

# Executive Briefing: Annual Tax Update

*November 2022*



# Your Presenters



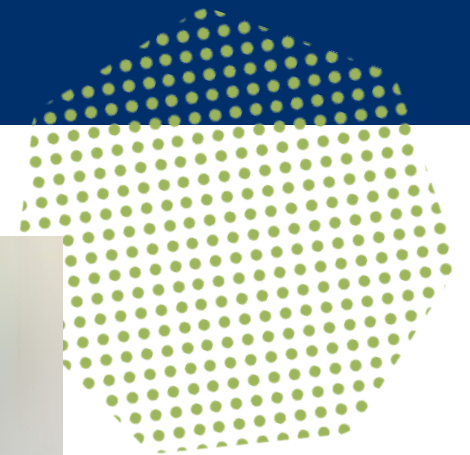
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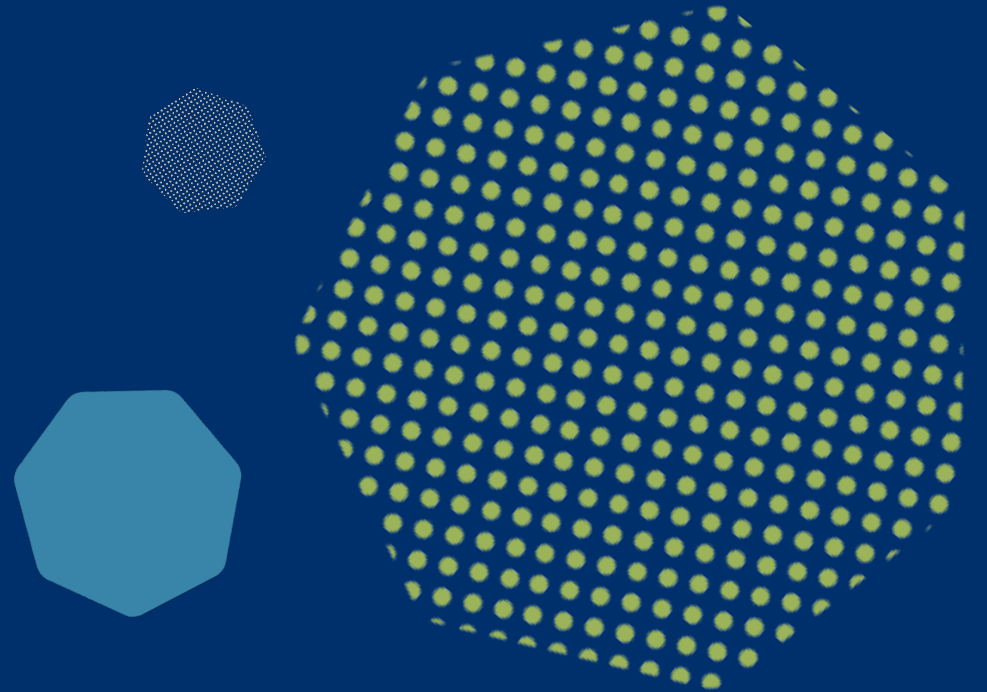
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**Change is coming.**



# Where Are We Now?

Bipartisan Infrastructure Deal



Creating Helpful Incentives to Produce  
Semiconductors Act of 2022 (CHIPS Act)



