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Act Now to Reduce Your Business' 2022 Tax Bill

By CBM Tax Services
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As we approach the end of 2022, it's imperative to take a closer look at your tax and financial plans. 2022 has been another year of unique opportunities and challenges ranging from the effects of historic levels of inflation, a changing political landscape, dramatic swings in the stock and real estate markets, and growing recession concerns, all poised to have long-term effects on your business and personal financial situations. Now is the time for business owners re-examine their current tax strategies to ensure they are meeting their current needs while also planning for future events. Having a plan is the best way to proceed.

Changing tax matters to note

- Business meals — There is a 100% deduction for expenses paid for food or beverages provided by a restaurant through December 31, 2022. This provision expires starting in 2023, when it returns to 50%.
- Increased mileage rates – There is a 62.5 cent per mile deduction available for business mileage effective July 1, 2022 that goes through December 31, 2022. During the first six months of 2022 the standard mileage rate was 58.5 cents per mile. Additionally, the medical and moving mileage rate was 18 cents per mile, moving up to 22 cents per mile on July 1, 2022. The charitable mileage rate remained constant at 14 cents per mile.

Please remember to maintain proper detailed proof of mileage claimed in one category or another.

- Purchases of property and equipment — 2022 will be the final year that Section 168(k) first-year 100% bonus depreciation is available for qualifying property and equipment purchases. Bonus depreciation allows businesses the ability to completely write off most business assets placed in service by December 31, 2022. Starting in 2023, the bonus depreciation rate drops to 80% for eligible property and equipment, and thereafter decreasing 20% per year until the bonus expensing provision expires beginning in 2027.
- For businesses with active construction underway, there still is the opportunity for certain improvements to be considered as qualified improvement property and thus be eligible for 15-year depreciation and 100% first-year bonus depreciation. These improvements must be fully completed and in service by the end of the year to be eligible.
- The 2022 maximum Section 179 deduction has been increased from $1.05 million to $1.08 million. Functioning similarly to 100% bonus depreciation, the full purchase price of eligible property placed in service by December 31, 2022 can be deducted, phasing out when qualified property purchases exceed $2.7 million. Section 179 deductions are also limited to the amount of taxable income for the year and cannot create a loss. We can assist with an analysis to help best optimize your depreciation deductions, to reduce your 2022 tax liability.
- Research and experimental expenditures must now be amortized under Section 174, rather than expensed. Under the updated rule, these expenditures must be capitalized and amortized over a five-year period for research conducted in the US, or over a 15-year period for research activities conducted internationally.
- The business interest limitation reverts to the original Tax Cuts and Jobs Act rule for 2022, which limits the deduction for business interest expenses to 30% of adjusted taxable income. Depreciation, amortization and depletion are no longer added back to the adjusted taxable income calculation. Businesses with annual gross receipts of less than $27 million are exempt from the limit.

Extended tax provisions

- The Alternative Fuel Credit that originally expired on December 31, 2021, was extended to 2024 as part of the Inflation Reduction Act. This allows taxpayers to claim a one-time credit for $0.50 per gallon credit against the excise tax liability for qualified alternative fuels sold or used for motor vehicles, motorboats and aviation vehicles.
- The limitation on excess business losses for noncorporate taxpayers was extended to 2028 by the Inflation Reduction Act. Originally, the limitation went into effect in tax year 2018 and limited the amount of trade or business deductions that noncorporate taxpayers could offset against nonbusiness income, which was $250,000 (or $500,000 for married filing joint tax returns). The 2022 limitations are $270,000 and $540,000 for single and joint filers.

