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Monthly US Tax Bulletin

October 2025

Welcome to the October edition of Grant Thornton Bharat's US Tax Newsletter, a monthly guide to keep you informed of key developments across the federal, state, and local tax landscape. In an environment marked by regulatory shifts, economic uncertainty, and increasing complexity, staying informed is crucial for making strategic and compliant decisions. This newsletter is designed to deliver timely, relevant, and actionable insights to help you navigate the evolving tax landscape with confidence.

This edition features curated updates on recent legislative changes, IRS enforcement priorities, and emerging trends. Whether you are navigating corporate tax reform, assessing cross-border implications, or managing compliance challenges, we aim to support your efforts with clarity and precision.

The most notable federal tax update this month is that Treasury and IRS plan to withdraw the Disregarded Payment Loss (DPL) rules, as per Notice 2025-44, extending transition relief for the Dual Consolidated Loss (DCL) rules without regard to the GloBE Model Rules for losses incurred in taxable years beginning before 1 January 2028. The IRS finalised regulations revising interest capitalisation under §263A(f) by eliminating the "associated property" rule and updating the definition of "improvement." The IRS is urging taxpayers to adopt Identity Protection PINs (IP PINs) and multi-factor authentication to strengthen the security against tax-related identity theft. The Work Opportunity Tax Credit (WOTC), which incentivises hiring from targeted groups, will expire in 2025. Affordable Care Act enforcement for large employers remains active despite the recent layoffs and resignation at the IRS, with steep penalties for non-compliance of appropriate IRS forms making timely and accurate reporting essential.

Several states have introduced significant tax changes. New Jersey launched a major tax credit programme to boost manufacturing and clean energy investment. California finalised market-based sourcing rules for services and intangibles. Alabama decoupled from federal R&D amortisation rules, allowing immediate deductions or elect to defer the expenses as provided in the pre-TCJA amortisation rules. New Hampshire announced a tax amnesty programme for unpaid liabilities. This programme provides a waiver of penalties and interest exceeding 50% of applicable interest. Philadelphia introduced phased Business Income and Receipts Tax (BIRT) rate reductions and removed small-business filing exemption, while clarifying market-based sourcing for software companies. Illinois enacted major reforms, including adoption of the Finnigan method, limits on related-party expense exceptions, a GILTI deduction cap, and expanded sales and use tax obligations for remote sellers and service providers.

We recognise that tax considerations are integral to broader business strategy. As such, we remain committed to helping you align your tax planning with your organisational objectives, ensuring you are well-positioned to respond to both immediate developments and long-term regulatory shifts.

We trust this edition provides a valuable perspective on the evolving tax and compliance landscape. As we continue to monitor developments at the federal and state levels, our goal is to keep you informed with insights that are both timely and actionable.

Happy reading!

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A

Key developments under US federal laws

Treasury and the IRS intend to issue proposed regulations withdrawing the disregarded payment loss ("DPL") rules.

Using Notice-2025-44, the Treasury and the IRS intend to issue proposed regulations withdrawing the disregarded payment loss ("DPL") rules under §1.1503(d)-1(d). The DPL rules were finalised on 14 January 2025 and are applicable with respect to losses incurred in taxable years beginning on or after 1 January 2026. In addition, this notice announces an extension of the transition relief initially announced in Notice 2023-80, with respect to the interaction of the Dual Consolidated Loss ("DCL") rules and the Model Rules published by the OECD/G20 Inclusive Framework on BEPS (the "GloBE Model Rules"). The notice extends the transition relief such that the DCL rules will be applied without regard to the GloBE Model Rules for losses incurred in taxable years beginning before 1 January 2028.

[Internal Revenue Bulletin (IRB) No. 2025-37 dt: 09/08/2025. Page 386. Notice 2025-44]

IRS finalises regulations modifying the interest capitalisation requirements for affected improvements

On 2 October 2025, the Internal Revenue Service (IRS) issued final regulations that revise the interest capitalisation requirements under §263A(f) for improvements classified as designated property. These regulations eliminate the "associated property" rule and related provisions from the existing framework. Additionally, the definition of "improvement" has been updated to align with current standards, ensuring consistency in application. Further modifications have been made to other related rules to reflect the removal of the associated property rule. These changes impact taxpayers engaged in the improvement of real or tangible personal property that qualifies as designated property under the uniform capitalisation rules. Businesses with gross receipts of up to USD 25 million (as adjusted for inflation pursuant to Sections 263A(i)and 446(c)) are exempted from the requirement to capitalise costs, including interest, under Section 263A; businesses with gross receipts of more than USD 25 million (as adjusted for inflation) are impacted by these final regulations. These final regulations do not impose an additional record-keeping or reporting burden related to Section 263A for taxpayers. However, the requirement to file the applicable tax form to effect a change in the accounting method introduces an additional compliance burden for taxpayers. These final regulations take effect on 2 October 2025.