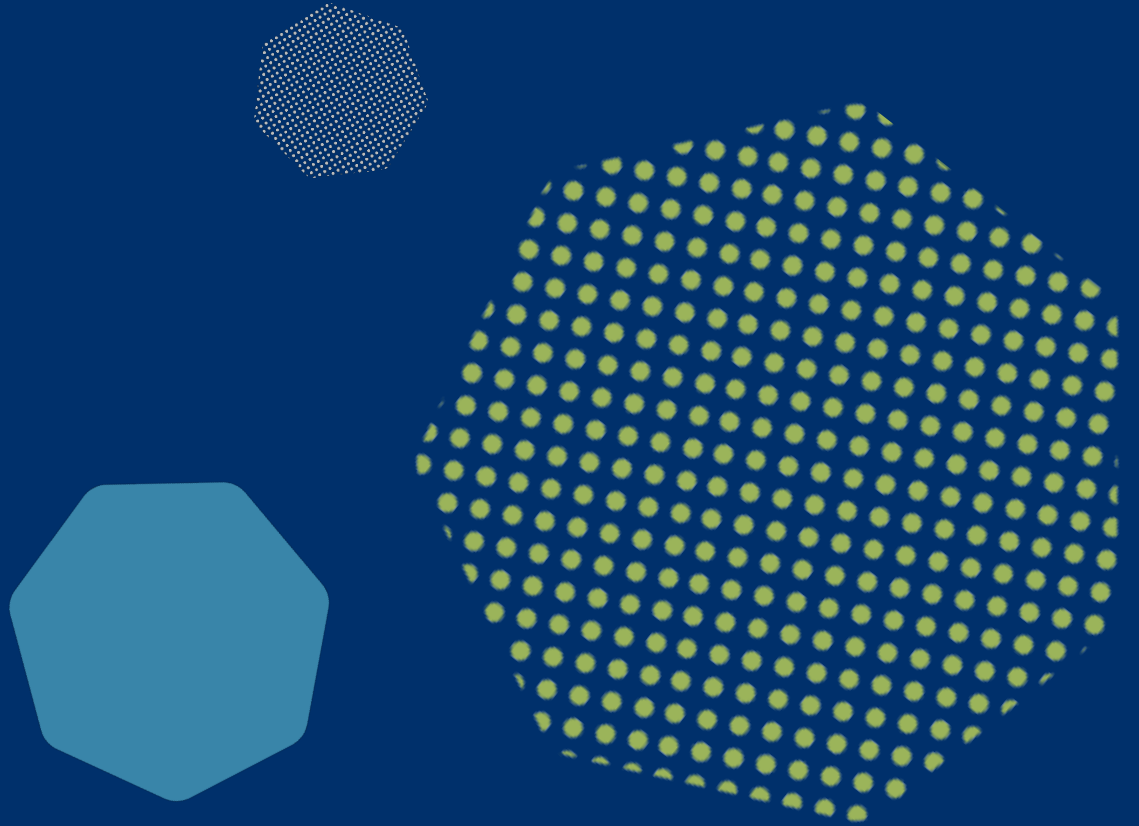
Inflation Reduction Act



Will there be more tax developments before 12/31/2022???



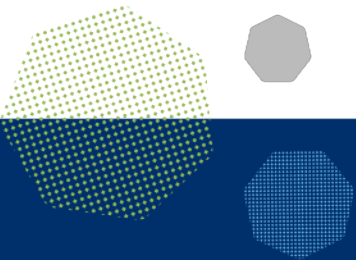
# Bipartisan Infrastructure Deal



# Bipartisan Infrastructure Deal

## Reporting of Digital Assets

- Beginning with the 2023 calendar year
- The sale of “digital assets” (i.e. Cryptocurrency) would be subject to 1099-B reporting by “brokers”.
- “Digital assets” would also be considered “cash” for purposes of the \$10,000 payment disclosure rules.
  - Form 8300 – Report of Cash Payments over \$10,000 Received in a Trade or Business.



# Bipartisan Infrastructure Deal

## Reinstatement of Superfund Excise Taxes

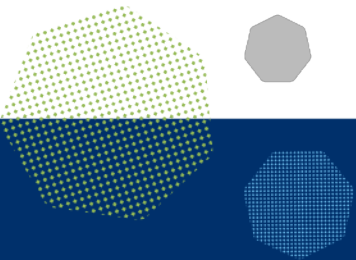
- Effective July 1, 2022
- Reinstatement of per-ton excise tax on sale of 42 chemicals
  - Generally, would apply to manufacturers, producers, and importers of these chemicals.
  - Some exceptions would apply



# Bipartisan Infrastructure Deal

## Tax Planning Ideas

- Review your eligibility to take the Employee Retention Credit for 2020 and 2021.
- If you accept digital currency, implement procedures to include this when reporting cash payments >\$10k.
- Consider and plan for the reinstated superfund excise taxes on chemicals.



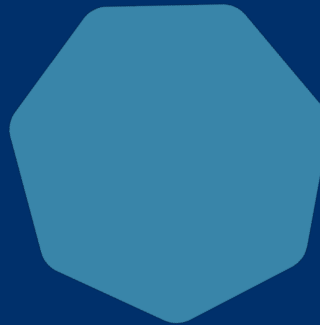
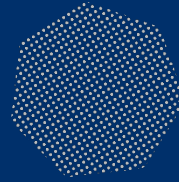


# Polling Question #1

- Has your business obtained any benefits from the Employee Retention Credit?
- No
- Yes, For 2020
- Yes, For 2021
- Yes, for 2020 and 2021



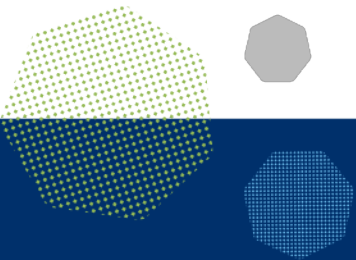
# Creating Helpful Incentives to Produce Semiconductors Act of 2022 (CHIPS Act)



# CHIPS Act

## Semiconductor Manufacturing Incentives

- Manufacturing Incentives
  - Subsidies, Grants, and Loans
  - R&D
  - Workforce development
- Investment Tax Credit
  - 25% Federal credit for investment in certain qualifying property for manufacturing semiconductors (Facilities and Equipment).
- Effective Years beginning after 12/31/2022



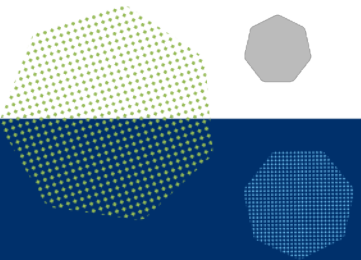
# Inflation Reduction Act



# Inflation Reduction Act

## Corporate Minimum Tax - Large Corporations

- A new minimum tax of 15% on financial statement profits
  - Would apply to corporations with:
    - 3-Year average adjusted financial statement income >\$1 Billion
    - Law contains rules to include affiliated entities, foreign-parented groups, effectively connected income.
- Effective Years beginning after 12/31/2022



