Greenberg Glusker

2025 Tax Update: What You Should Know

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This client alert provides a summary of the major provisions of the new tax bill. To make this extraordinarily complex bill somewhat understandable, we have left off several details and simplified the discussion, so it is critical to consult with a tax advisor based on your particular facts before relying on any description here.

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Summary

1. ESTATE AND GIFT TAX. Commencing in 2026, the estate and gift tax exemption is raised to $15 million for individuals and to $30 million for married couples, indexed for inflation after 2026.

2. INDIVIDUALS

a. Maximum Tax Rate. The current maximum individual tax rate of 37% is now permanent.

b. Standard Deduction. Commencing in 2025, the standard deduction is increased to $15,750 for single filers and to $23,625 for joint returns, adjusted for inflation for taxable years beginning after 2025. For 2025-2028 only, these amounts are increased by $6,000 for taxpayers over 65, but this additional amount is phased out for income over $75,000 for single filers and over $150,000 for joint returns.

c. Exemption for Tips. For 2025-2028, there is an above-the-line deduction for tips if (i) the tips are received in an occupation that customarily received tips prior to 2025, (ii) the tips are voluntary, and (iii) if the recipient is an employee, the employee reports the tips monthly to the employer on Form 4070 and the employer reports the tips on the annual Form W-2. The exemption is capped at $25,000 per year for both single filers and joint returns, and it is phased out for taxpayers with income in excess of $150,000 for single filers and $300,000 for joint returns.

d. Exemption for Overtime Pay. For 2025-2028, there is an above-the-line deduction for overtime pay if (i) the recipient is an employee, (ii) the overtime pay is required by federal law, and (iii) the employer reports the overtime pay on the annual Form W-2. The exemption is capped at $12,500 per year for single filers and $25,000 for joint returns, and it is phased out for taxpayers with income in excess of $150,000 for single filers and $300,000 for joint returns.

e. Section 1202 Stock. Commencing with stock acquired after July 4, 2025, the exclusion of gain under Section 1202 is substantially improved:

i. The exclusion of gain is now phased in by 50% after three years, 75% after four years, and 100% after five years.

ii. The minimum exclusion is raised from $10 million to $15 million, indexed for inflation after 2026.

iii. The permitted gross asset test is raised from $50 million to $75 million, indexed for inflation after 2026.

f. Deduction for Interest to Purchase Vehicle. For 2025-2028, there is an above-the line deduction for up to $10,000 per year of interest on a loan to purchase a vehicle if (i) final assembly of the vehicle occurs in the U.S., (ii) the loan is secured by a first lien on the vehicle, (iii) the vehicle is used for personal use, and (iv) the vehicle weighs less than 14,000 pounds. The deduction is phased out for income over $100,000 for single filers and $200,000 for joint returns.

g. Trump Accounts. For children born from 2025-2028, "Trump Accounts" will automatically be created by the government and funded with $1,000 when a return is filed with the child's Social Security number. After formation, parents can contribute non-deductible payments of up to $5,000 per year (increased by inflation after 2026) to the account, and later distributions allocable to the amount contributed are tax-free to the beneficiary. The income earned in the accounts will be tax free. No distributions are permitted until the child is eighteen years old, and the account must invest in ETF's tracking the U.S. public equity market (like the DOW or S&P 500). Employers can also contribute up to $2,500 per year (increased by inflation after 2027) to these accounts for their employees' children, which will not be treated as taxable income to the employees.

h. Casualty Losses. The limitation on the deduction for personal casualty losses to disasters declared by the President under the Disaster Relief and Emergency Assistance Act, which was set to expire at the end of 2025, is now made permanent. The deduction is expanded to include costs incurred as a result of a "State declared disaster," defined as a natural catastrophe that the state's governor and the Secretary of the Treasury determine causes damage severe enough to warrant the application of these rules.

i. Limit on Charitable Deductions. Commencing in 2026, charitable deductions are reduced by 0.5% of the taxpayer's income, with the disallowed portion carried forward. The income-based percentage limit for charitable contributions of cash by individual taxpayers to public charities is kept at 60%, as the provision reverting it to 50% at the end of 2025 was deleted.

j. Home Acquisition/Improvement Debt. The deduction for interest on home purchase and improvement debt not in excess of $750,000 ($375,000 if married filing separately), which was set to expire at the end of 2025, is now made permanent.

k. Home Equity Debt. The prohibition on the deduction of interest on up to $100,000 of a home equity loan that is not used to purchase or improve the home, which was set to expire at the end of 2025, is now made permanent.

l. State Taxes. For 2025-2029 only, the deduction for state taxes is increased to $20,000 for single filers and $40,000 for joint returns. However, the increased deduction is phased out to a floor of $10,000 by 30% of the taxpayer's income in excess of $250,000 for single filers and $500,000 for joint returns. All the dollar amounts above are increased by 1% per year after 2025. State workarounds with pass-through entity taxes are still allowed, and California just extended this approach through 2030. State taxes are now subject to an additional limit applicable to all itemized deductions, discussed immediately below.

