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CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS CONSULTANTS
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YEAR-END PLANNING: BUSINESSES

Dear Business Client:

With year-end approaching, it is time to start thinking about moves that may help lower your business' taxes for this year and next.

The standard year-end approach of deferring income and accelerating deductions to minimize taxes will continue to produce the best results for most small businesses, as will the bunching of deductible expenses into this year or next to maximize their tax value.

We have compiled a list of actions based on current tax rules that may help you save tax dollars if you act before year-end. Not all of them will apply to you or your business, but you may benefit from many of them. We can narrow down specific actions when we meet to tailor a particular plan for your business, In the meantime, please review the following list and contact us at your earliest convenience so that we can advise you on which tax-saving moves might be beneficial:

Taxpayers other than corporations may be entitled to a deduction of up to 20% of their qualified business income. For 2025, if taxable income exceeds $394,600 for a married couple filing jointly, (about half that for others), the deduction may be limited based on whether the taxpayer is engaged in a service-type trade or business (such as law, accounting, health, or consulting), the amount of W-2 wages paid by the business, and/or the unadjusted basis of qualified property (such as machinery and equipment) held by the business. The limitations are phased in; for example, the phase-in applies to joint filers with taxable income up to $100,000 above the threshold, and to other filers with taxable income up to $50,000 above their threshold.

Taxpayers may be able to salvage at least some of this deduction, by deferring income or accelerating deductions to keep income under the dollar thresholds (or be subject to a smaller deduction phaseout) for 2025. Depending on their business model, taxpayers also may be able increase the deduction by increasing W-2 wages before year-end. The rules are quite complex, so don't make a move in this area without consulting us.

More small businesses are able to use the cash (as opposed to accrual) method of accounting than were allowed to do so in earlier years. To qualify as a small business a taxpayer must, among other things, satisfy a gross receipts test, which is satisfied for 2025 if, during a three-year testing period, average annual gross receipts don't exceed $31,000,000 (next year this dollar amount is estimated to increase to $32,000,000). Note that many years ago it was $1 million. Cash method taxpayers may find it a lot easier to shift income, for example by holding off billings till next year or by accelerating expenses, for example, paying bills early or by making certain prepayments.

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Businesses should consider making expenditures that qualify for the liberalized business property expensing option. For tax years beginning in 2025, the expensing limit is $2,500,000, and the investment ceiling limit is $4,000,000. Expensing is generally available for most depreciable property (other than buildings) and off-the-shelf computer software. It is also available for interior improvements to a building (but not for its enlargement), elevators or escalators, or the internal structural framework), for roofs, and for HVAC, fire protection, alarm, and security systems.

Generous dollar ceilings mean that many small and medium sized businesses that make timely purchases will be able to currently deduct most if not all their outlays for machinery and equipment. What's more, the expensing deduction is not prorated for the time that the asset is in service during the year. So expensing eligible items acquired and placed in service in the last days of 2025, rather than at the beginning of 2026, can result in a full expensing deduction for 2025.

Businesses also can claim bonus first year depreciation deduction for machinery and equipment bought used (with some exceptions) or new if purchased and placed in service this year, and for qualified improvement property, described above as related to the expensing deduction. The write-off is permitted without any proration based on the length of time that an asset is in service during the tax year. As a result, the bonus first-year write-off is available even if qualifying assets are in service for only a few days in 2025.

Businesses may be able to take advantage of the de minimis safe harbor election (also known as the book-tax conformity election) to expense the costs of lower-cost assets and materials and supplies, assuming the costs aren't required to be capitalized under the UNICAP rules. To qualify for the election, the cost of a unit of property can't exceed $5,000 if the taxpayer has an applicable financial statement (AFS, e.g., a certified audited financial statement along with an independent CPA's report). If there's no AFS, the cost of a unit of property can't exceed $2,500. Where the UNICAP rules aren't an issue, and where potentially increasing tax rates for 2026 aren't a concern, consider purchasing qualifying items before the end of 2025.

A corporation (other than a large corporation) that anticipates a small net operating loss (NOL) for 2025 (and substantial net income in 2026) may find it worthwhile to accelerate just enough of its 2026 income (or to defer just enough of its 2025 deductions) to create a small amount of net income for 2025. This allows the corporation to base its 2026 estimated tax installments on the relatively small amount of income shown on its 2025 return, rather than having to pay estimated taxes based on 100% of its much larger 2026 taxable income.

Year-end bonuses can be timed for maximum tax effect by both cash- and accrual-basis employers. Cash-basis employers deduct bonuses in the year paid, so they can time the payment for maximum tax effect. Accrual-basis employers deduct bonuses in the accrual year when all events related to them are established with reasonable certainty.

- However, the bonus must be paid within 2½ months after the end of the employer's tax year for the deduction to be allowed in the earlier accrual year. Accrual employers looking to defer deductions to a higher-taxed future year should consider changing their bonus plans before year-end to set the payment date later than the 2.5- terms to make the bonus amount not determinable at year end.

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To reduce 2025 taxable income, consider deferring a debt-cancellation event until 2026.

Sometimes the disposition of a passive activity can be timed to make best use of its freed-up suspended losses. Where reduction of 2025 income is desired, consider disposing of a passive activity before year-end to take the suspended losses against 2025 income. If possible 2026 top rate increases are a concern, holding off on disposing of the activity until 2026 might save more in future taxes.

The pass-through state income tax deduction allows business owners to deduct state income tax on their business income without limit. This deduction allows a pass-through entity to elect to pay the state income tax due on the business income that would otherwise pass through and get paid on the owner's personal tax returns.

These are just some of the year-end steps that can be taken to save taxes. Again, by contacting us, we can tailor a particular plan that will work best for you.

Happy Holidays!

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