# Inflation Reduction Act

## Excess Business Loss (EBL) Limitation

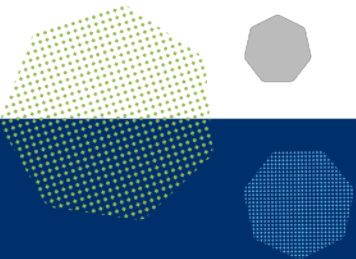
- Introduced in the Tax Cuts and Jobs Act (TCJA)
  - Limitation was set to expire at end of 2025.
- The Inflation Reduction Act has extended the EBL limitation through the end of 2028.
- The aggregate amount of deductible business losses are limited for individual taxpayers.
- Losses in excess of the limitation carry forward as a Net Operating Loss.

	<u>MFJ</u>	<u>Single</u>
2022	\$540,000	\$270,000
2023	\$578,000	\$289,000

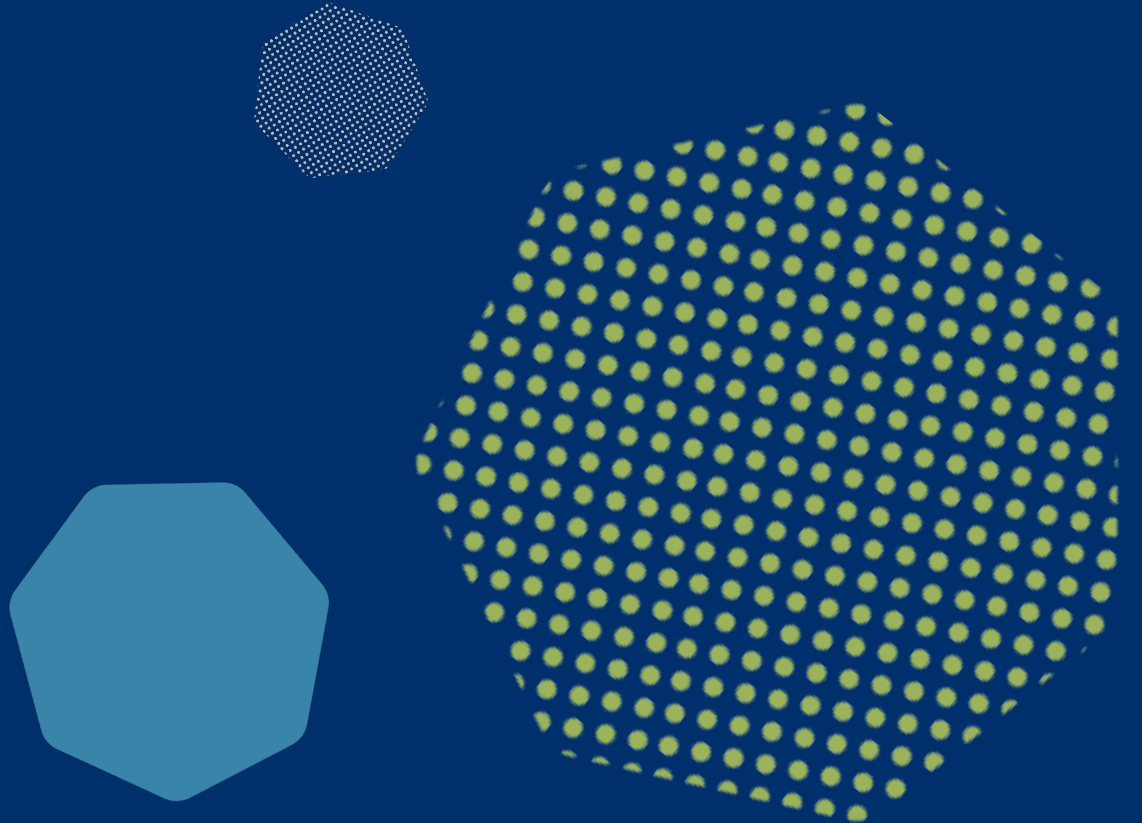
# Inflation Reduction Act

## Research & Development Credit against Payroll Taxes

- For years beginning after 12/31/2022
- Eligible Small Businesses can reduce payroll taxes up to \$500,000 annually.
  - Prior limit was \$250,000
- Eligible small business, generally
  - <\$5M in revenue
  - Revenue for less than 5 years.



**2022: What planning should be considered under current and existing tax law?**



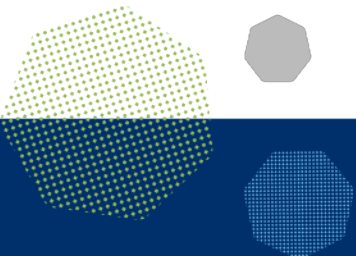


# Research & Development Expenses

- Effective for amounts paid or incurred in tax years beginning after December 31, 2021, taxpayers may no longer deduct research & development expenditures (IRC §174). These expenditures must be capitalized and amortized.

	<u>Amortization Period</u>
Domestic R&D	5 Years
Foreign R&D	15 Years

- Software Development – Amounts paid in connection with the development of any software shall be treated as a research & development expenditure.



