

Making the Most of Year-End Tax Planning for Businesses

Strategies for Optimizing Tax Outcomes This Fiscal Year

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Agenda

- Accounting Methods
- Tax Deductions
- Business Incentives & Tax Credits
- International Tax
- Transaction Planning
- Real Estate Considerations
- State & Local Tax

Accounting Methods

Accounting Methods

■ Inventory

- › Represents largest cost for many businesses = largest potential tax deduction
- › Choice of inventory methods/how inventory is accounted
 - Directly affects cost of goods sold calculation and taxable income
 - May result in acceleration of deductions

Accounting Methods (cont.)

■ Inventory Methods

› Alternative Inventory methods

- Lower of Cost or Market – Value ending inventory at market value when it is lower than cost of the inventory
- Net Realizable Value – Reduce value of inventory to net realizable value (selling price)

Accounting Methods (cont.)

- **Inventory Write-Offs (obsolete, unsalable, damaged, defective or not needed)**
 - › Financial reporting: reduced using a reserve account
 - › Tax purposes: generally must be disposed of to recognize an expense
 - › Review inventory and physically dispose of obsolete or unsalable inventory

Accounting Methods (cont.)

■ Bad Debts

- › Reserves for bad debts nondeductible for tax purposes
- › Identifying and writing off specific bad debts can result in a deduction
- › Analyze accounts receivables; identify and write off fully or partially worthless balances

Accounting Methods (cont.)

■ Prepaid Expenses

- › Opportunity to deduct certain prepaid expenses
- › Payments considered “economic performance” are generally deductible if:
 - Fixed and determinable at year-end, and
 - Related benefits occur within 12 or fewer months

Accounting Methods (cont.)

■ Prepaid Expenses (cont.)

- › Can generally be accelerated:
 - Insurance
 - Property taxes
 - Maintenance service contracts
 - Software subscriptions
- › Identify which prepaids are eligible for accelerated deduction and determine whether to pay before year-end
- › Can file change in accounting method to change tax treatment

Accounting Methods (cont.)

■ Year-End Compensation

- › Accrual basis taxpayers may be able to deduct accrued compensation (bonuses, commissions, vacation, severance pay) in the current year if:
 - Liability is fixed and reasonably determinable at year-end,
 - Employee has performed the services, and
 - Payment is made within 2 ½ months after year-end
- › Does not apply to related party employees

Accounting Methods (cont.)

■ Year-End Compensation (cont.)

- › Compensation contingencies at year-end are not deductible in the current year
- › Take steps to ensure accrued compensation is fixed at year-end
 - Board resolution establishing the liability
 - Formal policy establishing the liability

Polling Question 1:

Which accounting method do you think provides your business with the most planning opportunities?

- A. Inventory methods
- B. Bad debt and other reserve write-offs
- C. Prepaid expenses
- D. Year-end compensation, e.g., bonuses, vacation pay, etc.

Tax Deductions

Tax Deductions

- **Sec. 199A Qualified Business Income Deduction (QBID)**
 - › QBID: deduction equal to 20% of qualified business income
 - › The OBBBA permanently extended QBID (previously set to expire for taxable years beginning after December 31, 2025)
 - › Eligible taxpayers:
 - Individuals
 - Trusts and estates who are partners in partnerships (including certain LLC members)
 - S Corporation shareholders
 - Sole proprietorships

Tax Deductions (cont.)

- **QBID (cont.)**

- › Subject to several adjustments and limitations; benefit may phase out based on the level of adjusted gross income
- › Maximizing QBID requires careful planning

Tax Deductions (cont.)

■ Accelerated Depreciation Provisions

- › Bonus Depreciation – Permanently Extended (OBBBA)
 - Increased first-year depreciation percentage to 100% for property acquired and placed in service on or after January 19, 2025
 - Must be taken on all new or used property with a tax life of 20-years or less
 - Must elect out of bonus depreciation for it to not apply
- › If need additional deductions, consider whether qualifying assets can be acquired and placed in service before year-end

Tax Deductions (cont.)