[Federal Register, IRS final rule (TD 10034), 90 FR 47581]

Importance of applying for IRS Identity Protection PINS (IP PINS); IRS online accounts to safeguard from theft and scams.

The IRS and Security Summit partners are urging tax professionals and taxpayers to take proactive steps against tax-related identity theft. Key recommendations include enrolling in the IRS Identity Protection PIN (IP PIN) programme and setting up secure IRS online accounts.

Tax professionals are reminded that the multi-factor authentication (MFA) is not only a best practice but also a federal requirement under the Federal Trade Commission's Safeguards Rule. The MFA helps prevent unauthorised access to sensitive client data and protects against phishing and other cyber threats. The IRS also encourages taxpayers to obtain an IP-PIN, a six-digit number that adds an extra layer of security to their tax filings. IP PINs are renewed annually and must be obtained directly by the taxpayer. Both IRS online accounts and Tax Pro accounts offer secure access and management of tax information, helping to prevent fraud and identity theft.

This initiative is a part of the "Protect Your Clients, Protect Yourself" campaign, featured in the IRS Nationwide Tax Forums held across the US this summer.

[Internal Revenue – News Releases – IR-2025-83]

The Work Opportunity Tax Credit expires in 2025

Securing employment can be challenging, especially for individuals from certain groups who face persistent barriers to entering the workforce. The Work Opportunity Tax Credit (WOTC) is a federal incentive designed to encourage employers to hire individuals from these targeted groups by offering a tax credit for qualifying hires. The WOTC is available until 31 December 2025 for employers that hire workers who are qualified as part of these groups. These groups include qualified recipients of long-term family assistance, long-term unemployment, supplemental nutrition assistance programme benefits, supplemental security income, a state programme funded under Part A of Title IV of the Social Security Act relating to the temporary assistance for needy families, formerly incarcerated individuals, qualified unemployed veterans, including disabled veterans, residents living in empowerment zones or rural renewal counties, vocational rehabilitation programmes, summer youth employees living in empowerment zones. To claim the credit, employers must get certification that an individual is certified as a member of one of the groups listed above and submit IRS Form 8850 to their state workforce agency within 28 days of the employee's start date. Employers should not submit this form to the IRS. Eligible businesses can compute the credit on the applicable tax form and claim it on Form 3800, General Business Credit.

[Internal Revenue Services Tax Tip 2025-60]

IRS tightens Affordable Care Act enforcement for applicable large employers (ALEs)

The IRS has been actively enforcing the Affordable Care Act, as it applies to applicable large employers, also known as ALEs. Despite recent IRS staffing challenges, enforcement of the Affordable Care Act (ACA) for ALEs remains active. ALEs are those with 50 or more full-time equivalent employees who must offer minimum essential coverage and file Forms 1094-C and 1095-C. Failure to comply can result in employer-shared responsibility penalties and additional fines for submitting missing or incorrect information returns. ALEs that fail to meet the reporting requirement are subject to similar penalties assessed for failing to file or furnish Forms 1098, 1099, and W-2. It is common for the IRS to assume that an ALE failing to file appropriate forms also did not furnish forms to employees, triggering a second penalty per recipient. Notices often allow only 90 days to respond, making quick action critical. The Congress set a six-year limit on assessments for forms filed after 31 December 2024, but earlier periods may have no clear statute of limitations; however, it is certainly less. ALEs should maintain proof of coverage offers and submit timely filings, and may seek expert help promptly if contacted by the IRS to minimise potential liabilities.

[26 U.S. Code § 4980H, IRS Affordable Care Act Q&A]

B

Key developments under US state laws

Governor Murphy signs Bipartisan Legislation to strengthen New Jersey's manufacturing industry

On 13 August 2025, Governor Phil Murphy signed A5687/S4407, creating a new USD 500 million tax credit programme that incentivises manufacturing investment and job creation. The next New Jersey manufacturing programme, which will be administered by the New Jersey Economic Development Authority (NJEDA), will encourage growth in New Jersey's manufacturing sector by offering long-term benefits to manufacturing companies.

Under the programme, eligible businesses having a facility that is primarily (>50%) engaged in manufacturing industries, including advanced manufacturing, non-retail food and beverage, defence, clean energy, and life sciences can receive a tax credit award equal to the lesser of 0.1% of the eligible business's total capital investment multiplied by the number of new full-time jobs or 25% of the eligible business's total qualified investment, subject to a total cap of USD 150 million per project. USD 100 million in tax credits will be reserved for clean energy product manufacturers in industries such as solar, geothermal, and green hydrogen in the first two years, supporting innovative companies in furthering the state's clean energy goals and promoting clean manufacturing. After the first two years of the programme, any unused proceeds will be rolled over into the general manufacturing allocation. The NJEDA is now accepting applications and will remain open until all funds are committed or till 1 March 2029, whichever comes first.

