2025 National Income Tax Workbook

Chapter 9: Business Tax Issues PART I

PP 309 - 339

Land Grant University Tax Education Foundation

1

Table of Contents

P 309

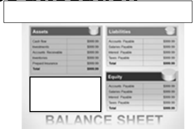
NEW LAW

2

2

Issue #1 – Purchase Price allocation

P 311



See Fig 9.1

1. Seller - stock ⟷ Buyer - assets Winner
2. Seller - character Capital gain ⟷ Buyer – basis Rapid depreciation
3. Both? - Installment sale

3

Considerations P 311

Considerations
- Non-tax
- Tax

Important, but not discussed.
Liabilities?
Estate Planning?

Figure 9.2
Page 312

4

Section 179 Deduction P 312

Buyer would like to allocate as much as possible to qualified Section 179 property

Qualified property (next!)
Acquired for use in an active trade or business
Acquired by purchase
Not acquired from a related party

5

179 – Qualified Property P 312

- Tangible personal property
- Other tangible property – used in manufacturing, research facility, bulk storage
- Single purpose agricultural structures
- Storage facilities
- Off-shelf computer software
- Qualified 179 <u>real</u> property?

6

179 – Qualified Real Property

P 313

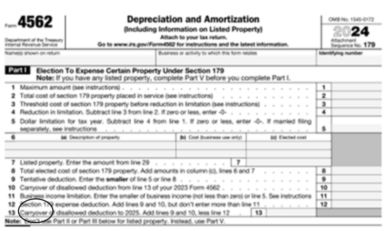
NEW - 2018

Improvements to Non-residential real property
- Roofs
- Heating, ventilation, air conditioning, fire protection & alarm
- Security systems

7

Section 179 election

P 313


Form 4562
Depreciation and Amortization
(Including Information on Listed Property)
Attach to your tax return.
Go to www.irs.gov/Form4562 for instructions and the latest information.
2024
Part I Election To Expense Certain Property Under Section 179
Note: If you have any listed property, complete Part V before you complete Part I.
1 Maximum amount (see instructions)
2 Total cost of section 179 property placed in service (see instructions)
3 Threshold cost of section 179 property before reduction in limitation (see instructions)
4 Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-
5 Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions
6 (a) Description of property (b) Cost (business use only) (c) Elected cost
7 Listed property. Enter the amount from line 29
8 Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7
9 Tentative deduction. Enter the smaller of line 5 or line 8
10 Carryover of disallowed deduction from line 13 of your 2023 Form 4562
11 Business income limitation. Enter the smaller of business income (not less than zero) or line 5. See instructions
12 Section 179 expense deduction. Add lines 9 and 10, but don't enter more than line 11
13 Carryover of disallowed deduction to 2025. Add lines 9 and 10, less line 12
Note: Don't use Part II or Part III below for listed property. Instead, use Part V.

Can't create a loss!

Can carryover excess

X

8

Bonus Depreciation - OBBB 70301

P 567

Placed in service

40% 1/19

100% 1/20

9

Bonus Depreciation – Qualified Property P 313

Depreciable Property having a useful life of 20 years or less

Computer software available to the general public

Qualified improvement property

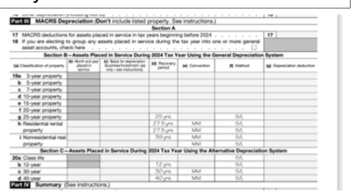
10

Bonus Depreciation – Electing Out P 313

Automatic, unless elect out

Election applies to all property in the same class

Elect out by claiming depreciation on 4562



11

Bonus Depreciation – Reduced rates Election P 567

From Chapter 14 – New Legislation – page 567

Transition rule – for the first tax year ending after 1/19/25, taxpayers can elect a reduced bonus depreciation rate of 40% (rate in affect between 1/1/25 and 1/19/25)

X

12

Allocation Methods

P 314

Written Agreement

- Buyer and Seller have a written agreement allocating the purchase price.
- Binding, unless IRS determines allocation not appropriate.

Use Form - 8594

Residual Method

- Constitutes a trade or business.
- Buyer's basis in the assets determined solely by consideration paid for the assets.
- Assets assigned by class, up to FMV, except Class VII.

13

Residual Method

P 314

Class I – Cash
Class II – Securities, Stock
Class III – Debt, A/R
Class IV – Inventory
Class V – All tangible assets not in any other class

Most identifiable ↓ plug

Class VI – Intangibles, except goodwill and going concern
Class VII – Goodwill and Going Concern

Most identifiable ↓ plug

14

Case Study

P 315- 317

Amal — 100% — Woods Bay Tax, Inc 1120S — Buyer

Not a Stock Sale

Agreement – Form 8594 - page 316

Assets:	Basis	FMV	Gain	Character	Form
A/R -	0	20,000	20,000	Ordinary	4797
Equipment –	41,233	65,000	23,767	Ordinary	4797
Goodwill -	0	143,000	143,000	Capital	8949
	41,233	228,000	186,767		

X

15

Issue #2 - correcting depreciation

p. 318

A mistake made in depreciation? What are you going to do?

Do nothing	Amend returns	Correct in current and future years	Change of accounting

16

Correcting depreciation

p. 318

2025
Proper depreciation

Prior years

Mathematical error
Incorrect method
Incorrect period
Incorrect convention
Change in use

Too little? Can't catchup

Too much? Can't add back to basis (even if no tax benefit)

(Can amend returns)

Unless part of a change of accounting!

17

Correcting depreciation

p. 318

Not Accounting Method Changes	Accounting Method Changes
	

18

<u>Not</u> Accounting method changes

p. 318

- Change in useful life
- Change in facts
- Change use of an asset
  - Examples coming
- Placed in service date
- Late depreciation election
- Mathematical or posting errors

19

Change in use

p. 319

Year 1 → Changes in how property is **used** (Facts changed) → Year 2, etc…

Calculate MACRS <u>properly</u> based on facts at the time

- Different recovery period
- Different depreciation method

20

Change in use

p. 319

Year 1 | Year 2 – year of change

Facts change

Treat as though the change occurred on first day of tax year.

