23 ☐ More than one activity for passive activity purposes*

*See attached statement for additional information.

For IRS Use Only

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List of Codes and References Used in Schedule K-1 (Form 1065)

Box Number / Item		**Where to report or where to find further reporting information. Page numbers refer to these instructions.**
1. Ordinary business income (loss). Determine whether the income (loss) is passive or nonpassive and enter on your return as follows.		
	Passive loss	See page 15
	Passive income	Schedule E (Form 1040), line 28, column (h)
	Nonpassive loss	See page 15
	Nonpassive income	Schedule E (Form 1040), line 28, column (k)
2. Net rental real estate income (loss)		See page 15
3. Other net rental income (loss)		
	Net income	Schedule E (Form 1040), line 28, column (h)
	Net loss	See Instructions for Form 8582
4a. Guaranteed payment services		See Instructions for Schedule E (Form 1040)
4b. Guaranteed payment capital		See Instructions for Schedule E (Form 1040)
4c. Guaranteed payment total		See page 15
5. Interest income		Form 1040 or 1040-SR, line 2b
6a. Ordinary dividends		Form 1040 or 1040-SR, line 3b
6b. Qualified dividends		Form 1040 or 1040-SR, line 3a
6c. Dividend equivalents		See page 16
7. Royalties		Schedule E (Form 1040), line 4
8. Net short-term capital gain (loss)		Schedule D (Form 1040), line 5
9a. Net long-term capital gain (loss)		Schedule D (Form 1040), line 12
9b. Collectibles (28%) gain (loss)		28% Rate Gain Worksheet, line 4 (Schedule D instructions)
9c. Unrecaptured section 1250 gain		See page 16
10. Net section 1231 gain (loss)		See page 17
11. Other income (loss)		
	Code A. Other portfolio income (loss)	See page 17
	Code B. Involuntary conversions	See page 17
	Code C. Section 1256 contracts & straddles	Form 6781, line 1
	Code D. Mining exploration costs recapture	See 2022 Pub. 535
	Code E. Cancellation of debt	See page 17
	Code F. Section 743(b) positive adjustments	See page 17
	Code G. Reserved for future use	
	Code H. Section 951(a) income inclusions	See page 17
	Code I. Gain (loss) from disposition of oil, gas, geothermal, or mineral properties (section 59(e))	See page 17
	Code J. Recoveries of tax benefit items	See page 18
	Code K. Gambling gains and losses	See page 18
	Code L. Any income, gain, or loss to the partnership from a distribution under section 751(b) (certain distributions treated as sales or exchanges)	See page 18
	Code M. Gain eligible for section 1045 rollover (replacement stock purchased by partnership)	See page 18
	Code N. Gain eligible for section 1045 rollover (replacement stock not purchased by the partnership)	See page 18
	Code O. Sale or exchange of QSB stock with section 1202 exclusion	See page 19
	Code P. Gain or loss on disposition of farm recapture property and other items to which section 1252 applies	See page 19
	Code Q. Gain or loss on Fannie Mae or Freddie Mac qualified preferred stock	See page 19
	Code R. Specially allocated ordinary gain (loss)	See page 19
	Code S. Non-portfolio capital gain (loss)	See page 19
	Codes T through X. Reserved for future use	
	Code ZZ. Other	See page 19
12. Section 179 deduction		See page 19
13. Other deductions		
	Code A. Cash contributions (60%)	See page 19
	Code B. Cash contributions (30%)	See page 19
	Code C. Noncash contributions (50%)	See page 19

