DHS ADVISORS

# Partnership and LLC Year-End Tax Planning Letter

December 1, 2025

Dear Client:

As the end of the year approaches, it is time to consider planning moves that may help lower your tax bill and stay compliant with various reporting requirements.

**Schedules K-2 and K-3**
The IRS requires Partnerships to complete Schedules K-2 and K-3, with Form 1065, to report items of international tax relevance from the operation of a partnership.

For the 2025 taxable year, a filing exception for purely domestic partnerships exists, and a partnership is not required to complete Schedules K-2 and K-3 and file them with the IRS if:

- The partnership has no or limited foreign activity, which is specifically defined in the instructions and includes domestic partnerships whose only foreign activity is passive category foreign income that:
  - Only generates $300 or less of taxes subject to the Foreign Tax Credit; and
  - Is shown on a payee statement such as Form 1099-DIV;
- All partners are U.S. citizens or resident aliens, partnerships with partners that are S corporations owned by a sole shareholder and disregarded single-member LLCs owned by U.S. citizens or resident aliens domestic decedent estates, domestic grantor trusts or domestic non-grantor trusts with U.S. citizen or resident alien individual beneficiaries, or sole shareholder S corporations;
- With respect to a partnership that satisfies the criteria above, partners receive a notification from the partnership at the latest when the partnership furnishes the Schedule K-1 to the partner. The notice can be provided as an attachment to Schedule K-1. The notification must state that partners will not receive Schedule K-3 from the partnership unless the partners request the schedule; No partners specifically request Schedule K-3 from the partnership on or before the 1-month date. The “1-month date” is 1 month before the date the partnership files Form 1065. For tax year 2025 calendar year partnerships, the latest 1-month date is August 15, 2025, if the partnership files an extension.

**Partnership Audit Rules**
The Bipartisan Budget Act of 2015 made significant changes to the IRS partnership audit rules effective for partnership tax years beginning in 2018. There are provisions to allow certain partnerships the ability to elect out of the new rules. To ensure that our firm has the required documentation to support the partnership’s decision in order to apply the new partnership audit rules to your 2025 returns, we will require you to complete the information requested on the addendum to your partnership tax services engagement letter.

**General Information**
Business records and documents should be up-to-date. You should have prepared minutes of your partners’ meetings. The minutes should describe the nature of the meeting and include any payments to the partners, loans to or from the partners, as well as rent paid, and any other financial transactions between the partnership and the partners. If you have inventories, you should take a physical count on December 31. Please remember that the due date for filing copy A of Form(s) W-2 and W-3, as

well as Form 1099-NEC is February 2, whether you file using paper forms or electronically. While the 1099-NEC filing threshold has been increased to $2,000 as part of the One Big Beautiful Bill Act, this increased filing threshold goes into effect beginning in 2026, and remains at $600 for 2025. Form 1099-MISC is due on paper by March 2, and electronically by March 31. If you file 10 or more information returns (W-2, 1099, etc.), you must file those forms electronically with the IRS.

**Capitalization Regulations**
Please review and update your asset capitalization policy. Businesses may be able to take advantage of the "de minimis safe harbor election" to expense the cost of lower-cost assets, materials, and supplies. The amount allowed to be expensed depends on whether the taxpayer has written accounting procedures in place and, if so, whether the taxpayer has an applicable financial statement. If the taxpayer has a *written* accounting procedure and issued applicable financial statements, costs can be expensed up to $5,000 per item. If a taxpayer does not issue financial statements, but has a written accounting policy, expenditures cannot exceed $2,500 per item, beginning in 2016.

**Business Asset Depreciation and Expense Deduction**
Under the One Big Beautiful Bill Act (OBBBA), a 100% first-year deduction is allowed for qualified new and used property acquired and placed in service between January 19 and December 31 of 2025. Qualified new property placed in service between January 1 and January 18 is eligible for a 40% first-year deduction under the Tax Cuts and Jobs Act (TCJA). After 2025, federal bonus depreciation will remain at 100% permanently under the OBBBA.

You should consider making expenditures for qualifying Code Section 179 property. The 2025 maximum amount that may be expensed under Code Section 179, for federal purposes, is $2,500,000. The expense deduction is reduced dollar-for-dollar to the extent eligible Section 179 property placed in service for the year exceeds $4,000,000. No Section 179 expense is allowed if eligible property additions exceed $6,500,000 in 2025.

The federal maximum depreciation allowance for passenger automobiles is decreased to $12,200 for the year the vehicle is placed in service, if bonus depreciation is not claimed. For passenger automobiles eligible for first-year bonus depreciation, the first-year depreciation allowance is increased by $8,000, resulting in a total of $20,200. Trucks and vans (including minivans and SUVs) with a gross vehicle weight exceeding 6,000 pounds are treated as transportation equipment and are not subject to the bonus depreciation limitations. The Section 179 deduction for any SUV rated at 14,000 pounds gross vehicle weight or less is limited to $31,300.