If new use allows for **shorter life or more accelerated depreciation**, taxpayer has the option:

1. Start using the new method in year of change
2. Continue as if change has not occurred

21

Change in use

p. 319

Year 1 | Year 2 – year of change

Facts change

Treat as though the change occurred on first day of tax year.

If new use results in **longer recovery period or less accelerated depreciation**, the taxpayer **must** use the new method.

22

Example 9.1 Change in Use

P 319

2020 —— 2024 2025

100,000 office – 7 year property Claimed depr of 77,690.	Basis 22,310	manufacturing 5 year property

Options:

1. calculate depreciation as though equipment placed in service in 2025 assuming used in manufacturing
2. Disregard change

23

Property converted from Personal to Business

P 319 - 320

- Placed in service on date of conversion
- Use applicable method, recovery period and convention (may qualify for bonus)
- Basis for depreciation is lesser of FMV or adjusted depreciable basis.

24

Example 9.2 Conversion to Rental P 320

1995 Principal Residence | 2025 Rental Property

Basis 150,000
FMV 130,000
Lesser 130,000
S/L 27.5 years

25

Convert from business to personal use P 320

Business use | Personal Use

Prorate Full year depreciation X $\frac{\text{Months in service}}{12}$

No gain or loss (or recapture) at time of conversion, but recapture applies at later disposition.

26

Correcting the change is use / placed in service P 320

Change in Use	≠	Change in Method of Accounting	Make change on 4562 in year of change
Change Placed in service date	≠	Change in Method of Accounting	Correct by amending return

27

Example 9.3

P 321

12/24 — 1/25 — 2026

- 12/24: Placed in service
- 1/25: Received invoice. Started depreciating
- OOPS!
- 2026: Realized mistake

OR!

Amend 2024

No 3115, no 481(a)

28

Example 9.3 – alternate approach

P 321

12/24 — 1/25 — 2026

- 12/24: Placed in service
- 1/25: Received invoice. Started depreciating
- 2026: Realized mistake

If taxpayer initiated, can correct the placed in service date by adjustments in the current and subsequent tax years.

29

Accounting method changes

P 321

2 ways to adopt an accounting method for depreciation:

~~1040X~~

1. Use a permissible method the first tax year the asset is placed in service
2. Use the same impermissible method for 2 or more consecutive tax years. (only 1 year, can amend)

30

Example 9.4

P 321

10/25 — 4/15/26 — Discovered error

7 year property

incorrectly filed 2025 using 5 year life

1. Not filed 2026, amend 2025 Not 2 years
2. Filed 2026, must use 3115

31

Changes that require consent

P 322

Impermissible (2 years)	Permissible
Depreciable (vice versa)	Nondepreciable
Depreciate (vice versa)	Expense
Claim add'l first year (for asset that does not qualify)	not claiming

Claim additional first year depreciation

Method, recovery period, convention

32

Two types of Accounting method changes

P 322

Automatic Consent

Advanced Consent required

33

Changes that require consent - automatic P 322

- One of the approved method changes found in the instructions to the 3115

List of DCNs	
No.	Change
262	**Changes within a section 471(c) inventory method**—for a qualifying applicant with average annual gross receipts of $25 million or less (adjusted for inflation) making changes **within** a section 471(c) inventory method. See section 22.19 of Rev. Proc. 2022-14. **Note.** This change does not receive audit protection. Additionally, reduced Form 3115 filing requirements apply to this change.
263	**Change from a small business taxpayer section 471(c) inventory method to an inventory method under section 471(a)**—for a qualifying applicant with average annual gross receipts of $25 million or less (adjusted for inflation) changing **from** using a small business taxpayer inventory method under section 471(c) inventory method **to** an inventory method under section 471(a). See section 22.20 of Rev. Proc. 2022-14.
264	**Certain late elections under sections 168(j)(3), 168(l)(3)(D), and 181(a)(1)**—for an applicant making a late election (1) not to apply section 168(j) for qualified Indian reservation property placed in service after December 31, 2017, for its 2018 or 2019 tax year; (2) not to apply section 168(l) for qualified second generation biofuel plant property placed in service after December 31, 2017, for its 2018 or 2019 tax year; or (3) to apply section 181 to the production costs for its 2018 or 2019 tax year of any qualified film, television, or live theatrical production, commenced by the taxpayer after December 31, 2017. See section 6.23 of Rev. Proc. 2022-14.
265	**Research and experimental expenditures (section 174)—to** charging specified research or experimental expenditures to capital account and amortizing such expenditures over a 5- or 15-year period, as applicable. See section 7.02 of Rev. Proc. 2022-14. **Note.** For specified research or experimental expenditures paid or incurred in the first tax year beginning after December 31, 2021, this change is implemented on a cut-off basis. For specified research or experimental expenditures paid or incurred in any year of change later than the first tax year beginning after December 31, 2021, this change is implemented with a modified section 481(a) adjustment. This change applies to amounts paid or incurred in tax years beginning after December 31, 2021. For amounts paid or incurred in tax years beginning before January 1, 2022, see DCN 17.

- Prepare 3115 in duplicate
  1. attach to return
  2. send to National Office
- No user fee

34

Changes that require consent – advanced consent P 322

Not an automatic change, basically need to get a letter ruling

File 3115:
- Anytime during tax year, but earlier the better
- User fee:
  - Gross income < 400,000 3,450
  - Gross income > 400,000 < 10,000,000 9,775
  - Gross income > 10,000,000 13,225

35

481(a) unfavorable (negative) P 323

Prior Year | Year of change | 1 | 2 | 3 | 4

Depreciation claimed xx,xxx
Proper depreciation <u>(xx,xxx)</u>
Claimed to much x,xxx ¼ ¼ ¼ ¼

4 year spread

Can elect to take all in one year, if less than 50,000 (check box on 3115)
Under audit – 2 year spread

36

481(a) favorable (positive)

P 323

Prior Year | Year of change | 1 | 2 | 3 | 4

Depreciation claimed xx,xxx
Proper depreciation (xx,xxx)
Didn't claim enough (x,xxx)