Box Number / Item		Where to report or where to find further reporting information. Page numbers refer to these instructions.
	Code D. Noncash contributions (30%)	See page 20
	Code E. Capital gain property to a 50% organization (30%)	See page 20
	Code F. Capital gain property (20%)	See page 20
	Code G. Contributions (100%)	See page 20
	Code H. Investment interest expense	Form 4952, line 1
	Code I. Deductions—royalty income	Schedule E (Form 1040), line 19
	Code J. Section 59(e)(2) expenditures	See page 21
	Code K. Excess business interest expense	See page 21
	Code L. Deductions—portfolio income (other)	Schedule A (Form 1040), line 16
	Code M. Amounts paid for medical insurance	Schedule A (Form 1040), line 1; or Schedule 1 (Form 1040), line 17
	Code N. Educational assistance benefits	See page 21
	Code O. Dependent care benefits	Form 2441, line 12
	Code P. Preproductive period expenses	See page 21
	Code Q. Reserved for future use	
	Code R. Pensions and IRAs	See page 21
	Code S. Reforestation expense deduction	See page 21
	Codes T through U. Reserved for future use	
	Code V. Section 743(b) negative adjustments	See page 22
	Code W. Soil and water conservation	See page 22
	Code X. Film, television, and theatrical production expenditures	See page 22
	Code Y. Expenditures for removal of barriers	See page 22
	Code Z. Itemized deductions	See page 22
	Code AA. Contributions to a capital construction fund (CCF)	See page 22
	Code AB. Penalty on early withdrawal of savings	See page 22
	Code AC. Interest expense allocated to debt-financed distributions	See page 22
	Code AD. Interest expense on working interest in oil or gas	See page 22
	Code AE. Deductions—portfolio income	See page 22
	Codes AF through AJ. Reserved for future use	
	Code ZZ. Other	See page 22
14. Self-employment earnings (loss)		
	Note. If you have a section 179 deduction or any partner-level deductions, see page 22 before completing Schedule SE (Form 1040).	
	Code A. Net earnings (loss) from self-employment	Schedule SE (Form 1040)
	Code B. Gross farming or fishing income	See page 22
	Code C. Gross nonfarm income	See page 23
15. Credits		
	Code A. Zero-emission nuclear power production credit	See page 23
	Code B. Credit for production from advanced nuclear power facilities	See page 23
	Code C. Low-income housing credit (section 42(j)(5)) from post-2007 buildings	See page 23
	Code D. Low-income housing credit (other) from post-2007 buildings	See page 23
	Code E. Qualified rehabilitation expenditures (rental real estate)	See page 23
	Code F. Other rental real estate credits	See page 23
	Code G. Other rental credits	See page 23
	Code H. Undistributed capital gains credit	Schedule 3 (Form 1040), line 13a
	Code I. Biofuel producer credit	See page 23
	Code J. Work opportunity credit	See page 23
	Code K. Disabled access credit	See page 23
	Code L. Empowerment zone employment credit	See page 23
	Code M. Credit for increasing research activities	See page 23
	Code N. Credit for employer social security and Medicare taxes	See page 24
	Code O. Backup withholding	See page 24
	Code P. Unused investment credit from the qualifying advanced coal project credit or qualifying gasification project credit allocated from cooperatives	See page 24
	Code Q. Unused investment credit from the qualifying advanced energy project credit allocated from cooperatives	See page 24
	Code R. Unused investment credit from the advanced manufacturing investment credit allocated from cooperatives	See page 24
	Code S. Unused investment credit from the clean electricity investment credit allocated from cooperatives	See page 24

Box Number / Item		Where to report or where to find further reporting information. Page numbers refer to these instructions.
	Code T. Unused investment credit from the energy credit allocated from cooperatives	See page 24
	Code U. Unused investment credit from the rehabilitation credit allocated from cooperatives	See page 24
	Code V. Advanced manufacturing production credit	See page 24
	Code W. Clean electricity production credit	See page 24
	Code X. Clean fuel production credit	See page 24
	Code Y. Clean hydrogen production credit	See page 24
	Code Z. Orphan drug credit	See page 24
	Code AA. Enhanced oil recovery credit	See page 24
	Code AB. Renewable electricity production credit	See page 24
	Code AC. Biodiesel, renewable diesel, or sustainable aviation fuels credit	See page 24
	Code AD. New markets credit	See page 24
	Code AE. Credit for small employer pension plan startup costs	See page 24
	Code AF. Credit for small employer auto-enrollment	See page 24
	Code AG. Credit for small employer military spouse retirement plan eligibility	See page 24
	Code AH. Credit for employer-provided childcare facilities and services	See page 24
	Code AI. Low sulfur diesel fuel production credit	See page 24
	Code AJ. Qualified railroad track maintenance credit	See page 24
	Code AK. Credit for oil and gas production from marginal wells	See page 24
	Code AL. Distilled spirits credit	See page 24
	Code AM. Energy efficient home credit	See page 24
	Code AN. Reserved for future use	
	Code AO. Alternative fuel vehicle refueling property credit	See page 24
	Code AP. Clean renewable energy bond credit	See page 24
	Code AQ. New clean renewable energy bond credit	See page 24
	Code AR. Qualified energy conservation bond credit	See page 24
	Code AS. Qualified zone academy bond credit	See page 24
	Code AT. Qualified school construction bond credit	See page 24
	Code AU. Build America bond credit	See page 24
	Code AV. Credit for employer differential wage payments	See page 24
	Code AW. Carbon oxide sequestration credit	See page 24
	Code AX. Carbon oxide sequestration credit recapture	See page 25
	Code AY. New clean vehicle credit	See page 25
	Code AZ. Qualified commercial clean vehicle credit	See page 25
	Code BA. Credit for small employer health insurance premiums	See page 25
	Code BB. Employer credit for paid family and medical leave	See page 25
	Code BC. Eligible credits from transferor(s) under section 6418	See page 25
	Codes BD through BG. Reserved for future use	
	Code ZZ. Other	See page 25
17. Alternative minimum tax (AMT) items		
	Code A. Post-1986 depreciation adjustment	See Instructions for Form 6251
	Code B. Adjusted gain or loss	See Instructions for Form 6251
	Code C. Depletion (other than oil & gas)	See Instructions for Form 6251
	Code D. Oil, gas, and geothermal—gross income	See Instructions for Form 6251
	Code E. Oil, gas, and geothermal—deductions	See Instructions for Form 6251
	Code F. Other AMT items	See Instructions for Form 6251
18. Tax-exempt income and nondeductible expenses		
	Code A. Tax-exempt interest income	Form 1040 or 1040-SR, line 2a
	Code B. Other tax-exempt income	See page 25
	Code C. Nondeductible expenses	See page 25
19. Distributions		
	Code A. Cash and marketable securities	See page 26
	Code B. Distribution subject to section 737	See page 26
	Code C. Other property	See page 26
20. Other information		
	Code A. Investment income	Form 4952, line 4a