# Depreciation Planning

- Bonus Depreciation

- 100% - 2021-2022
- 80% - 2023
- 60% - 2024
- 40% - 2025
- 20% - 2026

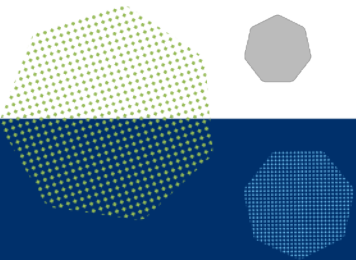
- §179 Depreciation

- Maximum expense election
  - 2022 - \$1,080,000
  - 2023 - \$1,160,000
- Phaseout threshold
  - 2022 \$2,700,000
  - 2023 \$2,890,000



# Depreciation Planning

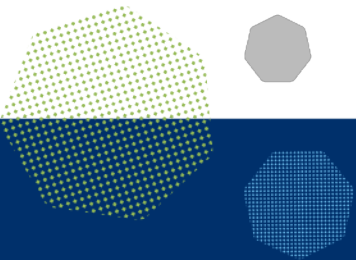
- Consider Cost Segregation Study
  - New construction
  - Building purchase
  - Remodel
- Consider elections to slow down depreciation
  - Manage tax rates
  - Manage Excess Business Losses
  - Manage Net Operating Losses



# Polling Question #2

Is the current state of the economy causing you to cut back on capital expenditures?

- Yes
- No



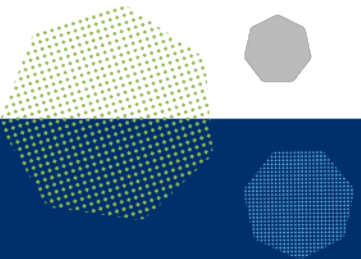
# Deductible Interest Expense - §163(j)

- Section 163(j), as amended by the TCJA, limited the amount of business interest allowed as a deduction to:
  - 30% of the taxpayer's adjusted taxable income (ATI) for the tax year.



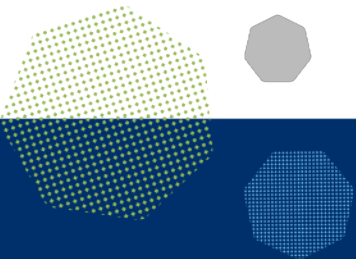
# Deductible Interest Expense - §163(j)

- ATI is computed as taxable income computed without regard to:
  - any item of income, gain, deduction, or loss that is not properly allocable to a trade or business,
  - business interest expense or business interest income,
  - the amount of any net operating loss (“NOL”) deduction,
  - the 20% deduction for certain passthrough income (199A),
  - and in the case of tax years beginning before 1/1/2022, any deduction allowable for depreciation, amortization, or depletion.



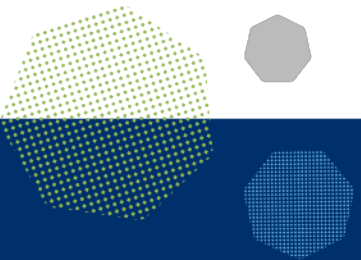
# 163(j)(7) Election – Real estate Business/Farming Business

- Two types of business can elect out of the 163(j) interest limitation:
  - Real property trade or business
  - Farming businesses
- The election is *irrevocable*, and requires the electing business to utilize the Alternative Depreciation System with respect to certain of its assets.



# LIFO Inventory

- Material and Labor Costs Are Increasing
- Consider making an election to account for your inventory on the LIFO (Last-in First-out) method of accounting





# S-Corporation vs. C-Corporation

## S-Corporation

- Single Tax
- 20% QBI Deduction (until 2025)
- Income passes through to shareholders

## C-Corporation

- Double Tax
- 21% Tax Rate
- Income taxed at corporation.

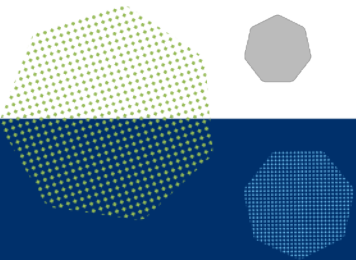


# Small Business Taxpayer Exception

Taxpayers with average gross receipts of less than \$27 million (\$29M for 2023):

May make an accounting method change to elect:

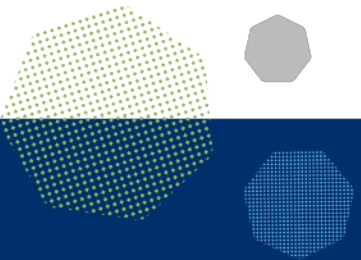
- To use the cash method of accounting.
  - To be exempt from requirement to maintain inventories.
    - However, taxpayers must:
      - Treat raw materials inventory as non-incidentals materials & supplies, or
      - Follow applicable financial statement treatment
  - To be exempt from the uniform capitalization (UNICAP) rules.
  - To be exempt from requirement to use percentage-of-completion accounting for long-term contracts to be completed in two years.



