New Tax Legislation Proposed

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Introduction

On January 31, the U.S. House overwhelmingly passed tax legislation containing provisions of importance to farmers and ranchers in particular and many taxpayers in general. H.R. 7024, known as the "Tax Relief for American Families and Workers Act of 2024," is scored at nearly $78 billion and contains some retroactive provisions. Some of the key provisions modify the employee retention credit (ERC), widen eligibility for the child tax credit (CTC), reinstate expensing for research and experimental (R&E) costs; increase expense method depreciation; and reinstate bonus depreciation to 100 percent for 2023.

The legislation is currently before the U.S. Senate where it appears to have bipartisan support, if not immediate space on the Senate calendar.

Pending tax legislation – it's the topic of today's post.

Details

ERC. The IRS has been making significant efforts to eliminate abuses of the ERC. The Congress constructed the ERC poorly which made it ripe for promoters to scam businesses, including farm businesses into thinking that they were eligible for the credit or eligible for more than what was appropriate. The bill prevents additional ERC claims as of January 31, 2024 – moving up the current April 15, 2025, deadline.

Note: To put the cost of the ERC in perspective, the Joint Committee on Taxation says sunsetting the ERC as of January 31, 2024, would save $77.1 billion in spending.

The bill makes several changes relevant to the ERC with respect to a "COVID-ERTC promoter." That's a person who "aids, assists, or advises on an affidavit, refund, claim, or other document related to the ERC" if the person charges fees based on the amount of the credit or meets a gross receipts test.

The bill also makes other changes to the ERC relevant to a "COVID-ERTC promoter" as follows:

- Extends the statute of limitations for the IRS to audit ERC claims from the current five years from the date of the claim to six years for claims involving a COVID-ERTC promoter.
- Increases the penalty for aiding and abetting the understatement of a tax liability to the greater of $200,000 ($10,000 in the case of a natural person) or 75 percent of the promoter's gross income derived (or to be derived) from providing aid, assistance, or advice with respect to a return or claim for ERC refund or a document relating to the return or claim.

- Requires a promoter to comply with due-diligence requirements (similar to the due-diligence requirements applying to paid tax return preparers) with respect to a taxpayer's eligibility for (or the amount of) an ERC. Each failure to comply comes with a $1,000 penalty.
- Require a promoter to file return disclosures and provide lists of clients to the IRS on request similar to those that "material advisers" are required to provide with respect to listed transactions.

CTC

The bill makes the following changes to the CTC:

- An increase in the maximum refundable amount per child to $1,800 in tax year 2023 from $1,600. That amount then increases to $1,900 in 2024 and $2,000 in 2025. Inflation adjustments also apply for 2024 and 2025.

- For tax years 2023-2025, the CTC is to be computed by multiplying a taxpayer's earned income exceeding $2,500 by 15 percent, with the resulting amount multiplied by the number of qualifying children.

- For 2024 and 2025, a taxpayer would be able to use the taxpayer's earned income from the prior tax year to compute the maximum child credit, but only if the taxpayer's earned income in the prior year was higher than the current year.

R&E costs. The bill would amend I.R.C. §174 to reverse (at least temporarily) the impact of the Tax Cuts and Jobs Act (TCJA) provision requiring amortization of domestic R&E costs. That change under the TCJA requires amortization over a five-year period effective for tax years beginning after 2021. The bill would maintain current deductible through 2025.

Business interest. For tax years beginning before 2018, business interest (such as is paid on loans for farmland, machinery, buildings, operating lines, etc.) was fully deductible. For tax years beginning after 2017 and before 2022, deductible business interest is limited to business income plus 30 percent of the taxpayer's adjusted taxable income (ATI) for the tax year that is not less than zero. The computation of ATI is determined *without* regard to any deduction allowable for depreciation, amortization, or depletion (i.e., earnings before interest, taxes, depreciation, and amortization (EBITDA)).

The bill specifies that, for taxable years beginning after December 31, 2021, and before January 1, 2024, ATI is computed *with* regard to deductions allowable for depreciation, amortization, or depletion (i.e., earnings before interest and taxes (EBIT)). However, ATI may be computed as EBITDA, if elected, for such taxable years. For taxable years beginning after December 31, 2023, and before January 1, 2026, ATI is computed as EBITDA. For taxable years beginning after December 31, 2025, ATI is computed as EBIT.

Note: The limit is computed at the entity level with any disallowed amounts carried over to the succeeding year.

The otherwise existing rules would continue to apply. That means that any disallowed amount is treated as paid or accrued in the succeeding tax year. However, businesses entitled to use cash accounting (i.e., those with average annual gross receipts not exceeding $30 million for 2024) are not subject to the limitation. Special rules apply to excess business interest of partnerships. In addition, a farming business may elect out of the limitation. *I.R.C. §163(j)(7)(C).*

Bonus depreciation. The bill would retroactively extend I.R.C. §168 bonus depreciation for qualified property at 100 percent for property placed in service after Dec. 31, 2022, and before Jan. 1, 2026 (Jan. 1, 2027, for longer production period property and certain aircraft) and for specified plants planted or grafted after Dec. 31, 2022, and before Jan. 1, 2026. Under current law, bonus depreciation was capped at 80 percent for 2023 and is 60 percent for 2024.

Note: The retroactive nature of this provision could cause numerous issues. Many farm assets are 20-year or less MACRS property and have uniquely benefitted from bonus depreciation. This is particularly true because the personal property trade provisions of the TCJA can cause large machinery purchases that exceed the I.R.C. §179 threshold which then causes taxpayers to utilize bonus depreciation.

Sec. 179 expensing. The bill would also increase the I.R.C. §179 maximum deductible amount to $1.29 million for 2024 (up from $1.22 million), reduced by the amount by which the cost of the qualifying property exceeds $3.22 million (up from $3.05 million). Those amounts would be adjusted for inflation after 2024.

Other provisions. The bill also includes an increase in the threshold for information reporting on Forms 1099-NEC, *Nonemployee Compensation*, and 1099-MISC from $600 to $1,000, effective for payments made after 2023.

Conclusion

Will the bill pass the Senate? Probably. But that won't likely occur before March 1. Of course, that's the date that many farmers use for filing returns. As a result, for those that have already made decisions concerning depreciation, the CTC, and, perhaps, the deductibility of interest, amended returns will need to be filed. Will IRS waive the penalties if farm returns (for those that didn't pay estimated tax) are filed after March 1? That may not be known until very late in February. This all increases the chance for errors on returns. In addition, IRS forms and tax preparation software will need to be revised which will create anxiety due to pending deadlines. Retroactive tax legislation is rarely a good idea from a return preparation standpoint.