■ Accelerated Depreciation Provisions (cont.)

› Sec. 179 Election – Increased (OBBBA)

- New maximum expense amount \$2.5 million (reduced by amount by which cost of qualifying property exceeds \$4 million)
- Qualifying property = new and used
 - Tangible personal property
 - Vehicles
 - QIP
 - Roofs, HVAC, fire protection, alarm and security systems (nonresidential)

Tax Deductions (cont.)

■ Accelerated Depreciation Provisions (cont.)

› Qualified Improvement Property (QIP)

- Improvements made to interior of nonresidential building – after building first placed in service
- Building must be owned or leased by taxpayer making the improvements
- Exterior improvements, structural changes and expansions/additions do not qualify
- QIP qualifies for bonus depreciation and Sec. 179 expensing

Tax Deductions (cont.)

■ Tangible Property Regulation Opportunities

- › Implemented in 2014 and (apparently) forgotten over time
- › Determine whether costs related to tangible property must be capitalized and expensed over time or can be deducted immediately as expenses
- › Considerations:
 - Are you following your capitalization policy?
 - Are there partial disposals that could result in losses?
 - Are repairs and maintenance being capitalized when they could be expensed under these regulations?

Tax Deductions (cont.)

■ **Sec. 163(j) Interest Expense Limitation**

- › Can further increase the already high cost of financing by limiting the deduction for net business interest expense.
- › The OBBBA reinstated a more favorable interest expense deduction framework by restoring an EBITDA-based limitation
 - Depreciation and amortization are now added back as part of the computation of adjusted taxable income (ATI)
 - Accelerated amortization on previously capitalized Section 174 will be added back to ATI in 2025

Tax Deductions (cont.)

■ **Sec. 163(j) Interest Expense Limitation (cont.)**

- › New OBBBA rules for 2026 tax year and beyond eliminate the planning strategy of capitalizing interest to inventory or other balance sheet accounts
- › Sec. 163(j) limitation must be considered before applying other capitalization provisions
- › In 2025, capitalized interest still removed from Sec. 163(j), could allow much larger deduction than previous years

Tax Deductions (cont.)

■ Charitable Contributions

- › For tax years beginning after December 31, 2025, the OBBBA imposes 1% floor on charitable contributions of C Corporations
- › C Corporation taxpayers should consider accelerating future planning charitable contributions to 2025

Tax Deductions (cont.)

■ Research and Experimentation (R&E) Expenses

- › The OBBBA allows taxpayers to immediately deduct domestic R&E expenses paid or incurred in the tax year beginning after December 31, 2024
 - Expenses for R&E performed outside the U.S. must still be capitalized and amortized over 15 years
- › Several elections to consider for 2025:
 - Deduct R&E expenditures for tax years beginning after December 31, 2024
 - Continue to capitalize R&E costs and amortize them over 60 months
 - Accelerate deduction for previously capitalized, but unamortized, costs over a one- or two-year period, starting with their first tax year beginning after December 21, 2024

Tax Deductions (cont.)

- **Research and Experimentation (R&E) Expenses (cont.)**
 - › Small business taxpayers can apply rule retroactively to tax years beginning after December 31, 2021
 - › Carefully consider which election(s) to make
 - To maximize tax benefits, consider effective tax rate, net operating losses, credits and other tax attributes

Tax Deductions (cont.)

■ Vehicle Tax Deductions

- › Standard Mileage vs. Actual Costs
- › Vehicle-Related Depreciation

Passenger Vehicles (less than or equal to 6,000 lbs. gross vehicle weight rating (GVWR):	Heavy SUVs, Trucks and Vans (6,001 – 14,000 lbs. GVWR):	Very Heavy Vehicles (greater than 14,000 lbs. GVWR):
<ul style="list-style-type: none">• Sec. 179 and/or bonus depreciation can be taken, but luxury auto limitations will apply.• For 2025, the first-year limit is \$12,200 (without bonus depreciation) or \$20,200 (with bonus depreciation).	<ul style="list-style-type: none">• Sec. 179 depreciation is available, but the amount is limited to \$31,300 per vehicle for 2025.• Bonus depreciation can be taken on the excess amount.	<ul style="list-style-type: none">• Full Sec. 179 depreciation is available, along with bonus depreciation.

