

2025 Year-end Tax Planning Considerations – Business Clients

As the 2025 year ends and a new year is on the horizon, getting a handle on your 2025 projected income may be the key to helping you save tax dollars. The One Big Beautiful Bill Act (OBBA) has introduced significant changes to tax laws that may be beneficial to you. If you haven't yet scheduled a year-end tax planning discussion with us and would like to, please call the office at **410-643-4477** and ask for **Marie**.

Here are some key annual considerations and notable tax law changes that may impact your business.

State Taxes

Staying compliant with state tax laws is essential, particularly if your business operates across multiple states or employs remote workers. Each state has its own definition of "a physical or economic presence" that may trigger tax obligations. As remote work and interstate sales continue to grow, identifying strategies to reduce your state tax exposure is increasingly essential. Because these rules vary significantly from state to state and can be complex, please don't hesitate to contact us with any questions or concerns.

Pass-through Entity (PTE) Tax

Maryland and several other states have implemented a Pass-through Entity Tax. This allows eligible businesses, such as partnerships and S corporations, to pay state income tax at the entity level. Doing so can reduce the federal taxable income that passes through to owners' personal returns, offering a workaround to the 2017 federal cap on state and local tax deductions.

In Maryland, the PTE tax is deductible for federal purposes in the year the entity makes the payment, not when the tax is assessed or incurred.

Sales Tax

If your business sells products or services online or across state lines, it's essential to understand and comply with **sales tax** requirements. Please note that we do not monitor your sales volume or transaction counts by state, nor do we register or file sales tax returns as part of your income tax preparation. We can recommend software solutions or connect you with a sales tax service provider. You must act on this matter independently to ensure compliance.

Fixed Assets and Depreciation

Fixed assets (such as computers, machinery, vehicles, furniture, and buildings) can be handled differently for tax purposes. This gives you flexibility in how and when you deduct their cost. Depending on your strategy, you can choose to expense these items more quickly to reduce your current tax bill or spread the deductions over time to manage future tax liabilities. The approach you take can directly impact your overall tax planning.

First-year bonus depreciation for qualified property (machinery, equipment, computers, etc.) placed into service after January 19, 2025, was scheduled to drop to 40% in 2025. The OBBA permanently restored this write-off to 100% for 2025 and beyond.

Section 179 expenditure increased from \$1 million to \$2.5 million, with the phaseout threshold raised to \$4 million.

The **Qualified Business Income Deduction (QBID)** has been made permanent and continues to be a great way to reduce your taxable business income. If you have taxable income from your sole proprietorship, partnership, or S Corporation, you may be eligible for up to a 20% deduction on your personal returns. Passive income from businesses, such as interest, dividends, and most rentals, does not qualify.

De minimis Safe Harbor for Business Purchases is an excellent tax break that allows small businesses to immediately deduct the cost of certain low-cost purchases, like furniture, equipment, tools, or office supplies, in the year they're bought and used, rather than spreading the deduction out over several years through depreciation. This rule is designed to simplify recordkeeping by allowing immediate expensing of minor purchases that would otherwise require complex tracking and depreciation schedules. You can deduct items that cost **up to \$2,500 per item or invoice**.

Benefits and Considerations for Business Owners

Health Insurance (Medical, Dental, and Vision)

S Corporation 2% or more Shareholder - Premiums paid by the business are deductible, but must be included as Federal and State taxable wages on shareholders' W-2. Although subject to Federal and State taxes for payroll reporting, it typically does not increase personal taxable income. Instead, it is reported as income with gross wages, then deducted "above-the-line" on the federal income tax return.

To qualify:

- The S Corporation may pay the health insurance premiums directly to the insurance provider for the benefit of the 2-percent shareholder-employee (and their spouse, dependents, or qualifying children).
- The 2 percent shareholder-employee may pay the premiums personally. Still, for the payment to be considered as established under the S corporation, the S corporation must reimburse the shareholder for those premiums within the same taxable year.
- **Premiums must be reported on the shareholder's W-2 to qualify for the deduction. Reporting them only on the K-1 is not acceptable and will result in the deduction being disallowed by the IRS.**

Partnerships and LLCs Taxed as Partnerships - Partnerships may deduct health insurance premiums paid for partners or LLC members as a business expense. These payments are reported as guaranteed payments on the partner's or member's K-1. The owner then reports the guaranteed payment as income on their personal return and may claim an "above-the-line" deduction for the allowable amount.

To qualify:

- The insurance plan must be established under the partnership or reimbursed directly to the owner if they hold the policy.
- The deduction is limited to the owner's net self-employment earnings from the business.

Sole Proprietors and Single-Member LLCs (Schedule C or F Filers) – Similar to business entities, sole proprietors and Single-Member LLCs, filing Schedule C or Schedule F with their personal returns may qualify for the self-employed health insurance deduction.

To qualify:

- The combined net profit from Schedule C or F businesses must be positive, and the deduction cannot exceed that amount.
- The health insurance plan can be in the name of the business or the individual.
- Medicare premiums paid by the owner or their spouse also qualify for this deduction.