100%
All in year of change

37

Cutoff method

P 324

One permissible method to another permissible method

Year of change

Assets adjusted basis recovered using new method →

38

Example 9.6 – Bill Dawson

p. 324 - 329

7/15/15 — Purchased skid loader 65,000

← Failed to claim depreciation, but allowed or allowable - fully depreciation →

2025 — Sold Skid loader 28,000

28,000 gain taxable as ordinary income on 4797

39

Example 9.6 – Bill Dawson

p. 324 - 329

Bill can claim a 65,000 481(a) adjustment in 2025

Let's walk through the 3115:
Pages 325 - 329

40

Practitioner Note - Bonus Depreciation

p. 330

- Bonus depreciation is mandatory, unless the taxpayer elects out.
- Elect out: Class by class + Timely filed return

- What if the taxpayer does not elect out and fails to claim bonus depreciation?
- Taxpayer has a depreciation error that must be corrected.
- Only one year filed, taxpayer can file an amended return
  Otherwise, file 3115 – automatic consent procedures.

X

41

Issue 3 - Start up and 0rganizational Expenses

p. 331

Start –Up New Business	Purchase Existing Business	Expanding Existing Business	Organizational Costs
195	195	195	248, but amortization similar to 195
or	or	or	or
262 personal	263 capital	162 Business exp	263 capital

42

Issue 3 - Start up Expenses

p. 331

Investigation period | First Tax year | 180 mo

- Investigating new businesses
- Creating a business
- Activities that are expected to become a business

Under 50,000: 5,000	amortize rest
Between 50,000 – 55,000: Reduce 5,000 for excess over 50,000	amortize rest
Over 55,000	amortize all

43

Beginning a trade or business

p. 331

Surveys

Advertising

Training employees

Travel

Salaries for executives or consultants

Accumulate

IRC 195

44

Not start up costs

p. 331-332

Interest - IRC 163. Not 195

Taxes - IRC 164. Not 195

Since not yet a trade or business, itemized deduction?

R & E costs - Not 195 (Discussed in New Law Chapter)

45

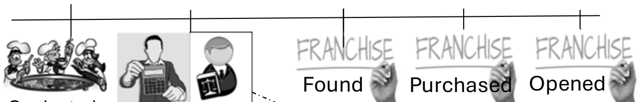
Purchasing (vs starting) a Business p. 332

General Investigatory Expenses	Specific Investigatory Expenses
Amortizable start-up costs 195	Capital expenditures 263
• Conducting industry research • Evaluating financial information • Assessing several potential businesses	• Appraising business assets • Review books and records • Regulatory documents • Due diligence

46

Example 9.7 - Jessica p. 332-333

1/25 6/25 9/3/25 10/10/25 10/15/25



Graduated Culinary School

- Analyze several restaurants
- Research restaurant industry

195 – deduct or amortize

- Lawyer reviewed agreement & Registered LLC
- CPA – set up books and payroll

263 – capitalize

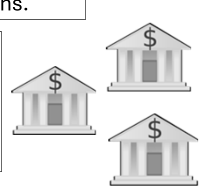
47

Expanding a business – *North Carolina Nat'l Bank* p. 333

Expanding a business is generally deductible under 162. Not subject to 195 limitations.

Original location

- Marketing, feasibility studies
- Staff – planning and implementing
- Regulatory permission



New Territories

Court agreed IRC 162 expenses

48

Expanding a business - Example 9.8

p. 333

Whitewater rafting

Ocoee Tennessee

Research acquiring another privately owned rafting business in new location

Similar

Pigeon River Tennessee

Investigatory expenses are not startup expenditures.
Marketing study is a 162 business expense.

49

Making the 195 election

p. 333

Deemed to have made the election

Forego the deemed election by affirmatively electing to capitalize start up expenses

- Applies to all start up expenses
- Irrevocable, unless change of accounting

50

Examples 9.10 and 9.11

p. 334

9.10 – Taxpayer accidentally deducted 10,000 start up expenses as 162 business expenses. This is an impermissible method and must change it's method of accounting.

9.11 – Taxpayer deducted and amortized start up expenses in 2023. In 2025 it was determined that Everest did not begin business until 2024. This is an impermissible method and must change it's method of accounting.

51

Examples 9.12, 9.13, 9.14 How to Amortize p. 335

	Start up Expenses	Date started	Calculations	
9.12	41,000	7/1	first	5,000
			36,000 / 180 mo x 6 =	1,200
				6,200
9.13	54,500	7/1	(54,500 – 50,000 = 4,500)	
			5,000 – 4,500 =	500
			54,000 / 180 x 6 =	1,800
				2,300
9.14	450,000	7/1	450,000 / 180 x 6 =	**15,000**

52

Tax Return Reporting – Example 9.15 p. 335 - 336

Schedule C

Elena Interior Designs

7/1

Start up Expenses

12,560

Sch C line 27b 5,000

4562 amortization
7,560 / 180 mo x 6 = 252

Page 336

53

Beginning of Active Business p. 337

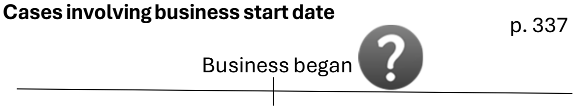
Beginning Date?

1. Start up expenses are incurred before the beginning date
2. If incurred after beginning date, fully deductible under 162
3. No deduction or amortization of start up expenses before the beginning date

54

Cases involving business start date

p. 337



WEBPAGE DEVELOPMENT – opened website to the public

RENTAL PROPERTY – property bought second to last day of tax year, not out for rent until following year.

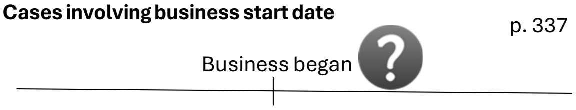
VINEYARD – hired architect, bought tractor, but sold property without planting a grapevine. Did not start business.

Not done yet. 2 more!