[New Jersey Assembly No. A5687/S4407]

California adopts final sourcing rules for services and intangibles

California's Franchise Tax Board ("FTB") adopted final regulations amending the rules regarding market-based sourcing for sales other than the sales of tangible personal property, effective for tax years beginning on or after 1 January 2026. Key amendments include the introduction of new default rules and presumptions for determining the location where the benefit of services is received, as well as revised definitions and unique sourcing provisions for the receipts derived from asset management services and professional services. In addition, a distinct sourcing rule is

established for large-volume professional services. Further, there are updated rules for sourcing receipts from specific government service contracts, along with new definitions and presumptions about the sourcing of receipts from the sale of marketable securities.

[California Code of Regulations, Title 18, Section 25136-2]

Alabama decouples from Federal R&D amortisation rules

House Bill 163 makes amendments to how businesses in Alabama handle research and experimental (R&E) expenses for tax purposes. The Tax Cuts and Jobs Act (TCJA), effective as of 2022, required businesses to amortise R&D expenses over five years, rather than deducting them immediately. This change increased taxable income and upfront tax liability for the companies investing in innovation. House Bill 163 decouples Alabama from the federal treatment of R&E expenses under Section 174, allowing businesses to revert to pre-TCJA rules for state tax purposes.

Starting with tax years beginning 1 January 2024, Alabama businesses can:

- Deduct their R&E expenses immediately in the year they are incurred, or
- Elect to defer the expenses as provided in the pre-TCJA amortisation rules.

This change is retroactive to 2024 and is intended to reduce the upfront tax burden for innovative businesses. This act took effect on 1 October 2025.

[House Bill 163]

New Hampshire enacts tax amnesty programme

New Hampshire has enacted House Bill 2, establishing a tax amnesty programme for eligible taxpayers with unpaid liabilities on certain tax types that were due before 30 June 2025. The amnesty programme will be available between 1 December 2025 and 15 February 2026. The amnesty programme will provide a waiver of penalties, as well as interest exceeding 50% of the applicable interest, which is calculated on unpaid or over-paid taxes administered by the New Hampshire Department of Revenue Administration (RSA 21-J:28) on the date of payment for the tax period.

[NH - House Bill 2]

Philadelphia tax policy update

Philadelphia has introduced a gradual reduction in the Business Income and Receipts Tax (BIRT) rates, effective from the 2025 tax year through 2038. Businesses must pay an annual tax based on two components: a) Receipts Tax, which is a millage (mills) rate applied to each dollar of annual receipts, and b) Net Income Tax, which is a percentage rate applied to net income. However, regulated industries (refers to public utilities, financial institutions, insurance companies and other entities that are subject to state or federal regulation regarding their rates or services) pay only the receipts tax, capped at a percentage of net income, which is 5.81% (for 2024) and 5.71% (for 2025). Under this change, the threshold of business receipts to determine the tax rate will gradually decrease from 1.415 mills (receipt rates in mills) in 2024 to zero by 2038 and thereafter. Similarly, the net income tax rate will be reduced from 5.81% in 2024 to 2.80% in 2038 and thereafter.

In addition to these rate changes, the city of Philadelphia's Department of Revenue has issued a key policy clarification for businesses that will be filing and paying BIRT for the first time in tax year 2025. Previously, businesses with less than USD 100,000 in Philadelphia sales were exempt from BIRT filing and payment. However, beginning in 2025, this exemption will no longer be applicable, and all businesses, regardless of their sales volume, will be required to file and pay BIRT if they have taxable activity in the city.

For software companies, the Department of Revenue has clarified that the market-based sourcing rule will apply when determining the source of receipts. In accordance with Section 408(8) of the Business Privilege Tax Regulations, the location where the customer receives the benefit of the product or service will be considered the source of the receipt

[Bill No. 250199]

Illinois budget amends Income tax and Sales and Use tax provisions

Illinois has enacted significant tax changes under Public Act 104-0006 (HB 2755), which impact both income and sales and use taxes. Effective for tax years ending on or after 31 December 2025, the state will adopt the Finnigan method for combined apportionment. The legislation eliminates two key exceptions to the addback rule for related-party interest and intangible expenses. It requires interest deductions under IRC §163(j) to be allocated first to the US members and then to foreign members. The GILTI deduction is capped at 50%, regardless of foreign ownership percentage. Capital gains from the sales of pass-through entity interests (excluding investment partnerships) will be sourced to Illinois based on a three-year average apportionment factor.

For sales and use tax, effective from 1 January 2026, remote sellers will be subject to the Illinois tax based on gross receipts of USD100,000 or more. The Levelling the Playing Field Act is expanded to include service providers, making them subject to both state and local taxes. The legislation introduced the default 15% tax rate for undocumented delivery locations and new rules for marketplace service taxation and service occupation tax elections.

[HB 2755]

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