# Polling Question #3

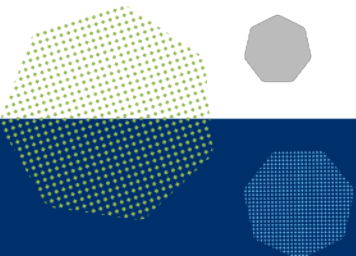
Have you recently reviewed your business succession, and personal estate planning:

- Yes, Business Succession planning
- Yes, Estate Planning
- Yes, Both Business Succession Planning and Estate Planning.
- None of the above



# Estate Planning

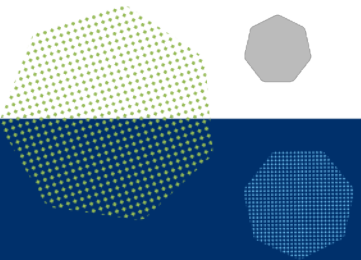
- Estate & gift tax lifetime exclusion:
  - 2022 - \$12,060,000
  - 2023 - \$12,920,000
  - Amount will be indexed for inflation each year through 2025
  - Estate & gift tax exemption is scheduled to revert back to 2017 amounts after December 31, 2025.
- Estate planning is still very important for administration of estate upon death.
- Annual exclusion amount for purposes of gifting
  - 2022 - \$16,000
  - 2023 - \$17,000



# Estate Planning

## Transfers During Lifetime

- Valuation Discounts
  - Lack of Marketability
  - Lack of Control
- Transfer by Gift
- Transfer by Sale
- Assets Grow Outside of your Estate
- Maintain Control of your business
  - Gift non-voting stock
  - Utilize trusts to hold stock

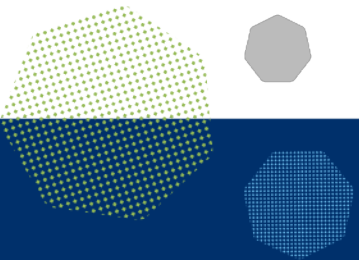


# SALT Update & Planning



# SALT CAP Workaround – “PTET” / “PTE” Tax

- The 2017 Tax Cuts and Jobs Act temporarily capped the deduction for aggregate state and local taxes, including income and property taxes (or sales taxes in lieu of income taxes), at \$10,000. The SALT cap is set to expire after 2025. For now, it mainly affects high-income earners who live or operate in high-tax states and itemize deductions.
- The SALT cap is primarily applicable to individuals—but not entities. Many states have passed laws to pay state and local taxes at the entity level. This so-called “workaround” benefits individual taxpayers for federal tax purposes.
- Individual PTE owners, who would have been subject to the \$10,000 SALT deduction cap if they had paid state and local taxes directly, see the benefit of taxes paid by the PTE reflected in a reduction of their shares of PTE income



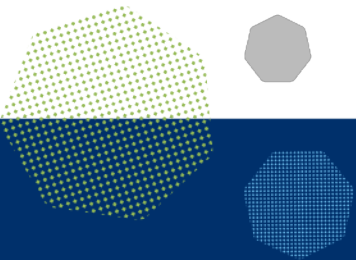
# SALT CAP Workaround – “PTET” / “PTE” Tax

State PTE tax - No two states are the same – Most state PTEs rules differ in the following:

- Who can make the election (CA can't have a limited p/s)
- Whether the tax is binding on all eligible partners
- Type of partners included (MO allows C Corp most do not)
- Income subject to tax (Apportioned, As a Corporation, Gross, etc.)
- Differences in tax rates (fixed or sliding scale)
- # of owner factors that can impact decision

Reasons Why State are Passing these Elections:

- Auditability – easier to audit a single taxpayer versus tracking down different owners.
- Compliance consistence on treatment of sourcing (allocation v apportionment).
- Surprised that we haven't seen more states be mandatory (i.e. CT).