55

Cases involving business start date

p. 337



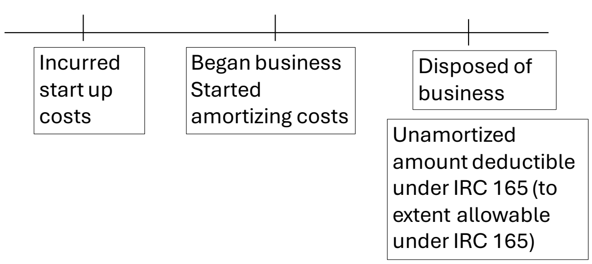
TV STATION – Obtained license and started broadcasting

ENGINEER – name, business cards, stationary, website, computer, desk and office supplies, promoted business. No clients. Did not bid on jobs. No income. Did not start business.

56

Disposition of Business

p. 337



57

Organizational Expenditures

p. 337

Business begins

1120: Expenses incident to the creation of the corporation

1065: Expenses incident to the creation of the partnership

No 162 expenses
Start up expenses

IRC 248 – Similar to start up rules:

Write-off first 5,000 and amortize the rest (reduce dollar for dollar if over 50,000)

On 195

58

Organizational Expenditures - corporations

p. 338

YES:

- Creation of corporation
- Chargeable to capital account
- Would be amortizable, if fixed life
- Incurred before end of first tax year
- Examples:
  - Temporary directors
  - Organizational meetings
  - State incorporation fees
  - Legal services

59

Organizational Expenditures - corporations

p. 338

NO:

- Issuing or selling stock:
  - Commissions
  - Professional Fees
  - Printing Costs
  - Costs to transfer assets to corp
  - Reorganization of a corporation

XX

60

Election to amortize

p. 338

- Similar to electing to amortize startup expenses
- On timely filed return. Made at entity level
- When corporation begins business
  (not when corporation comes into existence)

NO

YES

61

Costs of Organizing a Partnership

p. 338

YES:
- Creation of Partnership
- Chargeable to capital account
- Would be amortizable, if fixed life
- Incurred by the due date of the partnership return for the first tax year
- Expected to benefit partnership throughout its entire life

62

Costs of Organizing a Partnership

p. 339

Examples
- Acquiring assets, transferring assets
- Admitting, removing partners
- Cost of making contracts
- Syndication fees, legal fees, printing costs

63

Making the election p. 339

- Entity level
- Shareholder or partner cannot make an election to amortize organizational costs
- Cannot amortize costs to investigate an interest in an existing partnership. (may qualify as a startup cost)

XX

64

Issue #4 – Equity based compensation for small businesses p. 340

Ownership of company stock	Nonstatutory stock options	Phantom Stock
Taxable if present, unrestricted transfer. Election available.	Nontaxable when granted, unless readily ascertainable FMV. Taxable when exercised.	Deferred compensation based on reference to hypothetical phantom shares

65

Unrestricted ownership of stock p. 340

Any compensation paid to an employee, director, or independent contractor that is based on the value of specific stock (generally stock of employer)

in

66

Unrestricted ownership of stock

p. 340

Unrestricted share of ownership ⟷ Services

Taxable income = FMV, less any amounts paid

IRC 83

Compensation deduction

67

Example 9.16

p. 340

2/1/25 Regina receives

100 shares of employer's stock ⟷ Soley for Services

Regina

Taxable income =
100 x 30.00 FMV = **3,000**
?

IRC 83

3,000 compensation deduction

68

Cross –reference : Profits interest in partnership

p. 340

Rev Proc 93-27

Vested Profits interest ⟷ Services in partner capacity

(Not a capital interest)

Not a taxable event for the partner or partnership

69

Unrestricted ownership of stock

p. 341

Key words to be defined:

- ☆ Transfer of Interest
- ☆ Substantially vested
- ☆ Transferable
- ☆ Risk of forfeiture

70

Transfer of Interest – per IRC 83(a)

p. 341

"Actual transfer of property" →

Before treated as compensation

Factors defining "actual":

- Not returned if certain events happen
- Voting and dividend rights
- No restrictions on stock. Ie: sale
- Receive liquidating distributions
- Right to gain or loss based on stock's value

71

Example 9.17

p. 341

Highline Restaurant Corp → Lawrence

1/3/25

100 shares of company stock

Not transferable

Per IRC 83, no transfer

Sole restriction: If employment terminated, must sell stock back for book value date of termination over book value on 1/3/25.

72

Substantially vested: Transferable/ Risk of forfeiture

p. 341

Value of stock →

Substantially vested:
1. Transferable
2. Not subject to risk of forfeiture

1. Transferable: can sell, assign, pledge interest

73

Substantially vested/ Transferable/ Risk of forfeiture

p. 342

Value of stock →

Substantially vested:
1. Transferable
2. Not subject to risk of forfeiture

2. Substantial risk of forfeiture: if rights in property are conditioned, directly or indirectly, upon future performance (or refraining from performance) of substantial services of any person or upon the occurrence of a condition.....

74

Substantially vested/ Transferable/ Risk of forfeiture

p. 342

Value of stock →

Substantially vested:
1. Transferable
2. Not subject to risk of forfeiture

NOT Substantial risk of forfeiture: if at the time of transfer the facts and circumstances demonstrate that the forfeiture condition is unlikely to be enforced. Not substantial if the employer is required to pay FMV for the property, if there is a forfeiture.

75

Example 9.18

p. 342

Alysha might quit or get fired

Alysha hired

Employment contract awards 200 shares in the company after 5 years.

5 years

Alysha's right to the shares is subject to a substantial risk of forfeiture until her 5 year anniversary.

76

RECAP

p. 342

Unrestricted ownership of stock?

Must be a "*Transfer of Interest*"

Must be "*Substantially vested*"

Must be "*Transferable*"
and
Without "*Risk of forfeiture*"

Decision made at employer level, not employee level

77

Election to include in income – employee level

p. 342

An employee who receives substantially nonvested property in connection with performance of services can elect to include the value of the restricted stock in gross income in the year of transfer.
Income: FMV over amount paid.

FMV going up or down?

