TAX CUTS AND JOBS ACT OF 2017 (TCJA) AND THE 2025 "TAX CLIFF"

Some of the taxpayer favorable tax reductions from the Tax Cuts and Jobs Act of 2017 (TCJA) were permanent changes but most are set to expire on December 31, 2025. With President Trump and the Republican majority in both the Senate and House, these expiring provisions are predicted to be extended and continue to benefit most U.S. taxpayers. While this list is not exhaustive, it highlights key considerations for most middle market taxpayers.

Sunsetting of the Qualified Business Income Deduction (QBID) for Pass-Through entities and Sole Proprietors (Section 199A)

Currently an individual taxpayer may deduct 20% of qualified business income with respect to partnership, S corporation, or sole proprietorship income as well as qualified dividends. This deduction is subject to limitations based on wage base and/or qualified investment asset base. If this is not extended, this provision sunsets at the end of 2025.

Increasing Individual Income Tax Rates

The current corporate income tax rate of 21% is not scheduled to sunset so that will remain at least for the near future. Under the TCJA, individual marginal rates are 10%, 12%, 22%, 24%, 32%, 35%, and 37%. (Note: Taxes on capital gains and dividends were not changed by the TCJA.) If this does not get extended, the 12/31/2025 marginal rates will revert to their permanent pre-TCJA levels of 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%.

Repeal of Excessive Business Loss Limitation (Section 461(l))

Section 461(l) provides that for taxable years beginning after 2017 and before 2026, any excess business loss of a taxpayer other than a corporation is not allowed for the year. This disallowed excess business loss can be carried forward to a subsequent taxable year. This excess loss is non-deductible when it exceeds $250,000 ($500,000 for joint returns) as adjusted for inflation. Without an extension, this provision expires at the end of 2025 and reverts back to pre-TCJA rules.

Restoration of the State & Local Tax Deduction for Regular Tax Purposes

TCJA put a cap of $10,000 on the itemized deduction amount for state and local taxes (SALT). This cap applies to property tax, state and local income tax and general sales tax. This is especially a burden to taxpayers in states with a high tax rate. As a work around to this cap, many states implemented a pass-through entity level tax (PTE) opportunity which allows state income taxes to be deducted from ordinary income of the pass-through entity. These rules are complex and result in an administrative burden which can result in additional professional fees. If not extended, the SALT cap is removed and deductions for SALT taxes are restored to pre-TCJA amounts.

Phase-Down of Bonus Depreciation to Zero by 2027

Originally a 100% first year deduction was allowed on applicable fixed assets. This 100% allowance is phased down by 20% per calendar year. For 2024, the deduction is 40% going down to 0% by the year 2027. This will most likely be part of an extender package.

Continuation of the Amortization of Research and Experimental Expense Capitalization under Section 174

For taxable years beginning after 2021, research and experimental expenditures are required to be capitalized and amortized over 5 years for those incurred in the

U.S and over 15 years if incurred outside of the U.S. Prior to this, a taxpayer could elect to fully deduct the amount of certain reasonable research or experimental expenses incurred in a trade or business. The requirement to capitalize these expenses has been controversial as it does not encourage innovation in the U.S. Without a change to the tax laws, the requirement to capitalize these types of costs continues.

Repeal of the Excess Business Interest Limitation (Section 163(j)

TCJA generally limits the amount of interest currently deductible to the sum of (1) business interest income and (2) 30% of the taxpayer's adjusted taxable income. This limitation applies only to taxpayers with annual gross receipts exceeding $25 million (adjusted for inflation).

Decrease in Lifetime Gift and Estate Tax Exemption

TCJA doubled the lifetime exemption at the time from $5.49 million to $11.18 million. The 2025 lifetime exemption is $13.99 million. Unless this update is made permanent, the exemption will be reduced by 50% in 2026.

Extending the expiring tax laws requires Congressional action, not only executive power. Laws passed via a budget reconciliation process must either offset tax cuts with revenue or limit deficits within a 10-year window. If the House initiates this process in the next week or so, a final bill could meet the administration's target of early May. None of this is certain but evaluating for the current sunset of provisions should be part of every taxpayer's planning.

If any questions related to this article, please reach out to your BMF Tax Advisor.