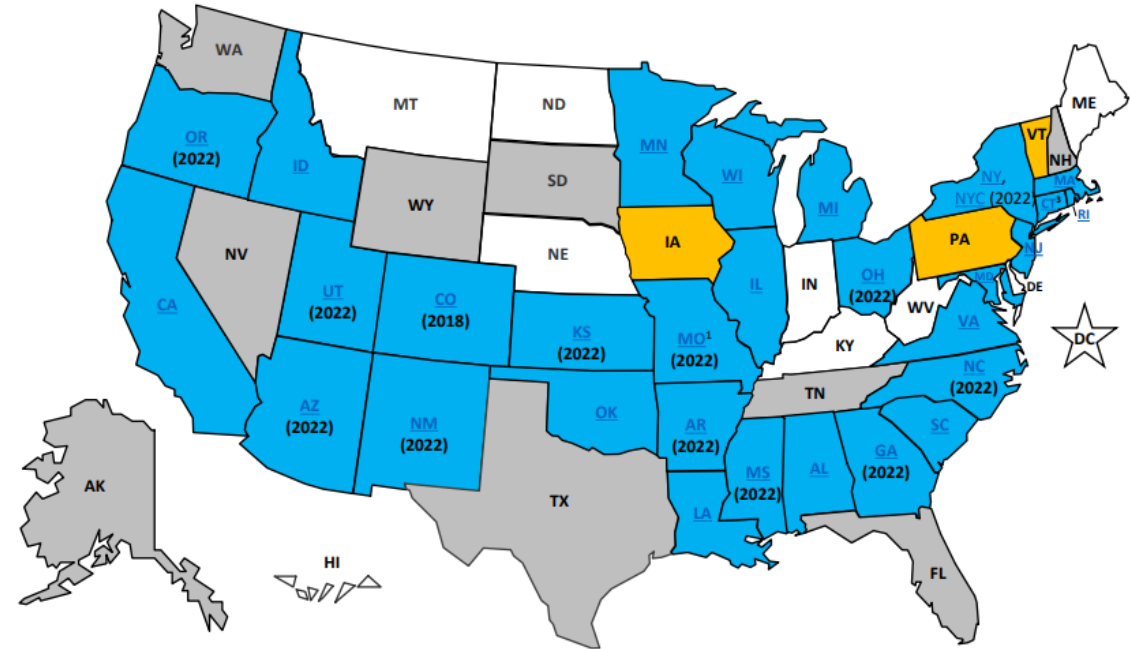




# SALT CAP Workaround – “PTET” / “PTE” Tax

- Challenges and complexities exist when an entity has income and resident partners in multiple states, states without PTET likely do not give partners a credit for taxes paid to other states (e.g. Pennsylvania).
- Current map (provided by AICPA) – Note the number of new states in 2022

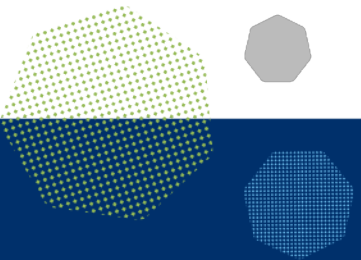
As of August 31, 2022



# Polling Question #4

True or False - I only need to look at the details on the PTE Tax in my home state / state of residence.

- True
- False

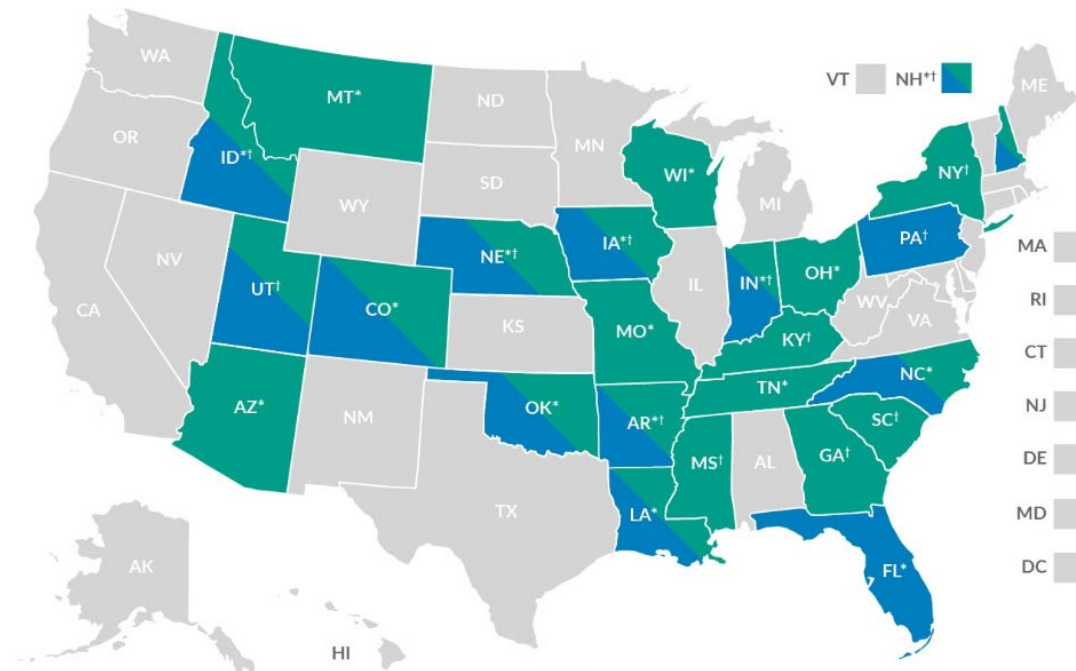


# Rate Reductions – 2021 and 2022

## Income Tax Rate Reductions Enacted or Implemented in 2021 and 2022

As of July 13, 2022

- Numerous states have enacted tax rate reductions for both individual and corporate income taxes.
- Map (provided by Tax Foundation)



Note: In Florida, a corporate income tax rate reduction was automatically triggered for 2021 only. Colorado's Taxpayer's Bill of Rights (TABOR) triggered a temporary individual and corporate income tax rate reduction for 2021. New Hampshire does not tax wage and salary income, but its tax on individual interests and dividends income is phasing out over time. Tennessee's tax on interests and dividends income, the Hall Tax, was eliminated effective January 1, 2021.  
Source: Tax Foundation.