78

Election to include in income

p. 342

Make election	Don't make election
WIN: Fair Market Value of Stock goes up	WIN: Fair Market Value of Stock goes down
LOSE: Fair Market Value of Stock goes down	LOSE: Fair Market Value of Stock goes up
No deduction if subsequently forfeited	

79

Capital Gain Treatment

p. 342

Employee who elects earlier recognition starts the holding period for the property. Subsequent appreciation is generally treated as capital gain income.

2025

Section 1(j)(5)(B)—Capital Gains Rates (Noncorporate Taxpayers)

Filing Status	Maximum 0% Rate Amount	Maximum 15% Rate Amount
MFJ and surviving spouse	$96,700	$600,050
MFS	$48,350	$300,000
HoH	$64,750	$566,700
All other individuals	$48,350	$533,400
Estate or trust	$3,250	$15,900

80

Example 9.20

p. 343

1/1/20

Employer granted Brian 1,000 shares. Forfeited if Brian left company for 5 years.

Brian made election
1,000 x 15 = 15,000 income

1/1/25

Forfeiture period ended. Stock now worth 34/share

Brian recognizes capital gain income:
1,000 x 34 = 34,000
Less (15,000)
19,000

81

Making the election

New!
Form 15620

Prior, IRS just suggested language to use

p. 343

Cannot be revoked

Where to File
Submit this completed and signed Form 15620 to the IRS **via mail** with the IRS office with which the person who performs the services files a federal income tax return.

Additional Copies
The person who performs the services is also required to submit a copy of the completed and signed Form 15620 to the person for whom the services are performed. In addition, if the person who performs the services and the transferee of the property are not the same person, the person who performs the services is also required to submit a copy of the completed and signed Form 15620 to the transferee of the property.

X

82

Type 2 - Nonstatutory and statutory Stock Options

p. 343

Nonstatutory

- Generally, no tax consequences for employer or employee when granted
- But, if option has readily ascertainable FMV, compensation recognized.
- IE: actively traded on established market, otherwise measured with reasonable accuracy

Statutory (practitioner note)

- Statutory – also called "qualified"
- ISO- Incentive stock options
- ESPP- employee stock purchase plan
- Different rules apply

83

Exercise of the option (nonstatutory)

p. 344

Ordinary income (including employment taxes) on the exercise of nonstatutory stock options

Option is exercised when the option grantee purchases stock at the strike price established in the option grant.

Corporation gets corresponding deduction.

84

Section 83(i) Election p. 344

PROBLEMS | SOLUTION | 5 years

Exercise stock option	PROBLEMS	SOLUTION
Exercise stock option	1. Transferability may be restricted 2. Employee may not have cash to pay tax	Elect to defer paying tax Earliest of: 1. Year become transferable 2. Becomes excluded employee 3. Stock becomes tradable 4. 5 years 5. Revokes election

NOTE: employer gets deduction equal to amount included in income

85

Section 83(i) Election p. 344

- Limited to smaller, privately held corporations
- Highly compensated officers and those owning over 1% of stock excluded.
- How to make the election:
  Notify IRS and employer within 30 days
  (similar to an 83(b) election)

X

86

Type 3 - Phantom Stock p. 345

Phantom stock plan is nonqualified plan deferred compensation arrangement

Deferred amounts are determined by reference to a hypothetical phantom shares of employer's stock.

Employer never issues the actual shares to the employee. May get:
1. growth in value
2. Receive entire value of stock, plus dividends

87

Phantom Stock

p. 345

Why use Phantom Stock?

Employer wants employee to share in the increase in value of corporation, but does not want to give employee voting rights.

Also, may be used by an S corporation and the employee is an ineligible shareholder.

88

Phantom Stock

p. 345

How is phantom stock taxed?

Excluded from income at the time of grant.

Included in income when "received".
- At the time credited to the employee's account
- Vested

89

Phantom Stock

p. 345

FICA

FMV of phantom stock is included in wages at the time it is credited to employee's account (when it is vested)

Appreciation after that is not FICA wages.

Federal Withholding

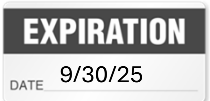
FMV of phantom stock is included in wages at the time it is credited to employee's account (when it is vested)

Appreciation after that is income subject to withholding.

X

90

Issue #5 Commercial Clean Vehicles p. 346



The credit will not be allowed for any vehicle **acquired** after 9/30/25

Acquired means having a written binding contract in place and a payment made before 9/30/25.

Vehicle does not have to be placed in service by 9/30/25. Credit claimed when placed in service.

91

Issue #5 Commercial Clean Vehicles p. 346

EXPIRED!!

Still important to know for 2025 (and maybe 2026?)

Then forget!

92

Issue #5 Commercial Clean Vehicles p. 346

EV vehicle credits

IRC 30D – new clean vehicle credit

- Can be <100% business use
- MSRP limits
- MAGI limits

IRC 25E - previously owned clean vehicle credit

- Smaller credit

IRC 45W – Commercial Clean Vehicle Credit

(must be 100% business use and new)

93

Qualified Commercial Clean Vehicles p. 346

- Qualified manufacturer
- Acquired for use in trade or business, not sale
- Use on public roads, not rails. Or mobile machinery
- Propelled to a significant extent by an electric motor that can be recharged by external source of electricity
- For use primarily in the U.S.
- No 30D new clean vehicle credit claimed

94

Qualified Commercial Clean Vehicles p. 346

- Per vehicle - lesser of:
  1. 15% of vehicles basis (30% if no internal combustion engine) - pretty easy
  2. Incremental cost of the vehicle - What? Something NEW

  Maximum 7,500 < 14,000 pounds
  40,000 > 14,000 pounds

95

Qualified Commercial Clean Vehicles p. 346

Incremental cost of the vehicle

Purchase price

Excess cost

Comparable vehicle powered by gas or diesel

Seems like that would be hard to determine!