Business energy credits

As enacted by the Inflation Reduction Act, the Plug-In Electric Drive Vehicle Credit is available to businesses for qualifying electric vehicles that have final assembly completed in North America on or after August 16, 2022. The credit allows businesses to receive a $7,500 tax credit for qualified electric vehicle purchases. This credit is now comprised of two $3,750 parts for vehicles meeting "Critical Minerals" and "Battery Components" requirements. "Critical Minerals" requirements are met when 40% to 80% (phased in) of the value of applicable critical minerals in the battery are extracted/processed in the US, or a country where the US has a free trade agreement or if it has been recycled in North America. "Battery Components" requirements are met when 50% to 10% (phased in) of the value of the battery components are assembled or manufactured in North America. The credit is subject to manufacturer-suggested retail price (MRSP) limits for Vans, SUVs and trucks costing less than $80,000, and sedans and compact cars costing less than $55,000.

State and Local Tax (SALT) workaround reminders

As a result of the Tax Cuts and Jobs Act of 2017 (TCJA), a $10,000 limitation on state and local tax deductions was imposed on individuals who itemize deductions on their federal income tax return. Since 2017, states have been taking action to provide relief to taxpayers through mandatory or elective pass-through entity (PTE) taxes to offer a work around to capped SALT deductions. This mechanism allows for states to shift the tax burden from the individual level to the entity level of their taxpayers, giving them a federal tax deduction in the process.

- Since the 2020 tax year, Maryland has allowed qualifying PTEs to pay tax at the entity level by filing a Form 511 (Pass-through Entity Election Income Tax Return). This form has allowed two credits for resident PTE members, a credit for distributive share of the PTE tax paid by the entity, and a credit for state income tax paid to other states, including by the PTE.

- The District of Columbia has not made any SALT workaround changes in the 2022 tax year. DC resident taxpayers are still able to claim a credit against their income tax liability for PTE paid on their behalf to another state. These tax payments are treated as if they were paid directly by the individual, providing some relief to residential taxpayers.

- Effective July 1, 2022, Virginia established their workaround for the federal income tax limitation on deductions for state and local taxes. This allows owners of a Virginia pass-through entity (PTE) to have the ability to pay Virginia tax at the entity level at a 5.75% rate. As defined by the state, a qualifying PTE is one that is, “100 percent owned by natural persons or other persons eligible to be shareholders in an S corporation.”.

IRS increased funding

- As part of the IRA signed into law by President Biden in August 2022, a $80 billion increase in funding to the Internal Revenue Service was approved. With much of this funding (approximately $45 billion) earmarked for increased enforcement, business owners need to be as aware of their potential tax exposures as ever. While the much-publicized increase in the desired number of new IRS employees (approximately 87,000), has been an interesting subject of conversation, realistically it will take years for the IRS to scale their hiring efforts to meet the level of enforcement they would like.

- In the meantime, the IRS will be focusing its auditing efforts on taxpayers with taxable incomes of $400,000 and up, creating the need for business owners, especially owners of pass-through entities, to have a grasp on their current tax positions and have a solid tax plan.

- Cryptocurrencies will also remain as an area of interest for IRS enforcement. Given the increased popularity and the amount of fraudulent activity surrounding them, businesses using cryptocurrencies as part of their operations have a greater chance of being subject to IRS audit. This is an immensely complex area, but we can help you work through the reporting requirements and related tax consequences.

Year-end planning makes for fewer surprises

- Every tax planning situation is unique and requires a comprehensive strategy to reduce running into unintended consequences. If the past few years have taught us anything, we know that everything is subject to change at a moment's notice. Having a specific plan in place to meet your needs with the ever-changing landscape in mind is essential. Good planning involves looking at multiple years, not just one. So please keep this in mind.

Contact Councilor, Buchanan & Mitchell

- Whether it is working toward a business succession plan or getting answers to your tax and financial planning questions, we are here to help. Please call your CBM contact, or Richard E. Morris, Director – Tax Services, in our office today at (301) 986-0600 to set up your year-end review. Planning now can help you minimize your tax bill and position you for greater success.

Please contact CBM Tax Practice Director Richard Morris with any question about your tax situation at 301.986.0600 or via email at rmorris@cbmcpa.com.

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