2024 TAX STRATEGIST WEBCAST SERIES

PRIVATE EQUITY

The Tax Outlook for Private Equity: 2025 and Beyond

DECEMBER 10, 2024

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With You Today

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Learning Objectives

Evaluate the potential impacts of the incoming administration's tax plan on private equity fund structures and operations.

Identify strategic opportunities to adapt to changes in the tax environment.

Analyze how proposed tax reforms could affect portfolio companies and influence investment strategies.

Knowledge Check #1

How has the outcome of the 2024 election impacted your view of future tax liability?

- **A** Expect it will remain the same
- **B** Expect it will decrease slightly
- **C** Expect it will increase slightly
- **D** Expect it will decrease significantly
- **E** Expect it will increase significantly
- **F** N/A

LEGISLATIVE ACTIVITY

TCJA Permanent Business Provisions

Whether through a tax package or an extenders bill, most TCJA provisions expire after 2025.

Permanent business provisions include: The 21% corporate rate and 15% CAMT are permanent (from IRA), as is the increased Sec. 179 expensing (from $500K to $1M), and business interest limitation (Sec. 163(j))

- 21% corporate rate
- 15% corporate AMT (enacted in IRA)
- Business interest limitation under Sec. 163(j), which limits the deduction to 30% of adjusted taxable income
- NOL deductions limited to 80% of taxable income with indefinite carryforward
- Requirement to capitalize and amortize R&E expenditures generally over 5 years
- Increased Sec. 179 expensing to $1 million, indexed for inflation with increased phaseout to $2.5 million

LEGISLATIVE ACTIVITY

TCJA Expiring Provisions

Expiring provisions include:

- Limit on excess business losses under Sec. 461; incomes over $500K must carry forward; expires after 2028
- Bonus depreciation phase out; 20% 2026, then zero in 2027
- Qualified 20% Business Income Deduction under Sec. 199A
- Individual provisions. The alimony provisions effective in 2018 are permanent.
  - Individual rates with top rate of 39.6%
  - AMT exemption
  - PEP and Pease (personal exemption and itemized deduction limits)
  - Charitable contribution limit
  - SALT $10,000 cap
  - Estate tax exemption reverts back from $13.61 million in 2024 to $7 million in 2026
    - The 40% rate is permanent

LEGISLATIVE ACTIVITY

Potential Revenue Impact

- Decrease to revenue for full 10-year extension of TCJA Provisions - $4.2 trillion
- Exempt overtime from individual taxation - $750 billion - $2 trillion
- Exempt Social Security from taxation - $1.2 - $1.3 trillion
- Exempt tip Income - $120 - $300 billion
- Lower corporate rate to 15% for domestic production - $200 - $360 billion
- Remove SALT cap - $1.0 trillion
- Impose a universal 20% tariff plus a 50% tariff on all imports from China – increase revenue by $2.7 – $3.8 trillion.

Sources used Committee for a Responsible Federal Budget and The Tax Foundation

Corporate Items

- Corporate rates will potentially be reduced from 21% to 20%/15% for U.S. manufacturers (to be defined). Reduction would not be material for most middle market private equity portcos.
- CAMT – 15% minimum book tax for large corporations (AFSI > $1 billion).
  - CAMT proposed regulations involve tremendous complexity
  - Cost to taxpayers versus revenue generation
  - Finalized regulation timing
  - Impact on M&A
- Excise – 1% corporate-level excise tax on redemptions of public corporation stock.
  - Intended rate increase under Harris off the table
  - Relatively easy to implement with the exception of certain specific structures
- Vance and SSGMA (March 24). Would tax otherwise tax-free mergers in excess of $500 million threshold.

Knowledge Check #2

Which of the following potential corporate tax changes in 2025 are you most interested in?

A Potential repeal of the corporate AMT

B Potential repeal of the corporate excise

C Potential rate decrease from 21% to 20%/15%

D Potential repeal of R&E capitalization requirement

E Potential extension of 100% bonus depreciation deduction

F N/A

Summary of Key Proposals for Partnership Reform

REPEAL

- Repeal the substantial appreciation requirement for "hot assets" with respect to partnership distributions
- Repeal guaranteed payments
- Repeal special rule for retiring or deceased partners – Section 736
- Repeal the disguised sale exception for preformation capital expenditures
- Repeal the 7-year anti-mixing bowl window – i.e., the rule would apply indefinitely

MANDATE

- Mandatory basis adjustments under Sections 734 and 743 (repeal Section 754 election)
- Mandatory use of remedial method for Section 704(c) allocations
- Mandatory revaluations, including through tiers in certain situations

OTHER CHANGES

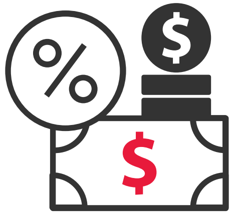
- Change allocation rules – repeal substantial economic effect safe harbor, impose a consistent allocation method for controlled partnerships, etc.
- Change rules for allocating debt
- Change rules for publicly-traded partnerships
- Change partnership rules for interest expense limitation – Section 163(j)
- Change partnership termination rules for related party transactions
- Change basis adjustment rules for related party transactions and tiered partnerships

Knowledge Check #3

Which of the following partnership tax changes are you most interested in?

- **A** Potential mandatory use of the remedial method
- **B** Potential repeal of guaranteed payments
- **C** Potential repeal of substantial economic effect safe harbor for partnership allocations
- **D** Potential repeal of disguised sale exception for preformation capital expenditures
- **E** N/A

TCJA Extenders



Bonus Depreciation

Under the TCJA, qualified property allowed 100% expensing in lieu of depreciation. Beginning in 2023, 100% deduction was reduced 20% per year until phaseout in 2027.

R&D Expensing

Section 174 amended to transition expensing of R&D costs to 5-year amortization for domestic research, 15 years for foreign.

Business Interest Deduction

Net interest plus 30% of adjusted taxable income. Post-2021, moved from an EBITDA calculation to EBIT.

Knowledge Check #4

Would you like the BDO team to reach out to you?

A Yes, I would like to speak someone from BDO.

B No, I am not interested at this time.

Thank You!

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