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The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010—Business Income Tax Provisions

To Our Clients and Friends:

On December 17, 2010 President Obama signed *The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010* (H.R. 4853—the 2010 Tax Relief Act). The 2010 Tax Relief Act extends for two years the so called Bush-era tax rate cuts, provides significant estate tax relief, and includes a two-year AMT “patch.” However, it also contains a trove of other tax breaks for businesses and individuals, including a 100% first-year bonus depreciation for qualifying new business property, a payroll / self-employment tax cut of two percentage points for 2011 only for employees and self-employed individuals, and a host of “extenders” for businesses and individuals.

Here is an overview of the more significant business tax provisions of the 2010 Tax Relief Act.

Section 179 Expensing and 100% Bonus Depreciation

By far the most attractive business incentive in the 2010 Tax Relief Act is the provision that allows taxpayers to deduct, as “bonus” depreciation under IRC §168, 100% of the cost of qualifying new business property acquired after September 8, 2010 and before January 1, 2012, and placed in service before January 1, 2012 (or before January 1, 2013, in the case of certain property).

The 2010 Tax Relief Act also continues the 2010 expensing limitation under IRC §179 at \$500,000 for qualifying new or used business property acquired in 2011 with a phase-out threshold amount of \$2,000,000 for 2011, and at \$125,000 in 2012 with a phase-out threshold amount of \$500,000 for 2012. The 2010 tax Relief Act would then reduce these amounts to \$25,000 and \$200,000 for tax years beginning after 2012.

The combination of expensing under IRC §179 and bonus depreciation under IRC §168 has worked well in recent years to stimulate investment in qualifying new and used business property. Here is a summary of the rules for the two sections for 2007 through 2012.

	2007	2008	2009	2010	2011	2012
Section 179 expensing election:						
Annual limit	\$ 125,000	\$ 250,000	\$ 250,000	\$ 500,000	\$ 500,000	\$ 125,000
Threshold for phase-out	500,000	800,000	800,000	2,000,000	2,000,000	500,000
Qualifying property	New/Used	New/Used	New/Used	New/Used	New/Used	New/Used
Section 168 bonus depreciation:						
Annual % of bonus depreciation	NA	50%	50%	50%/100%	100%	NA
Qualifying property	NA	New	New	New	New	NA

For both expensing (IRC §179) and bonus depreciation (IRC §168) purposes, qualifying property generally includes tangible personal property like machinery, equipment, furniture, etc.

The expensing election (if elected) is taken first, then bonus depreciation (unless opting out), and finally MACRS depreciation. Here are some illustrative examples using 2011 rules, assuming in each case that the taxable income limitation under IRC §179 does not apply:

	A	B	C	D
Assumed acquisitions in 2011:				
Cost of new property acquired	\$ 750,000	\$ 0	\$ 4,000,000	\$ 10,000,000
Cost of used property acquired	1,250,000	2,400,000	6,000,000	0
Total property acquired	\$ 2,000,000	\$ 2,400,000	\$ 10,000,000	\$ 10,000,000
Section 179 expensing election:				
Annual limit imposed by code section	\$ 500,000	\$ 500,000	\$ 500,000	\$ 500,000
Threshold for phase-out	2,000,000	2,000,000	2,000,000	2,000,000
Qualifying property (new or used)	500,000	100,000	Phased out	Phased out
Section 168 bonus depreciation:				
Annual % of bonus depreciation	100%	100%	100%	100%
Qualifying property (new only)	\$ 750,000	\$ 0	\$ 4,000,000	\$ 10,000,000
Claimed in 2011:				
Section 179	\$ 500,000	\$ 100,000	\$ 0	\$ 0
Section 168	750,000	0	4,000,000	10,000,000
Total	\$ 1,250,000	\$ 100,000	\$ 4,000,000	\$ 10,000,000

- A. The Section 179 deduction is limited to \$500,000 by law and the Section 168 deduction is limited to \$750,000—the amount of new equipment acquired.
- B. The Section 179 deduction is phased down to \$100,000 by law and the Section 168 deduction is limited to \$0—the amount of new equipment acquired.
- C. The Section 179 deduction is phased down to zero by law and the Section 168 deduction is limited to \$4,000,000—the amount of new equipment acquired.
- D. The Section 179 deduction is phased down to zero by law and the Section 168 deduction is limited to \$10,000,000—the amount of new equipment acquired.

The 2010 tax Relief Act also extends the election to accelerate AMT credits in lieu of bonus depreciation through 2012, although property manufactured, constructed or produced during 2010 would not be eligible for this election.