BUT ← Safe harbors

96

Incremental cost for tax year 2024 p. 347

Notice 2024-5

The guidance informs taxpayers that the Department of the Treasury and the Internal Revenue Service have reviewed the incremental cost for all street vehicles in calendar year 2024. The analysis shows that the incremental cost of all street vehicles that have a gross vehicle weight rating ***of less than 14,000 pounds will be greater than $7,500 in calendar year 2024.***

Accordingly, the incremental cost will not limit the available credit amount for street vehicles that have a gross vehicle weight rating of less than 14,000 pounds and are placed in service in calendar year 2024

97

Incremental cost for tax year 2025 p. 348-349

Notice 2025-9

2 safe harbors

1. Incremental costs across several classes of clean vehicles. See P. 348 for ES-2 table. Notice all over 7,500 except 2 classes of plug-in hybrids.
2. Retail Price Equivalent
   See P. 349 for table. Do the math based on the purchase price and class of vehicle to prove the incremental cost is over 7,500.

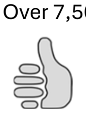
98

Retail Price Equivalent calculation p. 348-349

If you paid 25,000 for a midsize car:

Amount paid for car		25,000	
Retail price equivalent factor	div	1.5	8,334
Cost of midsize car – non-EV		16,666	

Over 7,500



99

Leased vehicles p. 349

A taxpayer can claim the credit on a vehicle purchased for lease in the taxpayer's trade or business

Not subject to the normal clean vehicle credits limits on vehicle price, buyer income, battery source and assembly location.

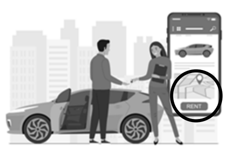
Credit goes to the leasing company, not lessee. However, dealership may pass on these savings.

100

Sale vs Lease p. 349

FAQ #6 – factors – more like a sale

- Term covers 80-90% of economic life
- Bargain purchase option that compels lessee to purchase
- Terms that result in lessor transferring ownership risk



Sale?
No credit

101

100% Business Use requirement p. 350

To claim the Commercial Clean vehicle credit, the vehicle must be subject to depreciation.

It must be 100% business use. You can claim a credit under IRC 30D when business use is less than 100%.

Small exception to 100% business use for incidental personal use.

Also, no credit if vehicle is sold in the same year.

102

Recapture

p. 350

Section 30D(f)(5) authorizes IRS to provide for recapture if the property ceases to be eligible property.

Reg 1.45W-4(c)(2)(i) provides for recapture if the taxpayer ceases to use the vehicle for 100% business during the 18 months beginning when the vehicle placed in service.

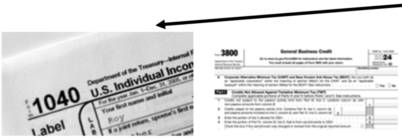
Simply don't claim the credit, or if the taxpayer already claimed the credit, the credit is recaptured.

A subsequent buyer may be able to claim the credit.

103

Claiming the credit – partnerships/S Corp

p. 350



or

If other clean vehicle credits

104

Example 9.21

p. 350

6/1/25
5 Star Realty, LLC
Purchases E-tron
for 50,630

100% business use

5 Star prepares 8936
See pg 351

5 Star puts the 7,500 on Forms K-1

X

105

Form 8936
Schedule A

Vehicle information

KEY!!

100%

<100%

0%

A. Commercial
B. Part business/ Part Personal

Part I **Vehicle Details**

1a Year
b Make
c Model
2 Vehicle identification number (VIN) (see instructions)
3 Enter date vehicle was placed in service (MM/DD/YYYY)
4 Was the vehicle used primarily outside the United States? Answer "No" if it was but an exception applies. See instructions.
☐ **Yes. Stop here.** You can't claim a credit amount for a vehicle used primarily outside the United States.
☐ **No.**
5 Does the VIN entered on line 2 belong to a **new clean vehicle** placed in service during the tax year? See instructions for definitions.
☐ **Yes.** Go to Part II.
☐ **No.** Go to line 6.
6 Does the VIN entered on line 2 belong to a **previously owned clean vehicle** acquired after 2022 and placed in service during the tax year? See instructions for definitions.
☐ **Yes.** Go to Part IV.
☐ **No.** Go to line 7.
7 Does the VIN entered on line 2 belong to a **qualified commercial clean vehicle** acquired after 2022 and placed in service during the tax year? See instructions for definitions. A..
X **Yes.** Go to Part V.
☐ **No. Stop here.** You can't use this schedule to figure a credit amount for a vehicle not described on line 5, 6, or 7.

Part II **Credit Amount for Business/Investment Use Part of New Clean Vehicle**

8 Did you acquire the vehicle for use or to lease to others, and not for resale? Answer "No" if you are leasing the vehicle from another person.
☐ **Yes.**
☐ **No. Stop here.** You can't claim a credit amount for a vehicle you didn't acquire for use or to lease to others, or acquired for resale.
9 Tentative credit amount (see instructions) — 9 — B..
10 Business/investment use percentage (see instructions) — 10 — %
11 Multiply line 9 by line 10. Include this credit amount on line 6 in Part II of Form 8936. If you entered 100% on line 10, stop here. Otherwise, go to Part III below — 11

Part III **Credit Amount for Personal Use Part of New Clean Vehicle**

12 Subtract line 11 from line 9 in Part II. Stop here and include this credit amount on line 9 in Part III of Form 8936 — 12

106

14 in Part IV of Form 8936 — 17

Part V **Credit Amount for Qualified Commercial Clean Vehicle**

18a Is the vehicle of a character subject to the allowance for depreciation? Answer "Yes" if the exception for certain tax-exempt entities discussed in the instructions applies.
☐ **Yes.**
☐ **No. Stop here.** The vehicle is not a qualified commercial clean vehicle unless the exception applies.
b Did you acquire the vehicle for use or to lease to others, and not for resale? Answer "No" if you are leasing the vehicle from another person.
☐ **Yes.**
☐ **No. Stop here.** You can't claim a credit amount for a vehicle you didn't acquire for use or to lease to others, or acquired for resale.
c Is the vehicle also powered by gas or diesel? See instructions.
☐ **Yes.**
☐ **No.**

19	Enter the cost or other basis of the vehicle. See instructions	19	
20	Section 179 expense deduction (see instructions)	20	
21	Subtract line 20 from line 19	21	
22	Multiply line 21 by 15% (0.15) [30% (0.30) if the answer on line 18c above is "No"]	22	
23	Enter the incremental cost of the vehicle. See instructions	23	
24	Enter the smaller of line 22 or line 23	24	
25	**Maximum credit.** Enter $7,500 ($40,000 if the vehicle's gross vehicle weight rating (GVWR) is 14,000 pounds or more)	25	
26	Enter the smaller of line 24 or line 25. Include this credit amount on line 19 in Part V of Form 8936	26	A.

