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Saving Benefits of the New Pass Through Law

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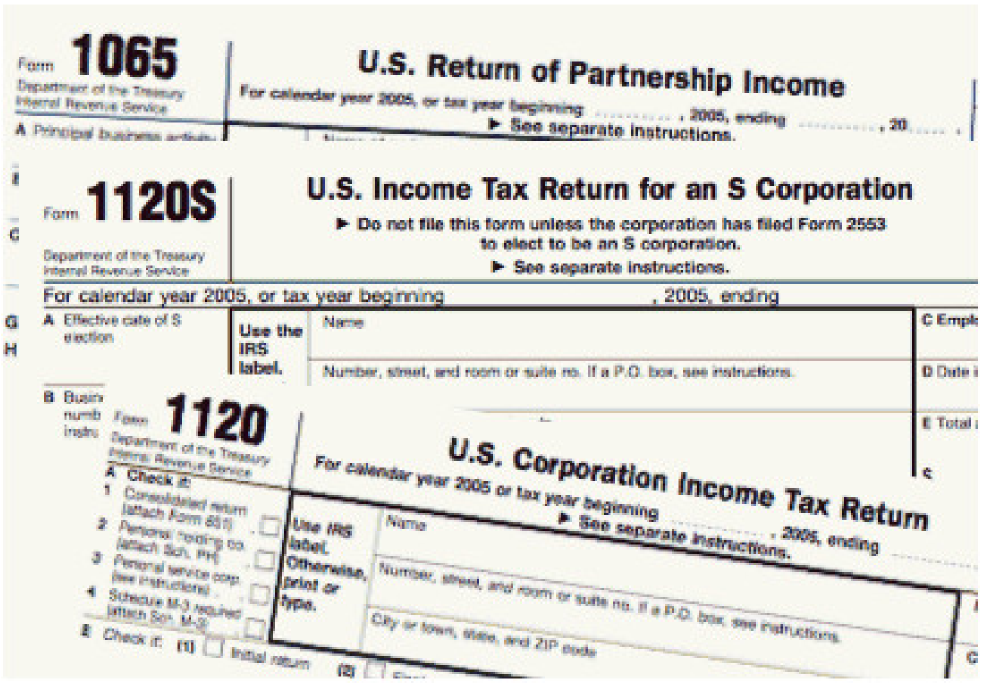

The New Jersey Society of Certified Public Accountants (NJCPA) is reminding taxpayers about specific tax-saving benefits available from the new Pass-Through Business Alternative Income Tax Act (S3246), which was signed by Governor Murphy on Jan. 13. While the new law does not apply to single-member LLCs or sole proprietorships, if these businesses add a partner — even for a 1-percent ownership stake — or in the case of a single member LLC, elect to be treated as a Subchapter S

"I have been suggesting to my small business clients, who are landscapers, contractors, etc., and who are set up as single-member LLCs or sole proprietorships, to consider adding a member (partner) to their business so that they can qualify under this new legislation," said Gail Rosen, CPA, of Gail Rosen CPA PC of Martinsville, New Jersey. "The highest tax savings I have calculated for my clients so far is $8,237, and that client has filed the paperwork to change from a single-member LLC to a multi-member LLC." Spouses, who have typically been involved in these businesses, can be added for a small-percentage ownership and the business owners can save considerably on their taxes every year, she added.

Wayne D. DeFeo, LEED AP, principal and founder of DeFeo Associates, a Warren, New Jersey-based full-service environmental consulting firm and client of Gail Rosen's, said he is seriously considering adding a partner to achieve the tax savings. "I have to look at all of the tax consequences and of course my business model. However, I am strongly leaning in that direction," he said. "My initial tax saving estimates are in the $2,000 to $3,000 range per year. I could then make investments in new computer equipment more easily. It would also allow me to look at a better monthly cash flow."

The switch to a pass-through entity, as opposed to a C corporation, where long-term double taxation can be expensive, has other benefits, such as reducing the chances of an audit if the business owners file their taxes as a partnership versus a single owner, according to Rosen. "A business that has gross income of between $100,000 and $200,000 before deductions has approximately a one in 48 chance of being audited (2.1-percent chance) as a single owner. Partnership returns have approximately a one in 260 chance (0.4-percent chance) of being audited. This equates to more than five times less of a chance of being audited if they file as a partnership," she explains. She also noted that with this setup, having a separate tax return for the entity can come in handy if a business ever needs to give their tax return to a third party; for instance, to sell their business or apply for a loan. This way, the business owner can hand over

owners were at a disadvantage.

With the new law, Sobel explained, “while you will report the income on your personal Form NJ-1040, you will receive 100-percent credit for the New Jersey taxes paid at the entity level and pay no additional state taxes than you would have paid prior to enactment of the Pass-Through Business Alternative Income Tax Act.”

The new legislation took effect Jan. 1, 2020, and is not retroactive for the 2019 tax year. Business owners should work with their CPA or financial advisor to weigh all the factors to determine whether they should take advantage of the benefits of the Act.

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