Retirement Plans

Business retirement plans offer significant benefits for the business, its owners, and its employees, and can help attract talent. There are many choices, including SEP IRA, SIMPLE IRA, 401K, ROTH 401K, and others.

Some benefits:

- Employer contributions are generally tax-deductible, reducing the business's taxable income.
- Employee contributions (except Roth contributions) are not taxed until distributed, allowing for tax-deferred growth.
- Plan assets grow tax-free until distribution.
- Distributions may be eligible for tax-favored rollovers into other retirement programs.
- Attracting and Retaining Employees.
- Employers can choose plans that fit their business size, structure, and goals, with options for employer-only or employee-and-employer contributions.

Beginning in September 2022, the new **Maryland Saves Program** (<https://marylandsaves.com>) requires most businesses to offer a retirement plan. This program is a low-cost, simple solution for retirement plan savings with no employer fees or requirements.

Reasonable Compensation

Owners of C Corporations and S Corporations should carefully consider the wages and compensation they receive from their businesses to ensure they qualify as "reasonable compensation" under IRS guidelines. The IRS evaluates reasonable compensation based on factors such as the owner's qualifications, responsibilities, the nature of the work performed, and the size and profitability of the business.

Employee and Fringe Benefits

Tax-Free Student Loan Repayment Benefit

Employers may pay up to \$5,250 per employee per year toward the employee's qualified education loans, and this amount is excluded from the employee's gross income for federal tax purposes. This exclusion applies to payments made directly to the lender or to the employee, provided the payments are for the employee's own qualified education loans.

2025 Dependent Care Assistance

For 2025, businesses can provide employees with up to **\$5,000** in tax-free dependent care assistance (**\$2,500** if married filing separately). This benefit helps cover the cost of care for dependents while the employee (and their spouse, if applicable) works or looks for work. Child must be under the age of 13, the employee's dependent, a spouse who is unable to care for themselves, or another dependent who meets the same criteria.

Starting in 2026, the cap increases to **\$7,500** (\$3,750 for married filing separately) under new legislation.

Business Meals and Entertainment

Businesses can generally deduct **50%** of the cost of meals that are directly related to business activities. This includes meals with clients, customers, or employees, as long as there's a clear business purpose—like discussing work, closing a deal, or holding a meeting. The meal can take place at a restaurant, during travel, or even in the office.

To qualify, the expense must be ordinary and necessary for the business, and you need to keep good records—like receipts, who attended, and the business reason for the meal. Some exceptions allow for **100% deductions**, such as meals provided to employees for company events or meals included in taxable employee compensation.

Entertainment expenses are generally not deductible for tax purposes. The IRS disallows deductions for most costs related to entertaining clients, customers, or employees—such as tickets to sporting events, concerts, golf outings, or meals where the primary purpose is entertainment.

Odds and Ends

2025 IRS 1099 Filing

The IRS is cracking down on businesses that fail to issue required 1099 forms. For 2025, the penalties for missing or incorrectly filing a 1099 have increased significantly. Depending on when the form is filed, penalties range from \$60 to \$330 per form. If the IRS determines there was intentional disregard, the penalty jumps to \$660 per form, with no maximum.

If you pay **\$600 or more** in a calendar year to a **non-corporate vendor, subcontractor, or independent contractor** for **services** (not goods), you must issue **Form 1099-NEC**. You're required to report payments made in cash or by check, but not those made by credit/debit card or via **third-party platforms** like PayPal or Venmo. To simplify tax reporting, it's wise to request a **completed IRS Form W-9** from the payee **before they begin work**.

You can download a copy of Form W-9 here: <https://www.irs.gov/pub/irs-pdf/fw9.pdf>.

Available Tax Credits

There is a range of tax credits and incentives designed to promote business investment and job creation. These benefits are available across various industries, including technology and innovation, renewable energy, and economically distressed or low-income communities. For example, businesses that incur qualified research and development (R&D) expenses may be eligible for the **federal R&D tax credit**. Additionally, many states and local governments offer their own tax incentives.

BIG NEWS FOR 1099 REPORTING - For tax year 2026, the OBBBA has increased the 1099 reporting threshold from \$600 to \$2,000 reporting threshold. Fewer forms to file!

CREDIT MADE PERMANENT - Enhanced Paid Family and Medical Leave Credit - The paid family and medical leave credit is made permanent and expanded to include insurance premiums and clarified for aggregation and state/local paid leave.

STARTING TAX YEAR 2026 – Business, Travel, and Employer-provided meals:

- Employer-provided meals for their employees at their office/business location for the employer's convenience during the regular workday are not deductible for tax purposes - 0% deductible. This includes de minimis fringe benefits like coffee, snacks, etc.

- This does not include employee-focused events such as holiday parties, team-building events, overtime, and training, which are still 100% deductible.

Navigating the ever-changing landscape of tax laws can feel overwhelming, but you don't have to do it alone. If you have any questions or need guidance, feel free to reach out to us. We are here to help!

Christopher Williams CPA/PFS, CFP®, MST, chrisw@kmaf.cpa

Gregory Litvinuck CPA, gregl@kmaf.cpa

Art G. Svrjcek, CPA, arts@kmaf.cpa

Main Office: (410) 643-4477