Extension of Expired Provisions

A variety of temporary tax provisions, often referred to as “extenders,” expired at the end of 2009 and more were scheduled to expire at the end of 2010. These expired or expiring provisions of the 2010 Tax Relief Act include tax credits, deductions and various tax incentives. See our separate letter summarizing the extenders applicable to individuals.

Gain exclusion

The 2010 Tax Relief Act extends a provision of the Small Business Jobs Act of 2010 and provides for a 100% exclusion under IRC §1202 of gain from the sale of certain small business stock acquired at certain dates through 2011 and held for five years. The gain exclusion was

previously 50% and then 75% depending on the year of purchase of the qualifying small business stock.

Tax Credits

The following business tax credits were also extended through 2011 by the 2010 Tax Relief Act:

- IRC §25C tax credit for non-business energy property (which would also be returned to the limitations and standards applicable before amendment by the American Recovery and Reinvestment Act of 2009, PL 111-5);
- IRC §30C alternative fuel vehicle refueling property tax credit;
- IRC §40 tax credit for alcohol used as fuel;
- IRC §40A tax credit for biodiesel and renewable diesel fuel;
- IRC §41 research and experimental tax credit
- IRC §45(d)(8) tax credit for refined coal facilities;
- IRC §45A Indian employment tax credit;
- IRC §45D new markets tax credit;
- IRC §45G tax credit for certain railroad track expenditures;
- IRC §45N mine rescue team training tax credit;
- IRC §45P employer wage tax credit for active duty members of the uniformed services;
- IRC §51 work opportunity tax credit;
- IRC §54E qualified zone academy bonds (but not the Section 1397E tax credit for holders of qualified zone academy bonds, and the Section 6431 refundable tax credit is repealed);
- IRC § 6426 and 6427 excise tax credits for alternative fuels; and American Samoa economic development credit under the Tax Relief and Health Care Act of 2006.

Of the above extended credits, the IRC §41 research and experimental tax credit is the most significant extender, because it provides a substantial credit for qualifying research activities. The definition of what qualifies as a research activity is broad.

Deductions

The following expired or expiring business deductions were also extended through 2011 by the 2010 Tax Relief Act:

- IRC §168(e)(3)(E) 15-year straight-line cost recovery for qualified leasehold improvements and for qualified restaurant improvements;
- IRC §168(i)(15)(D) seven-year cost recovery period for motor sports entertainment complexes;
- IRC §168(j) accelerated depreciation for property on Indian reservations;
- IRC §170(e)(3)(C) enhanced deduction for contributions of food inventory;
- IRC §170(e)(3)(D) enhanced deduction for contributions of book inventory to public schools;
- IRC §170(e)(6) enhanced deduction for corporate contributions of computer equipment for educational purposes;
- IRC §179E(g) election to expense advanced mine safety equipment;
- IRC §181(f) expensing treatment for certain film and television productions;

- IRC §198(h) expensing of environmental remediation costs;
- IRC §199(d)(8) deduction for income attributable to domestic production activities in Puerto Rico; and
- IRC §1367(a)(2) basis adjustment to stock of S corporations making contributions to charity.

Other Extended Provisions

Other less common expired or expiring business provisions that were extended through 2011 by the 2010 Tax Relief Act, include:

- IRC §132 parity for exclusion from income for employer-provided mass transit passes and parking benefits;
- IRC §168(n) expensing and special depreciation allowance for qualified disaster assistance property (extended through 2012);
- IRC §451 special rule for sales or dispositions to implement FERC or state electric restructuring policy for qualified electric utilities;
- IRC §512(b)(13) special rules for certain amounts received by tax-exempt organizations from controlled entities;
- IRC §613A(c) suspension of limitation on percentage depletion for oil and gas from marginal wells;
- IRC §871(k) treatment of regulated investment company dividends and assets;
- IRC §897(h) qualified investment entity treatment of regulated investment companies under the Foreign Investment Tax Act;
- IRC §953(e) and 954(h) exceptions for active financing income;
- IRC §954(c) look-through treatment of payments between related controlled foreign corporations;
- IRC §2105(d) look-through of certain regulated investment company stock in determining gross estate of nonresidents;
- IRC §1367(a) basis adjustment to stock of S corporations making charitable contributions of property;
- IRC §1391 empowerment zone incentives;
- IRC §1400, 1400A and 1400B District of Columbia Enterprise Zone incentives;
- IRC §1400L(b) New York Liberty Zone bonus depreciation;
- IRC §1400N Gulf Opportunity Zone incentives; and
- IRC §7652(f) “cover over” of tax on distilled spirits to Puerto Rico and the U.S. Virgin Islands; and
- Grants under the American Recovery and Reinvestment Act of 2009 for specified energy property in lieu of tax credits.

Circular 230 disclosure:

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