m. Reduction of Itemized Deductions. Commencing in 2026, for taxpayers in the 37% tax bracket (i) itemized deductions other than state taxes save only 35% instead of 37% of taxes and (ii) state taxes save only 32% instead of 37% of taxes.

n. Elimination of Miscellaneous Itemized Deductions. The prohibition on the deduction of miscellaneous itemized deductions, which was set to expire at the end of 2025, is now made permanent. This basically applies to (i) unreimbursed employment expenses of employees, (ii) investment-related expenses, and (iii) tax preparation costs.

o. Section 529 Plans. Section 529 plans, which used to be limited to college expenses, are now expanded to include all education expenses, including elementary, secondary, home schooling, and occupational training, commencing July 4, 2025.

p. Moving Expenses. The prohibition on the deduction for business-related moving expenses, and the taxation of employer reimbursement for such expenses, which was set to expire at the end of 2025, is now made permanent.

q. AMT Exemption Amount. The current alternative minimum tax exemption amounts that were set to expire at the end of 2025 are now made permanent.

3. SECTION 199A. The deduction permitted for individual taxpayers, trusts, and estates under Section 199A for up to 20% of "Qualified Business Income" is now made permanent.

4. AGRICULTURAL LAND LOANS. Banks and insurance companies get to exclude 25% of the interest they receive on loans if (a) the loan is a new loan (and not a refinancing) made after July 4, 2025, and (b) the loan is secured by agricultural real property in the U.S.

5. TAX ON PRIVATE COLLEGES. Commencing in 2026, there is a new tax imposed on the investment income (including royalties attributable to intangible property developed with federal funding) of private colleges that have (a) more than 3,000 students and (b) a per-student endowment fund in excess of $500,000. The tax rate ranges from

1.4% to 8% depending on how large the college's endowment fund is per student.

6. CHARITABLE DEDUCTIONS FOR C CORPORATIONS. Commencing in 2026, charitable deductions of C corporations are reduced by 1% of their net income, with no carryforward. The prior limit of 10% of income continues to apply, subject to carryforward of the excess if that limit is exceeded.

7. GENERAL PROVISIONS FOR ALL TAXPAYERS

a. Opportunity Zones. There is a substantial expansion and extension of the benefits of Opportunity Zones on a permanent basis, which generally become effective in 2027:

i. There are tightened rules for designating Zones, and the Zones will be redrawn every ten years, starting on July 1, 2026. The redrawn Zones will become effective at the start of the following calendar year (e.g., in 2027 for the Zones designated on July 1, 2026), and Qualified Opportunity Funds ("QOFs") must acquire (or substantially improve) property in the new Zones after 2026.

ii. The new rules only apply to investments in QOFs made after 2027. However, since an investment in a QOF can be made within 180 days of the date of gain recognition, and the date of gain recognition itself is deferred to the end of the year for pass-through entities, investors will be able to use the new rules even for gain recognized in 2026 if they invest in a QOF in 2027 within the rollover time limit.

iii. The tests for qualifying as a QOF must be met with property acquired or substantially improved after 2026. It will not work for investors to invest in 2027 in a QOF holding property under the prior rules even if the property remains in a Zone after the redrawing on July 1, 2026.

iv. There is no longer an outside specific calendar date by which deferred gain must be recognized. In all cases, the deferred gain will be deferred and recognized five years from the date of investment in a QOF unless an "inclusion event" occurs earlier.

v. The prior rule continues to apply that provides for a reduction of the deferred gain by 10% if the investment in the QOF is held for five years. However, the prior reduction of deferred gain by 15% after seven years no longer applies, since the deferred gain is now recognized after five years.

vi. If at least 90% of the QOF's assets is in Zones in rural areas (a "Qualified Rural Opportunity Fund"), the investor can exclude 30% of the deferred gain if the investment in the QOF is held for five years.

vii. For investments held at least ten years, *there is no tax on any later sale of the interest in the QOF as long as it is sold within thirty years of the date of investment in the QOF.* If the investment in the QOF is held for more than thirty years, the basis of the investment in the QOF is locked in at the market value of the interest in the QOF at the end of thirty years.

viii. For existing structures in rural areas, the "substantial improvement" test is relaxed, requiring only 50% of the adjusted basis (instead of 100%) to be invested. This rule is effective for property acquired by QOFs after July 4, 2025.

ix. Commencing in 2025, QOFs are now subject to extensive additional reporting requirements, both to the IRS (to be filed electronically) and to investors that sell an interest in the QOF, with substantial penalties for failure to file the required reports.

b. <u>100% Deduction under Section 168(k)</u>. Under revised Section 168(k), all taxpayers can deduct 100% of the cost (with no limit) of almost all new or used “Qualified Property” (which includes almost all personal tangible property used in a trade or business and films shot in the U.S.) acquired by a contract entered into after January 19, 2025, when the property is placed in service.