Schedule A (Form 8936) 2023

Subtract sec 179

15% or 30%

Maximum 7,500

To Form 8936 line 19

107

Form 8936

5	Enter the **smaller** of line 2 or line 4	5	
Part II	**Credit for Business/Investment Use Part of New Clean Vehicles** **Note:** Individuals can't claim a credit on line 6 if Part I, line 5, is more than $150,000 ($300,000 if married filing jointly or a qualifying surviving spouse; $225,000 if head of household).		
6	Enter the total credit amount figured in Part II of Schedule(s) A (Form 8936)	6	
7	New clean vehicle credit from partnerships and S corporations (see instructions)	7	
8	**Business/investment use part of credit.** Add lines 6 and 7. Partnerships and S corporations, stop here and report this amount on Schedule K. All others, report this amount on Form 3800, Part III, line 1y	8	
Part III	**Credit for Personal Use Part of New Clean Vehicles** **Note:** You can't claim the Part III credit if Part I, line 5, is more than $150,000 ($300,000 if married filing jointly or a qualifying surviving spouse; $225,000 if head of household).		
9	Enter the total credit amount figured in Part III of Schedule(s) A (Form 8936)	9	
10	Enter the amount from Form 1040, 1040-SR, or 1040-NR, line 18	10	
11	Personal credits from Form 1040, 1040-SR, or 1040-NR (see instructions)	11	
12	Subtract line 11 from line 10. If zero or less, enter -0- and stop here. You can't claim the personal use part of the credit	12	
13	**Personal use part of credit.** Enter the **smaller** of line 9 or line 12 here and on Schedule 3 (Form 1040), line 6f. If line 12 is smaller than line 9, see instructions	13	
Part IV	**Credit for Previously Owned Clean Vehicles** **Note:** You can't claim the Part IV credit if Part I, line 5, is more than $75,000 ($150,000 if married filing jointly or a qualifying surviving spouse; $112,500 if head of household).		
14	Enter the total credit amount figured in Part IV of Schedule(s) A (Form 8936)	14	
15	Enter the amount from Form 1040, 1040-SR, or 1040-NR, line 18	15	
16	Personal credits from Form 1040, 1040-SR, or 1040-NR (see instructions)	16	
17	Subtract line 16 from line 15. If zero or less, enter -0- and stop here. You can't claim the Part IV credit	17	
18	Enter the **smaller** of line 14 or line 17 here and on Schedule 3 (Form 1040), line 6m. If line 17 is smaller than line 14, see instructions	18	
Part V	**Credit for Qualified Commercial Clean Vehicles**		
19	Enter the total credit amount figured in Part V of Schedule(s) A (Form 8936)	19	A..
20	Qualified commercial clean vehicle credit from partnerships and S corporations (see instructions)	20	
21	Add lines 19 and 20. Partnerships and S corporations, stop here and report this amount on Schedule K. All others, report this amount on Form 3800, Part III, line 1aa	21	

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 37751E Form **8936** (2023)

So credit coming from Partnership and S corp K-1s can be added

From Schedule A line 26

To Form 3800

108

Form 3800

Form 3800 (2023) Page 3

Part III **Current Year General Business Credits (GBCs)** (see instructions). If there is more than one credit amount to report on lines 1a through 1zz, line 3, or lines 4a through 4z, enter the number of items you have for that line in column (c) and complete Part V.

	(a) Current year credits from:	(b) Elective payment or transfer registration number	(c) # items	(d) Pass-through or transfer credit entity EIN	(e) Credits from non-passive activities	(f) Credits from passive activities	(g) Credit transfer election amount (enter amounts transferred out as a negative amount)	(h) Gross elective payment election amount	(i) Net elective payment election amount	(j) Combine columns (e), (f), and (g), less column (i)
1a	Form 3468, Part II									
b	Form 7207									
c	Form 6765									
d	Form 3468, Part III									
e	Form 8826									
f	Form 8835, Part II									
g	Form 7210									
h	Form 8820									
i	Form 8874									
j	Form 8881, Part I									
k	Form 8882									
l	Form 8864 (diesel)									
m	Form 8896									
n	Form 8906									
o	Form 3468, Part IV									
p	Form 8908									
q	Reserved (45Z)									
r	Form 8910									
s	Form 8911, Part II									
t	Form 8830									
u	Form 7213, Part II									
v	Form 3468, Part V									
w	Form 8932									
x	Form 8933									
y	Form 8936, Part II									
z	Reserved									
aa	Form 8936, Part V				A..					
bb	[illegible]									
cc	Form 7213, Part I									

109

SCHEDULE 3 (Form 1040)
Department of the Treasury Internal Revenue Service

Additional Credits and Payments
Attach to Form 1040, 1040-SR, or 1040-NR.
Go to www.irs.gov/Form1040 for instructions and the latest information.