■ Individual Income Tax Reduction

■ Corporate Income Tax Reduction

\* Rate reduction enacted/implemented in 2021

† Rate reduction enacted/implemented in 2022

# State Income Tax Updates

## Missouri

- **Research & Development Tax Credit** – The aggregate of all R&D tax credits authorized by Missouri’s Director of Economic Development is capped at \$10 million, annually. \$5 million shall be reserved for minority business enterprises, women’s business enterprises and small businesses.
  - For Tax Years beginning on or after January 1, 2023
  - Limitations:
    - Missouri’s Director of Economic Development may authorize a taxpayer to receive a tax credit against tax in an amount equal to or greater of 15% or 20% (College) of the taxpayer’s “Additional Qualified Research Expenses” (AQRE) in the state. AQRE is the current year QRE over the previous 3 year average. “Qualified research expenses” have the same meaning as provided in IRC Section 41.
    - Tax credit cannot exceed 200% of the taxpayer’s average qualified research expenses incurred during the three immediately preceding tax years. No single taxpayer can receive more than \$300,000 in tax credits per tax year. If the total eligible claims for credits received in a year exceed the annual cap, each eligible claimant shall be issued credits on a pro rata basis, after all new businesses (less than five years old) are issued full tax credits first.
    - 12 succeeding years or transfer, sell or assign up to 100% of the credit amounts to other taxpayers. For a taxpayer with a flow-through tax treatment to its members, the tax credit will be allowed to members in proportion to their share of ownership on the last day of the taxpayer’s tax period.

# State Income Tax Updates

## Pennsylvania

- **Rate Change, Sourcing Change (Intangibles) and Economic Nexus –**
  - Starting with the 2023 tax year, Pennsylvania’s corporate income tax rate will phase down from its current rate of 9.9%. For tax years beginning in 2023, the corporate income tax rate will be 8.99%, and will decrease 0.5% yearly until it reaches its final 4.99% rate beginning January 1, 2031.
  - Codified the state’s corporate income tax economic nexus standard, which until now, was summarized in the Pennsylvania Department of Revenue’s Corporation Tax Bulletin 2019-04. For tax years beginning after December 31, 2022, a corporation with \$500,000 or more of sales sourced to Pennsylvania in the current tax year is presumed to have substantial nexus with the state and is subject to state corporate income tax.
  - Amends the rules for sourcing gross receipts from intangible property. Currently, gross receipts from intangible property are sourced using an income-producing activity (i.e., costs of performance) approach. For tax years beginning after December 31, 2022, gross receipts from intangible property will be sourced using a market-based approach, which is currently used for sourcing receipts from services.
- **Other Development - PA Amazon FBA Ruling – September 9, 2022**
  - *Pennsylvania has ruled in Online Merchants Guild v. Hassell that out-of-state sellers using the Fulfillment by Amazon program did not have the minimum contacts necessary with the state to be subject to the state sales tax or personal income tax, finding that the storage of merchandise by Amazon in Amazon warehouses in the state insufficient.*

# MTC – P.L. 86-272 Interpretation

- In August of 2021 the Multistate Tax Commission (MTC) made the first changes in over 20 years to their interpretation of P.L. 86-272. The most significant changes relate to the adoption of nexus creating activities conducted via the internet. CA and NY adopted, more to come.
- The MTC acknowledged the shift to a service & internet-based economy and now recommend that the following activities be considered beyond the protections of P.L. 86-272 when conducted over the internet:
  - Regularly providing post-sale assistance to in-state customers through an electronic chat or email that customers initiate by clicking on an icon on the business's website (Ex. 2)
  - Remotely fixing or upgrading in-state customers' previously purchased products by transmitting code or other electronic instructions to those products over the internet (Ex. 7)
  - Placing on the business's website an invitation to viewers in the customer's state to apply for non-sales positions within the business (the example states that the website enables viewers to fill out and submit an online application and submit a resume and cover letter) (Ex. 4)

# Sales Tax Updates

## Effective January 1, 2023:

- **Missouri - (as the last state in the US) begins enforcement of post-Wayfair economic nexus standards and marketplace facilitator legislation.**
  - Consumers will see Amazon and other marketplace facilitators collecting tax on all sales.
  - MANY more **out of state** vendors (software, manufacturing equipment, etc.) will begin collecting tax on 1/1/2023.
  - For any exempt purchases (resale, manufacturing, etc.) make sure that vendors have exemption documentation on file or taxes will be charged erroneously.
- **Kentucky – SaaS and other Services now Subject to Tax**
  - On April 13, 2022, the Kentucky Legislature overrode Governor Andy Beshear’s veto of House Bill 8, which contains several new tax provisions. For sales and use tax purposes, the legislation expanded the list of taxable services subject to state sales and use tax to include **over 35 additional services**. Services such as marketing and website hosting will now be subject to the state sales tax starting January 1, 2023. Refer to House Bill 8 for a full listing of taxable services that may apply to your business.
  - It’s important to note, starting in 2023, Kentucky will join the list of states that tax “prewritten computer software access services” (i.e., SaaS).

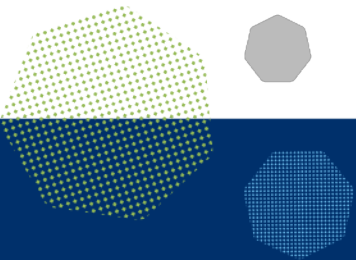
# Sales Tax Updates (Cont.)