- › Accounting for Personal Use

Polling Question 2:

Section 199A (aka the QBI deduction) is applicable to C Corporations.

- A. True
- B. False

Business Incentives & Tax Credits

Business Incentives & Tax Credits

- **Sec. 1202 Qualified Small Business Stock Exclusion**
 - › Tax incentive for investors in certain small businesses
 - › Allows capital gains from sale of Qualified Small Business Stock (QSBS) to be excluded from federal income tax
 - › Must acquire stock directly from company in exchange for money, property or services and hold it for more than five years

Business Incentives & Tax Credits

- **Sec. 1202 Qualified Small Business Stock Exclusion – Expanded Benefits (OBBBA)**
 - › Rules now allow partial exclusions on three-year (50%) and four-year (75%) holding periods, in addition to 100% exclusion after five years
 - › Increases aggregate gross asset threshold to qualify as a “small business”
 - › Raises lifetime cap on excluded gains per issuer
 - › Consider converting a previously ineligible investment type into an eligible corporation to qualify for Sec. 1202 benefit
 - Consider all tax and economic consequences

Business Incentives & Tax Credits

■ Research and Development (R&D) Credit

- › Available to companies developing new or improved business components:
 - Products
 - Processes
 - Computer software
 - Techniques
 - Formulas that result in new or improved functionality, performance, reliability or quality
- › Several methods for calculating the credit
- › Many qualifying businesses do not claim the credit
- › Consider qualifying activities of your company

Business Incentives & Tax Credits

- **Interest Charge Domestic International Corporation (IC-DISC) for Exports**
 - › Pass-through entities and sole proprietors who manufacture or distribute U.S. goods for export, or foreign architectural, engineering or managerial services
 - › Taxpayer with IC-DISC can pay and deduct a commission calculated based on qualifying exports and the related net income to the IC-DISC
 - Ordinary deduction - tax value may be as high as the highest marginal income tax rate of the business
 - Receipt of commission is tax-free to the IC-DISC; if commission is distributed as dividend payment, qualifies for capital gain tax rates

International Tax

International Tax

- **FDII Deduction – Modified (OBBBA) Tax Years Beginning after December 31, 2025**
 - › Eliminates requirement to reduce deduction eligible income by 10% of the qualified business asset investment (QBAI)
 - › FDII now includes returns from tangible assets and is renamed “foreign-derived deduction eligible income” (FDDEI)
 - › Deduction is now 33.34% for tax years beginning after December 31, 2025, equating to a 14% effective tax rate on eligible export income

International Tax

- **Avoiding Accidental Permanent Establishments**
 - › Taxpayers doing business in foreign countries potentially liable for local income tax for income earned in the foreign country
 - › If U.S. has income tax treaty with a country, a fixed place of business (or permanent establishment) must exist to create an income tax liability
 - Employees exercising authority to conclude contracts often create a deemed permanent establishment

International Tax

- **Avoiding Accidental Permanent Establishments (cont.)**
 - › U.S. businesses should evaluate business activity outside U.S. for unintentional permanent establishment/local country income tax liability
 - › For countries in which the U.S. does **not** have an income tax treaty, a very low level of activity could potentially create a taxable presence, e.g., Argentina, Brazil, Hong Kong, Taiwan, Vietnam)

Transaction Planning

Transaction Planning Considerations

- › Gain from sale of a business can be taxed differently for federal, state and local tax purposes
- › Buyer generally prefers asset purchase – avoids assuming certain target liabilities and is permitted to step-up the basis of assets
- › Seller often prefers equity sale because some or all the gain will often be taxed at preferential capital gain rates

Transaction Planning Considerations (cont.)

