MP&S Tax Alert: American Taxpayer Relief Act Will Save Taxes for Many Businesses

The American Taxpayer Relief Act of 2012 (ATRA) extends and enhances many breaks for businesses. In particular, it provides incentives for businesses to invest in assets, research and people. This article provides an overview of ATRA's most important changes for businesses, along with the implications for 2012 tax returns and tax planning for 2013 and beyond.

Bonus Depreciation

ATRA extends 50% bonus depreciation — an additional first-year depreciation allowance — generally through 2013. Qualified assets include *new* tangible property with a recovery period of 20 years or less (such as office furniture and equipment), off-the-shelf computer software, water utility property and qualified leasehold improvement property.

ATRA also extends the provision allowing corporations to accelerate certain credits in lieu of claiming bonus depreciation for qualified assets placed in service through Dec. 31, 2013 (Dec. 31, 2014, for certain long-lived and transportation property).

Be sure to consider whether you made any asset purchases that might qualify for 50% bonus depreciation on your 2012 tax return. Also, if you are anticipating major asset purchases in the next year or two, you may want to time them so you can benefit from 50% bonus depreciation. However, you should also consider whether you qualify for Section 179 expensing (discussed immediately below), which may provide a greater tax benefit.

Sec. 179 Expensing

Sec. 179 is another tax law provision that encourages investment. It allows smaller businesses to immediately write off the full price of qualifying asset purchases rather than depreciating them over several years. The deduction is reduced by $1 for every $1 of expenses in excess of a phaseout threshold, which is why this tax break primarily benefits smaller businesses. The expensing election can be claimed only to offset net income, not to reduce net income below zero.

Before ATRA, the Sec. 179 expensing limit for 2012 was $125,000, with a phaseout threshold of $500,000 — and these amounts were scheduled to drop to $25,000 and $200,000, respectively, for 2013. ATRA increases these amounts for assets placed in service in both years to $500,000 and $2 million, respectively (the same amounts that applied in 2010 and 2011).

If you are eligible for full Sec. 179 expensing, it may provide a greater benefit than bonus depreciation because it can allow you to deduct 100% of an asset acquisition's cost. Additionally, only Sec. 179 expensing is available for *used* property. However, bonus depreciation may benefit more taxpayers than Sec. 179 expensing, because it is not subject to any asset purchase limit or net income requirement. You will also want to consider state tax consequences.

Leasehold-Improvement, Restaurant and Retail-Improvement Property

For 2009 through 2011, accelerated depreciation was available for qualified leasehold-improvement, restaurant and retail-improvement property. ATRA extends it to 2012 and 2013. Specifically, the provision allows a shortened recovery period of 15 years — rather than 39 years — for such property.

Consider whether you made asset purchases that might qualify for accelerated depreciation on your 2012 tax return. In addition, if you're thinking about making such investments in the future, you may want to do so in 2013 to ensure you can take advantage of this break if it's not extended again.

Research Credit

For many years, the research credit (also commonly referred to as the "research and development" or "research and experimentation" credit) has provided an incentive for businesses to increase their investments in research. However, the credit expired at the end of 2011.

ATRA extends the credit to 2012 and 2013. The credit is generally equal to a portion of qualified research expenses. It's complicated to calculate, but the tax savings can be substantial. (Please contact your MP&S tax advisor if you would like further information on the calculation of this credit).

Work Opportunity Credit

The Work Opportunity credit, designed to encourage hiring from certain disadvantaged groups, expired Dec. 31, 2011, for most groups. An expanded credit for qualifying veterans expired Dec. 31, 2012. ATRA extends the credit for most eligible groups through 2013.

Examples of disadvantaged groups for purposes of the credit include food stamp recipients, ex-felons and nondisabled veterans who've been unemployed for four weeks or more, but less than six months. For these groups, the credit generally equals 40% of the first $6,000 of wages paid to qualifying employees, for a maximum credit of $2,400. A larger credit of up to $4,800 is generally available for hiring disabled veterans. Additionally, if you're hiring veterans who've been unemployed for six months or more in the preceding year, the maximum credits are even greater:

- $5,600 for *non*disabled veterans, and
- $9,600 for disabled veterans.

If you're considering making new hires, and workers from one or more of these disadvantaged groups might meet your needs, making the hires before the end of 2013 may be beneficial from a tax perspective. Also, be sure to check to see if you qualify for the credit on your 2012 tax return.

Transit Benefits

Some fringe benefits are not included in an employee's wages for income and payroll tax purposes, yet the employer is still allowed to deduct them. Generally, the maximum transit benefit that could receive such treatment has been higher for parking than for van-pooling and mass transit.

Tax legislation in 2009, however, provided for the limits to be equal through 2010. Legislation in 2010 extended this parity through 2011. ATRA has extended it through 2013. For 2012 and 2013, the limits are both now $240 per month, though there's been some discussion about increasing the 2013 amount. If you offer transit benefits, keep parity in mind for your 2013 program.

Flow-Through Entities

ATRA does have a downside for businesses structured as flow-through entities: Because their income flows through to the owners' tax returns, entities such as partnerships, limited liability companies (LLCs) and S corporations will in a sense be affected by ATRA's changes to ordinary-income tax rates for individuals. Consequently, if you're the owner of such an entity and will face the higher maximum 39.6% rate, traditional income and deduction timing strategies may help you minimize the impact, or at least defer taxes.

In certain circumstances, consideration can also be given to converting a flow-through entity business to a C corporation because the top corporate rate remains at 35%. However, there are many other tax and nontax consequences of such a conversion, so it's important to discuss the impact with your MP&S tax advisor as well as your attorney before implementing such a change.

Which Breaks Will Benefit your Business?

ATRA also extends many other business tax breaks that are too limited in applicability to cover here but that can provide significant benefits to the taxpayers who qualify for them. Please contact us to learn which ATRA breaks may apply to you.

MP&S TAX PLANING GUIDE

To facilitate ongoing access to the latest tax rules and regulations, MP&S offers an online tax guide that is updated on an ongoing basis.

FOR MORE INFORMATION

If you have questions about anything you read in this Alert or in the MP&S tax guide, please contact a MP&S tax advisor or Steven Eliach, JD, LLM, the Principal-in-Charge of the MP&S Tax Practice, by phone at 212.503.6388 or by email at seliach@markspaneth.com.