TF - 33

Box Number / Item		Where to report or where to find further reporting information. Page numbers refer to these instructions.
	Code B. Investment expenses	Form 4952, line 5
	Code C. Fuel tax credit information	Form 4136
	Code D. Qualified rehabilitation expenditures (other than rental real estate)	See page 27
	Code E. Basis of energy property	See page 27
	Code F. Recapture of low-income housing credit for section 42(j)(5) partnerships	See page 27
	Code G. Recapture of low-income housing credit for other partnerships	See page 27
	Code H. Recapture of investment credit	See Form 4255
	Code I. Recapture of other credits	See page 27
	Code J. Look-back interest—completed long-term contracts	See Form 8697
	Code K. Look-back interest—income forecast method	See Form 8866
	Code L. Dispositions of property with section 179 deductions	See page 27
	Code M. Recapture of section 179 deduction	See page 28
	Code N. Business interest expense (information item)	See page 28
	Code O. Section 453(l)(3) information	Schedule 2 (Form 1040), line 14
	Code P. Section 453A(c) information	Schedule 2 (Form 1040), line 15
	Code Q. Section 1260(b) information	Schedule 2 (Form 1040), line 17z
	Code R. Interest allocable to production expenditures	See Regulations sections 1.263A-8 through -15
	Code S. Capital construction fund (CCF) nonqualified withdrawals	Schedule 2 (Form 1040), line 17z
	Code T. Depletion deduction	See 2022 Pub. 535
	Code U. Section 743(b) basis adjustment	See page 28
	Code V. Unrelated business taxable income	See page 28
	Code W. Precontribution gain (loss)	Form 8949 and/or Schedule D (Form 1040); or Form 4797
	Code X. Payment obligations including guarantees and deficit obligations (DROs)	See page 29
	Code Y. Net investment income	See Instructions for Form 8960
	Code Z. Section 199A information	Form 8995 or 8995-A
	Code AA. Section 704(c) information	See page 30
	Code AB. Section 751 gain (loss)	See page 30
	Code AC. Section 1(h)(5) collectibles gain	See page 30
	Code AD. Section 1(h)(6) unrecaptured section 1250 gain	See page 30
	Code AE. Excess taxable income	See Instructions for Form 8990
	Code AF. Excess business interest income	See page 30
	Code AG. Gross receipts for section 448(c)	See page 30
	Code AH. Noncash charitable contributions	See page 30
	Code AI. Interest and tax on deferred compensation to partners	See page 30
	Code AJ. Excess business loss limitation	See page 30
	Code AK. Gain from mark-to-market election	See page 31
	Code AL. Section 721(c) partnership	See page 31
	Code AM. Section 1061 information	See page 31
	Code AN. Farming and fishing business	See page 31
	Code AO. PTP information	See page 31
	Code AP. Inversion gain	See page 31
	Code AQ. Conservation reserve program payments	See page 31
	Code AR. IRA disclosure	See page 31
	Code AS. Qualifying advanced coal project property and qualifying gasification project property	See page 31
	Code AT. Qualifying advanced energy project property	See page 31
	Code AU. Advanced manufacturing investment property	See page 31
	Code AV. Reserved for future use	
	Code AW. Reportable transactions	See page 31
	Code AX. Corporate alternative minimum tax (CAMT)	See page 31
	Code AY. Foreign partners, Form 8990, Schedule A	See page 31
	Codes AZ through BD. Reserved for future use	
	Code ZZ. Other	See page 32
21. Foreign taxes paid or accrued		See page 32