- › Certain tax provisions permit an equity sale for legal purposes and an asset sale treatment for income tax purposes – structure significantly impacts how the sale is taxed
- › If considering selling, model out projections of the gain and applicable taxes under various scenarios

Polling Question 3:

Are you considering selling your business in the next 12-24 months?

- A. Yes
- B. No
- C. Unsure

Real Estate Considerations

Real Estate Considerations

- **Interest Expense Limitation and Real Property Trade or Business Exception**
 - › Irrevocable election; exempts an entity from the interest limitation
 - › ADS required for real property; no bonus on QIP
- **Cost Segregation Studies**
 - › Identifies specific real property assets and reclassifies for income tax purposes into often shorter depreciable lives

Real Estate Considerations (cont.)

- **Revisit Repair Regulations**

- › Capitalization policy
- › *De minimis* safe harbor and other elections
- › Is something truly an improvement, or is it a deductible repair?

- **Write-Off of Abandoned Project Costs**

- **Qualified Opportunity Zones (QOZs)**

- › Economic development program providing taxpayers with tax benefits in exchange for reinvesting capital gains into businesses and real estate located in opportunity zones
- › Made permanent as part of the OBBBA

State & Local Tax

State & Local Tax

- **State Income Tax Conformity with Changing Federal Legislation**
 - › Varies widely by state; some automatic, some must enact specific legislation
 - › When federal tax provisions change, many states indicate whether or not they will conform
 - › Continue to monitor 2025 and 2026 state legislation around tax conformity with federal changes that could materially impact state tax liability

Polling Question 4:

What business planning topics are you most interested in learning more about?

- A. Accounting methods
- B. Deductions
- C. Tax credits and incentives
- D. State and local

State & Local Tax

■ State Tax Nexus Considerations

- › Increasingly more complex since the *Wayfair* decision and more remote work
- › *Wayfair*, while intended for sales tax, has affected nexus standards for state and local income tax
- › States are becoming more aggressive in assessing nexus

State & Local Tax

- **State Tax Nexus Considerations (cont.)**

- › Many businesses shifting to hiring remote employees
- › More complex state tax filings for employers – now must also consider activities of each remote employee to understand when a state or local income tax filing may be required
- › Remote work may impact statutory credits and/or negotiated incentives.

State & Local Tax

■ State Tax Nexus Considerations (cont.)

- › Nexus studies increasingly important tool in tax planning and risk mitigation
- › Public Law 86-272 generally limits income tax nexus for businesses whose employees are soliciting sale of tangible personal property
 - Pay close attention to job responsibilities of remote employees

State & Local Tax

■ Sales/Use Tax

- › In many states, sales of tangible property are subject to sales tax
- › Services traditionally classified as nontaxable; however, more states expanding taxation of certain services and digital purchases
- › Create policies to identify taxable vs. exempt purchases to help ensure not under or overpaying sales/use tax liabilities

State & Local Tax

■ Sales/Use Tax (cont.)

- › Sales tax exemptions may require seller to collect/maintain valid exemption certificates
- › Need procedures/processes to minimize exposure if selected for state tax audit. Clearly identify:
 - When sellers are required to collect sales tax on taxable sales
 - How business will collect and manage exemption certificates
- › Consider a nexus study to help ensure you are filing where required and properly documenting when exempt

State & Local Tax

■ Pass-Through Entity Tax (PTET)

- › PTET state legislation allows pass-through business entities to elect to pay and deduct state income taxes
 - Avoids state income tax deduction limit on individual shareholder or partner
- › Even with OBBBA's increase in state and local tax deduction, PTET still beneficial to many
 - For taxpayers with adjusted gross income (AGI) above \$500,000, this increased deduction will phase back down to the historical \$10,000

Year-End Planning Takeaways

- **Be proactive**

- › The tax code, including the OBBBA, offers businesses numerous tax savings opportunities
- › Tax efficiency does not often occur by chance
- › Work with your tax advisers now and throughout 2026 to proactively manage tax obligations and work toward achieving substantial savings that can positively impact your bottom line

- *Please visit our website to read the [2025 Year-End Tax Planning Guide for Private Companies](#)*

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