California does not conform to the federal bonus depreciation deduction or the Code Section 179 limits and passenger automobile depreciation changes.

**Pass-Through Entity (PTE) Tax Election Information**
As previously discussed in other communications, for taxable years beginning on or after January 1, 2021, and before January 1, 2031, qualifying PTEs may annually elect to pay an entity-level state tax equal to 9.3% of its qualified net income. This will decrease the federal net income included on qualified taxpayers pass pass-through income (Schedule K-1), and they will receive a credit for their share of the entity-level tax, reducing their California personal income tax liability.

This allows the owner to reduce federal Adjusted Gross Income rather than having a state tax deduction on Schedule A, which would normally be subject to the $40,000 state and local tax ("SALT") deduction limit. For federal purposes, the net income is reduced by the amount of the tax paid at the entity level.

For California tax purposes, the state tax deducted on the federal return will be added back to net income, but the individual will receive a non-refundable California tax credit, equal to 100% of the state tax paid by the pass-through entity on their behalf.

**Beneficial Ownership Information (BOI) Reporting**
As discussed in previous communications, the Financial Crimes Enforcement Network (FinCEN) required entities that register with state or tribal government agencies to report Beneficial Ownership Information (BOI) by the initial due date of January 1, 2025. On March 26, 2025, FinCEN published an interim rule that redefined entities required to report BOI to include only those formed under the law of a foreign country that have registered to do business in a U.S. state or tribal jurisdiction.

**Retirement Plan Contributions**
Please confirm the contributions that you have made to your plan so far in 2025. Contributions of employee elective deferrals to SIMPLE IRA and SIMPLE 401(k) plans are due 30 days after the month of the payroll deferral, making the final deposit due by January 30, 2026. Contributions of employee elective deferrals to 401(k) plans are due 15 business days after the month of the payroll deferral, making the final deposit due by January 15, 2026. The maximum contribution allowed for SIMPLE plans is $16,500 ($20,000 if you are age 50 or older). The maximum contribution allowed for 401(k) plans is $23,500 ($31,000 if you are age 50 or older). Any matching contributions or non-elective contributions are due by the due date of your return, including extensions.

The contributions you make to each employee's SEP-IRA cannot exceed the lesser of 25% of compensation or $70,000. Self-employed individuals involved in incorporated businesses use the shareholder's W-2 compensation for their personal contribution and follow the previously stated criteria. Self-employed individuals not involved in incorporated businesses must take the net earnings from self-employment into account for their SEP calculation, and their contribution may be up to 25% of their modified net profit. Contributions for SEP-IRA plans are due by the due date of the employer's return, including extensions. Additional information on retirement plans for small businesses can be located in IRS Publication 560.

**Taxable Fringe Benefits**
Generally, the value of non-cash fringe benefits must be determined no later than January 31 of the following year. However, we recommend you consider the impact of the fringe benefits you provide during December to avoid penalties for not making timely payroll tax deposits.

**Before you prepare W-2 forms for your employees' 2025 compensation, please review the following:**
Benefits, including holiday bonuses and amounts paid in cash or cash equivalents, such as gift cards, are included in payroll, regardless of the amount. De minimis fringe benefits, such as personal use of business equipment, gifts, etc. must be small in value and infrequent. These can be excluded from payroll.

If you paid for group-term life insurance over $50,000 for an employee or a former employee, you must report the taxable cost of excess coverage in box 12 of Form W-2, with code C. The amount to report is determined by using IRS Publication 15-B.

Contributions made by an employer to an employee's health savings account (HSA) are excluded from federal wages and not subject to federal employment taxes. No exclusion from wages or taxes is allowed for California payroll reporting. The 2025 contribution limits are $4,300 for a self-only HSA

and $8,550 for a family HSA. An additional contribution of $1,000 is allowed if the employee is age 55, or older, at year-end.

To comply with the Affordable Care Act, employers are required to report the cost of health benefits provided in box 12 of the form W-2 with code DD.

Please remember to check Form W-2, box 13, retirement plan, if your employee is an active participant in your company's retirement plan. This includes qualified retirement plans, annuities, SEP, and SIMPLE plans.

Employee Use of Company Vehicles - If you provide a vehicle to an employee that was used for both business and personal use, the value of the personal use must be included on the employee's W-2 and is subject to payroll taxes.

Written records must indicate the time and place of travel, the business purpose of the expense or use, and the mileage traveled for all employee use of business vehicles.

The following is a brief description of the four different methods that can be used to determine the value of the auto provided to the employee and what records need to be kept. For more detailed information, see IRS Publication 15-B.