## Wisconsin – NFT Guidance – Look-through to underlying product/service

- Wisconsin has issued guidance on the taxability of non-fungible tokens (NFTs) in its most recent monthly tax bulletin. Per the bulletin, the sale or purchase of an NFT may be taxable if the underlying product, good, or service is taxable in Wisconsin. The bulletin provides three illustrative examples:
  - If the NFT entitles a purchaser to download music or movies, the sale of the NFT is a taxable specified digital good.
  - If the NFT entitles a purchaser an admission to a sporting event, the sales of the NFT is a taxable admission.
  - If the NFT entitles a purchaser to a tangible piece of artwork, the sale of the NFT is taxable tangible personal property.

## Tennessee – Farm Equipment Sales and Use Tax Exemption Updated Effective 1/1/2023

- The new regulations replaced the prior list of specifically enumerated items qualified for exemption, and exempts building materials, fencing material, warranties, and most other items of tangible personal property used primarily in agricultural from tax.
- Automobiles, trucks, household appliances, and fuel for vehicles operated on public highways do not qualify for the exemption.

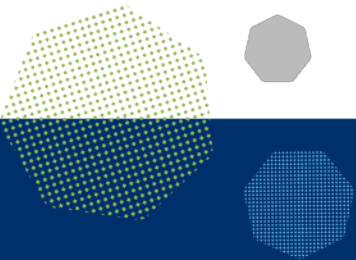




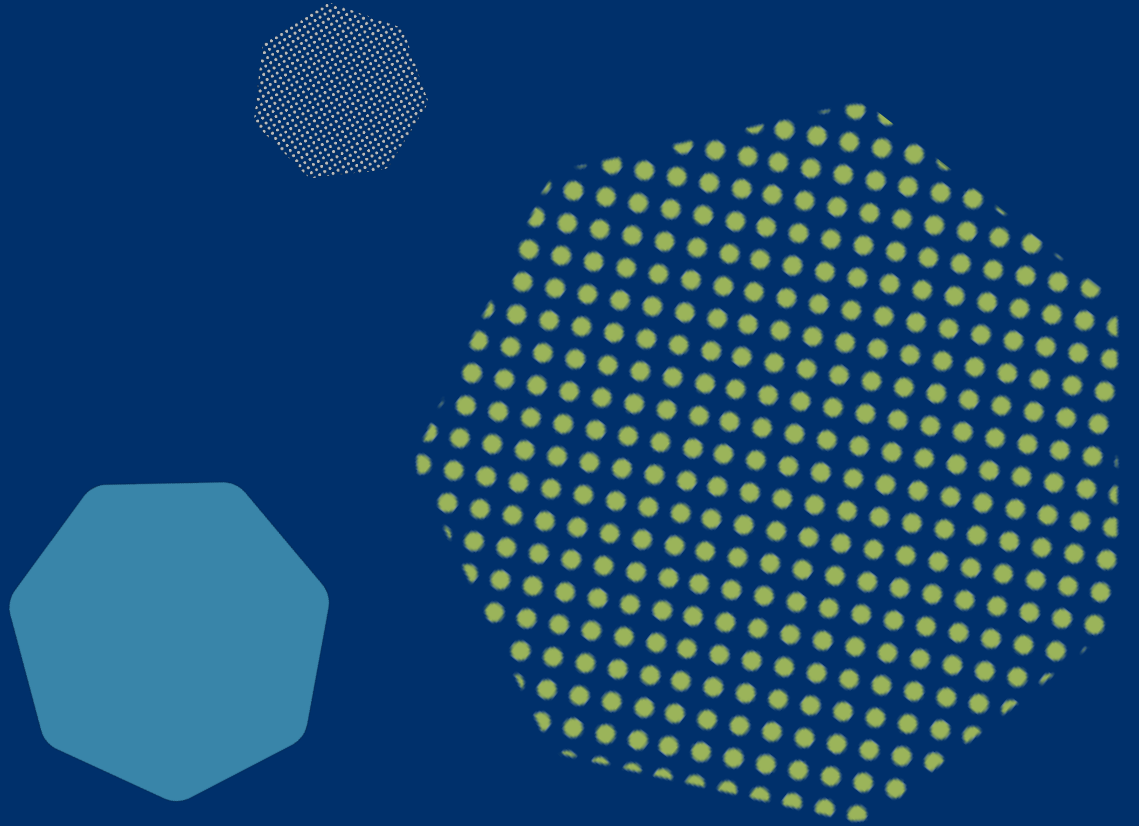
# State Activity – Nexus Questionnaires and Audits

States seeking additional revenue through expansion of tax base (see prior updates on nexus, taxation of services, etc.) and enforcement. Pivotal timing for sales/use tax as most states are now 2.5 – 4 years past “economic nexus” regulation enactment.

1. Arizona – Sales Tax Registration Scrutiny
2. Wisconsin – Nexus Questionnaires - aggressive income tax nexus determinations for service providers
3. Customer Sales Tax Audits Resulting In Vendor Inquiry



# Questions



# THANK YOU!



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