c. <u>100% Deduction for Certain Buildings</u>. There is now a 100% deduction for the cost of purchasing or constructing buildings in the United States when they are placed in service if the following requirements are met: (i) the purchase must occur, or construction must commence, after January 19, 2025, and before 2029, (ii) the building must be placed in service after July 4, 2025 and before 2031, (iii) the building must be used for the manufacturing, production, or refining of tangible personal property (“Qualified Use”), with recapture if the building ceases to be used for a Qualified Use within ten years of being placed in service, and (iv) either the original use of the building must commence with the taxpayer or the building was not used for a Qualified Use from January 1, 2020, through May 12, 2025.

d. <u>Section 179</u>. Commencing in 2025, the maximum amount a taxpayer may expense under Section 179 is increased to $2.5 million, and the phase-out threshold is raised to $4 million. These amounts are indexed for inflation for taxable years beginning after 2025. Given the 100% deduction under Section 168(k) (discussed above), Section 179 is primarily relevant for tangible personal property that is affixed to buildings.

e. <u>Section 181</u>. Section 181 (which permits the deduction of up to $15 million of producing a film in the U.S.) is amended effective in 2025 to include sound recordings produced in the U.S., but limited to $150,000 per year. However, all of Section 181 is currently scheduled to expire at the end of 2025, so this may be a short-lived provision.

f. <u>Sale of Farmland</u>. If a taxpayer sells farmland to a farmer and the land is subject to a legally enforceable restriction prohibiting its use for anything other than farming for at least ten years after the sale, the taxpayer can elect to pay any tax on the sale in four annual installments without interest, even if the sale proceeds are paid on closing.

g. Reporting Trade or Business Payments. For payments made after 2025, the requirement to report payments made in connection with a trade or business is raised from $600 to $2,000, indexed for inflation after 2026.

h. Electric Vehicle Credit. The electric vehicle credit is terminated for purchases after September 30, 2025.

i. Clean Energy Credits. There is rapid phase-out or termination of all clean energy credits.

j. Excise Tax on Foreign Payments. Commencing in 2026, there is a new 1% excise tax imposed on transfers of funds by cash, money order, or check from the U.S. to outside the U.S., other than payments by a bank or by credit card. Both the person originating the transfer and the entity making the transfer are liable for the tax.

k. Meals for Employees. The limitation on employers deducting only 50% of the cost of providing meals to employees for the convenience of the employer is now made permanent. However, the law is clarified to state that the limit does not apply to (i) recreational, social, or similar activities primarily for the benefit of employees (e.g., company picnics, holiday parties) and (ii) expenses for food or beverages that are excludable from the gross income of the recipient as de minimis fringe benefits (e.g., occasional meals provided at the office that are considered too small to be practical to account for).

l. Research Expenditures. Research or experimental expenditures incurred in the U.S. after 2024 are immediately deductible, and any capitalized expenses incurred from 2022-2024 may also be deducted in 2025. This does not include expenditures for land or for depreciable property used in connection with research or experimentation, but most depreciable property will qualify for immediate deduction under Section 168(k). The deduction is reduced by any research tax credit taken for the expenditures.

m. Excess Business Losses. The limit on the deduction of excess net business losses of a taxpayer other than a C corporation against non-business income, which was originally scheduled to expire at the end of 2028, has been made permanent. The current limit on the deduction of such losses is $313,000 for single filers and $626,000 for joint returns, and these amounts are indexed for inflation after 2025.

n. Business Interest. Commencing in 2025, the limitation on the deduction of business interest in excess of the sum of (i) business interest income plus (ii) 30% of “adjusted business taxable income” is now calculated by adding back depreciation, amortization, and depletion to “adjusted business taxable income,” resulting in higher permitted interest deductions, and most capitalized interest is no longer subject to this limitation. However, starting in 2026, Subpart F income is not included in calculating “adjusted business taxable income.”

8. FOREIGN PROVISIONS

a. Foreign Derived Intangible Income. The tax rate to C corporations on "foreign-derived intangible income" (which is now renamed "foreign-derived deduction eligible income") will increase from the current 13.125% to 14% after 2025.

b. Global Intangible Low-Taxed Income. The tax rate to C corporations on "global intangible low-taxed income" (which is now renamed "net CFC nested income") of their controlled foreign corporations will increase from the current 10.5% to 12.6% after 2025.

c. Source of Income for Inventory. Effective for taxable years beginning after 2025, net income from the sale of inventory produced in the U.S. and sold through a branch in a foreign country is treated as 50% foreign source.

d. Subpart F Attribution. Effective for taxable years beginning after 2025, stock of a foreign corporation owned by a foreign person is no longer attributed to a related U.S. person for purposes of determining whether the related U.S. person is a U.S. shareholder of the foreign corporation. However, stock of a foreign subsidiary owned by a foreign parent corporation is attributed to the foreign parent's U.S. subsidiary for purposes of determining whether the U.S. subsidiary is a U.S. shareholder of the foreign subsidiary and, therefore, whether the foreign corporation is a controlled foreign corporation ("CFC") of the U.S. subsidiary. The pro rata share of the CFC's Subpart F income that the U.S. subsidiary is required to include in gross income, however, continues to be determined based on the U.S. subsidiary's ownership of the CFC, without application of the new downward attribution rule.

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