1. **General Valuation Rule --** Under this rule, the value of an employer-provided vehicle to be included on the employee's W-2 is its fair market value (FMV). The FMV of the vehicle is the amount an employee would have to pay a third party in an arm's-length transaction to lease the vehicle in the geographic area where the employee uses the vehicle. Neither the amount the employee considers to be the value nor the cost you incur to provide the vehicle determines its FMV. The FMV is multiplied by the ratio of personal miles to total miles driven, and the result is reduced by reimbursements, if any, received from the employee to determine the amount to include in the employee's income.

2. **Cents-Per-Mile Rule --** Under this rule, the value of an employer-provided vehicle to be included on the employee's W-2 is determined by multiplying the standard mileage rate by the total miles the employee drives the vehicle for personal purposes. The standard mileage rate for 2025 is 70 cents per mile, if you provide fuel. (If you did not provide fuel, you can reduce the rate to 64.5 cents per mile).

   The cents-per-mile rate includes the value of insurance and maintenance (even if not actually provided during the period).

   The cents-per-mile rule may be used for an employer-provided vehicle (including cars, vans, and trucks), first made available to an employee for personal use in calendar year 2025, with a maximum value of $61,200.

3. **Commuting Rule --** Under this rule, the value of a vehicle provided to an employee for commuting is determined by multiplying each one-way commute (that is, from home to work or from work to home) by $1.50. If more than one employee commutes in the vehicle, this value applies to each employee. This amount must be included in the employee's wages if not reimbursed by the employee.

   The commuting rule can be used if you require the employee to commute in the vehicle, and you have a written policy against using the vehicle for personal purposes, other than

commuting. However, you cannot use it for a corporate officer, a director, or certain categories of control or highly compensated employees.

4. **Annual Lease Value Rule --** Under this rule, the value of an automobile provided to an employee is determined by its annual lease value. For an automobile provided only part of the year, use either its prorated annual lease value or its daily lease value.

   Instead of excluding the non-personal value, you can include the entire annual lease value of the car in the employee's wages. The employee can then claim any deductible business expense for the car as a miscellaneous itemized deduction on his or her personal California income tax return. However, employee business expenses are no longer deductible on the employee's federal income tax return.

   The annual lease value includes the value of insurance and maintenance (even if not actually provided during the period). It does not include the value of fuel for personal use. If fuel for personal use is provided, then it must be included separately in the employee's wages. The fuel may be valued at FMV, or at 5.5 cents per mile.

   To determine the annual lease value of an automobile you must first determine the FMV of the automobile on the first date it is available to any employee for personal use, and then find the lease value. The annual lease value table can be found on page 27 of IRS Publication 15-B. A link has been provided for your convenience: https://www.irs.gov/pub/irs-pdf/p15b.pdf

Safe Harbor Rules -- Employers may implement written policy statements of “no personal use” or “commuting use only” of a company vehicle that will qualify as sufficient evidence corroborating an employee's own statement, without the need for a second set of records.

**Nondeductible Parking Benefits**

OBBBA permanently eliminated an employer's income tax deduction for expenses incurred in providing qualified transportation fringe benefits (parking, commuter transportation, transit passes). However, this change did not affect the employee's fringe benefit treatment. The amount of qualified parking excludable from an employee's income is limited to $325 per month for 2025.

The IRS released guidance in Notice 2018-99 clarifying that a portion of taxpayers' "parking expenses" is considered nondeductible as a qualified transportation fringe benefit. This has significantly expanded the number of taxpayers who will need to calculate the nondeductible portion of their parking expenses. Now, all employers that own or lease a parking lot where their employees park will need to consider if an add-back to taxable income is required. This provision applies to expenses incurred or paid after December 31, 2017.

**Other Reporting Requirements under the Affordable Care Act (ACA)**

Applicable Large Employers, generally employers with 50 or more full-time employees in the prior year (including full-time equivalent employees), are subject to the ACA employer mandate, and must report “minimal essential coverage” (MEC) for their health plans.

Form 1095-C must be prepared and provided to each full-time employee. The due date to furnish Form 1095-C to individuals is March 2, 2026. Form 1094-C is used to report summary information and to transmit Forms 1095-C to the IRS. These forms must be electronically filed no later than March 31, 2026. These forms fall under the revised electronic filing requirement, where 10 or more forms in the aggregate must be filed electronically.

Employers that offer employer-sponsored self-insured coverage also use Form 1095-C to report information to the IRS and to employees. There are additional reporting requirements for self-insured employers. Penalties will be charged for noncompliance with the employer mandate as well as the compliance reporting.

**Harassment Training**
Employers with five or more employees must provide at least two hours of classroom or other effective interactive training and education regarding sexual harassment to all supervisory employees and at least one hour of classroom or other effective interactive training and education regarding sexual harassment to all nonsupervisory employees in California within six months of their assumption of a position. This training must be provided once every two years.

More information is available at: https://www.calcivilrights.ca.gov/shptfaq-employer/

Limitations and restrictions exist on the information provided, so please feel free to contact us with any questions you might have regarding these or any other year-end tax strategies that we can assist you with or develop for you.

Sincerely,

DHS Advisors