GattoMcFerson
Certified Public Accountants

May 26, 2025

Dear Friends and Colleagues,

The House of Representatives met their Memorial Day goal and passed a massive tax proposal that impacts both individuals and businesses. This proposal is a long way from being enacted, but it gives you an idea of which way the wind is blowing.

Recent Tax Proposal

Back in 2017, the Tax Cuts and Jobs Act was passed, resulting in some significant individual and business tax law changes. Many of these changes are set to expire after 2025. The House of Representatives recently passed a detailed tax proposal addressing these expiring provisions, plus some other modifications.

Individual tax rates: The 2017 Tax Act lowered tax rates across the board. The top rate decreased from 39.6% to 37%. These lowered tax rates have been permanently extended beyond Dec. 31, 2025. Long-Term Capital Gain tax rates also remain unchanged.

Standard deduction: The 2017 Tax Act almost doubled the standard deduction for all filers, and for 2025, the amounts are set at $15,000 for single taxpayers, and $30,000 for married-filing-joint taxpayers. These increases have been permanently extended.

Itemized Deductions – SALT: The state and local tax (SALT) deduction had been capped at $10,000, which for taxpayers in states like California and New York, was devastating. The deduction has been increased to $40,000 in the proposal for years after 2024, but with certain strings attached. This increase would begin to phase-out for taxpayers with Adjusted Gross Income (AGI) of over $400,000. The deduction would revert back to its original $10,000 for taxpayers with AGI over $500,000.

Also, it is unclear if or when the SALT modification would impact the Pass-Through Entity Tax credit, which was implemented by high-tax-rate states as a work-around to this provision.

Itemized Deductions - Mortgage Interest: The 2017 Act limited the home mortgage interest deduction to the first $750,000 of debt for any debt borrowed after December 2017. This change has been permanently extended.

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Itemized Deductions – Miscellaneous: The 2017 Act eliminated most miscellaneous itemized deductions that exceeded 2% of the taxpayer's Adjusted Gross Income, such as investment/ advisory fees and unreimbursed employee expenses. This change has been permanently extended.

Child tax credit: The 2017 Act increased the child tax credit from $1,000 to $2,000 per qualifying child. This credit has been increased to a maximum of $2,500 and extended until December 31, 2028.

Personal exemptions: The 2017 Act suspended personal exemptions, which, at the time, was $2,000 per dependent. This change has been permanently extended.

Alternative Minimum Tax: The 2017 Act increased the exemption amounts, essentially eliminating this extra tax for most taxpayers. This has been permanently extended.

Sec. 199A - Qualified Business Income (QBI): Shareholders and owners of passthrough businesses (S Corporations, LLCs) and sole proprietorships, can now claim a deduction of up to 20% of their QBI. This has been permanently extended, with the deduction amount increased to 23%, along with modifications to how the deduction is calculated.

Bonus depreciation on qualified business property: The 2017 Act allowed for a large increase in the amount of qualified property (equipment, fixtures, improvements) that could be written off by a business in the year of purchase. This increase has been extended through December 31, 2029.

Estate and Gift Tax: The 2017 Act almost doubled the estate tax exclusion amount from $5,490,000 in 2017 to $11,180,000. The current exclusion amount, after inflation, is nearly $13 million per person ($26 million for married couples). At the end of 2025, this will be permanently extended, with the exclusion bumped to $15,000,000.

Reduction of Clean Energy Incentives: Scales back many clean energy tax incentives introduced in 2017. It would eliminate tax credits for electric vehicle charging infrastructure, residential energy upgrades, and solar installations on homes for projects placed in service after December 31, 2025.

Pass-Through Entity Tax Payments

It is unclear if or when there will be limitations on the Pass-Through Entity Payment (PTE) due to the above-mentioned SALT increase. However, because the tax proposal is a long way from becoming law, with many twists, turns and changes to come, we believe it is prudent to assume the PTE will still be in play for 2025.

As we have discussed before, several states, including California, enacted legislation that allows S-Corporations and partnerships to pay state income taxes at the business level via their Pass-Through Entity (PTE) tax return - Form 1120S or Form 1065. This treatment allows state taxes paid at the entity level to be deductible by the shareholder/partner for Federal income tax purposes. This “work-around” was designed to avoid the current $10,000 limitation on the deductibility of state and local taxes for Federal tax purposes.

To take advantage of the PTE Credit for 2025, California required a “down-payment” on this credit.

This amount was calculated one of two ways:

1. If you did not take advantage of the PTE credit for the 2024 tax year, then you are required to pay $1,000 to California before June 16, 2025, with the remaining balance of the 2025 credit payable by December 31, 2025;
2. If you did take advantage of the PTE credit for the 2024 tax year, then you are required to pay at least 50% of the 2024 credit before June 16, 2025, with the remaining balance of the 2025 credit payable by December 31, 2025.

To be eligible for the 2025 PTE credit, you have to pay the greater of these two amounts. There are no exceptions to this requirement.

Los Angeles County Wildfire Victims

A reminder, the IRS and California have granted filing and payment postponements to Los Angeles County wildfire victims, if needed.

Taxpayers located in Los Angeles County now have until October 15, 2025, to file and pay taxes that normally would be due between January 7, 2025 and October 15, 2025. This includes, but is not limited to:

- 2024 quarterly estimated income tax payments normally due on January 15, 2025, and 2025 estimated tax payments normally due on April 15, June 16, and September 15, 2025;
- Individual income tax returns and payments normally due on April 15, 2025;
- 2024 contributions to IRAs and health savings accounts for eligible taxpayers;
- Calendar-year partnership and S corporation returns normally due on March 17, 2025;
- Calendar-year corporation and fiduciary returns and payments normally due on April 15, 2025; and
- Calendar-year tax-exempt organization returns normally due on May 15, 2025.

Taxpayers who have an address of record in Los Angeles County will automatically qualify for relief.

<u>Taxpayers who live outside of Los Angeles County but have a tax preparer in Los Angeles County also qualify for this extension.</u>

If you do not want or need this extension, you may still file on time.

Should you have any questions about the above information, or any other tax planning issues, please feel free to reach out by phone or email.

Sincerely,

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