OMB No. 1545-0074
2023
Attachment Sequence No. 03

Name(s) shown on Form 1040, 1040-SR, or 1040-NR | Your social security number

Part I **Nonrefundable Credits**

1	Foreign tax credit. Attach Form 1116 if required	1	
2	Credit for child and dependent care expenses from Form 2441, line 11. Attach Form 2441	2	
3	Education credits from Form 8863, line 19	3	
4	Retirement savings contributions credit. Attach Form 8880	4	
5a	Residential clean energy credit from Form 5695, line 15	5a	
b	Energy efficient home improvement credit from Form 5695, line 32	5b	
6	Other nonrefundable credits:		
a	General business credit. Attach Form 3800	6a	A..
b	Credit for prior year minimum tax. Attach Form 8801	6b	
c	Adoption credit. Attach Form 8839	6c	
d	Credit for the elderly or disabled. Attach Schedule R	6d	
e	Reserved for future use	6e	
f	Clean vehicle credit. Attach Form 8936	6f	
g	Mortgage interest credit. Attach Form 8396	6g	
h	District of Columbia first-time homebuyer credit. Attach Form 8859	6h	
i	Qualified electric vehicle credit. Attach Form 8834	6i	
j	Alternative fuel vehicle refueling property credit. Attach Form 8911	6j	
k	Credit to holders of tax credit bonds. Attach Form 8912	6k	
l	Amount on Form 8978, line 14. See instructions	6l	
m	Credit for previously owned clean vehicles. Attach Form 8936	6m	
z	Other nonrefundable credits. List type and amount:		

X

110

Form 3468 – Investment Credit

p. 352

Form 4255 — Recapture of Investment Credit

Form **3468**
Department of the Treasury Internal Revenue Service

Computation of Investment Credit
▶ Attach to your tax return.
▶ Schedule B (Business Energy Investment Credit) on back.

OMB No. 1545-0155
1985
24

Name(s) as shown on return | Identifying number

Part I **Elections (Check the box(es) below that apply to you (See Instruction D).)**

A I elect to increase my qualified investment to 100% for certain commuter highway vehicles placed in service before January 1, 1986 (section 46(c)(6)) ☐
B I elect to increase my qualified investment by all qualified progress expenditures made this and all later tax years ☐
Enter total qualified progress expenditures included in column (4), Part II ▶
C I claim full credit on certain ships under section 46(g)(3) (See Instruction B for details.) ☐

Part II **Qualified Investment** (See instructions for rules on automobiles and other property with any personal use)

1 Recovery Property		Line	(1) Class of Property	(2) Cost or Other Basis	(3) Applicable Percentage	(4) Qualified Investment (Column 2 x column 3)
Regular Percentage	New Property	(a)	3-year		60	
		(b)	Other		100	
	Used Property	(c)	3-year		60	
		(d)	Other		100	
Section 48(q) Election to Reduce Credit (instead of adjusting basis)	New Property	(e)	3-year		40	
		(f)	Other		80	
	Used Property	(g)	3-year		40	
		(h)	Other		80	

2 Nonrecovery property—Enter total qualified investment (See instructions for line 2) 2
3 New commuter highway vehicle—Enter total qualified investment (See Instruction D(1)) 3
4 Used commuter highway vehicle—Enter total qualified investment (See Instruction D(1)) 4
5 **Total qualified investment in 10% property**—Add lines 1(a) through 1(h), 2, 3, and 4 (See instructions for special limits) 5

111

Form **3468** Department of the Treasury Internal Revenue Service

Investment Credit

Attach to your tax return.
Go to www.irs.gov/Form3468 for instructions and the latest information.

OMB No. 1545-0155 **2024** Attachment Sequence No. **174**

Name(s) shown on return | Identifying number

Part I **Information on Qualified Property or Qualified Facility** (see instructions)

1 If making an elective payment election or transfer election, enter the IRS-issued registration number for the facility

2a (i) Enter the facility's emissions value or rate (kg of CO2e per kg of qualified clean hydrogen):
(ii) Enter the Department of Energy (DOE) control number, if applicable (see instructions):

b Check this box if you are claiming a section 48E credit for a qualified facility and you have petitioned for a provisional emissions rate, and have received an emissions value from the DOE and/or used a designated lifecycle analysis (LCA) model to determine an emissions value. See instructions

3a Type (solar, clean hydrogen, rehabilitation, etc.):

b If different from filer, enter:
(i) Owner's name:
(ii) Owner's TIN:

c Address of the facility (if applicable):

d Coordinates. (i) Latitude: Enter a "+" (plus) or "-" (minus) sign in the first box. (ii) Longitude: Enter a "+" (plus) or "-" (minus) sign in the first box.

12 pages!!

112

2025 form not available yet

2024 Form 3468:

Part 1 – Information
Part 2 – Coal Project
Part 3 – Advanced Energy Project
Part 4 – Advanced Manufacturing
Part 5 – Clean Electricity Investment
Part 6 – Energy Credit Under Section 48
Sections A – N

Energy

Part 7 - Rehabilitation Credit

113

Issue #6 – Clean Energy Credit p. 352

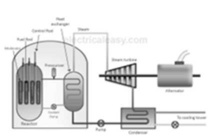
12/31/2024

IRC 45 - Energy Investment Tax credit

Inflation Reduction Act - 2022

IRC 45Y - Clean Electricity **Production** Credit

IRC 48E - Clean Electricity **Investment** Credit



114

Clean Electricity Credits p. 352

Both credits:
- Tech-neutral
- Emissions based
- Neutral and flexible between clean electricity technologies
- Facility taxpayer owns that is used to generate electricity

115

Clean Electricity Credits p. 352- 353

Clean Electricity **Production** Credit = kilowatt hours produced x ***rate***

Clean Electricity **Investment** Credit = investment in qualified facility or energy storage facility x ***rate***

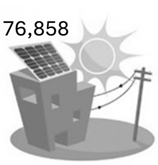
116

Example 9.22 p. 354 - 359

James constructed commercial building in 2025

solar

76,858



Rent →

Happy Trails

(James owns)

Qualifies for 30% clean electricity investment credit and 10% domestic content bonus. (IRC 48E)

See pages 355 – 359 for 3468 and 3800

117

Example 9.22 p. 354 - 359

Part V – Line 3c Regular credit	76,858 x 30%	= 23,057
Bonus Line 3e	76,858 x 10%	= 7,686
Total		30,743

118

OBBBA – Termination of Clean Electricity Production Credit + Investment Credit p. 565

Termination date for both credits has changed. Cannot claim either credit on wind and solar placed in service after 12/31/2027.

Exception- wind and solar facilities for which construction began on or before 7/4/26.

Other property - nuclear, geothermal, etc... 2032

XX

119

120