Franzen & Franzen, LLP
Certified Public Accountants

September 16, 2013 – Expiring Business Tax Provisions

The following highlights business tax provisions that are scheduled to expire.

Expiring Business Tax Provisions

Additional first-year "bonus" depreciation. Congress has consistently extended this provision allowing businesses to take an additional depreciation deduction for the cost of qualified property placed in service in a certain year on top of the property's original depreciation allowance. The amount of this bonus depreciation has changed, however. For example, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, P.L. 111-312, extended 50-percent bonus depreciation and expanded it to 100 percent of the cost for qualified property acquired and placed into service between September 8, 2010, and January 1, 2012. Following January 1, 2012, the amount dropped again to 50 percent. The 2012 Taxpayer Relief Act extended 50-percent bonus depreciation through the end of 2013.

Increased expensing limits for Code Sec. 179 property. The 2012 Taxpayer Relief Act extended through 2013 enhanced Code Sec. 179 small-business expensing. The Code Sec. 179 dollar limit for tax years 2012 and 2013 is $500,000 with a $2-million investment limit, meaning businesses can take a deduction for costs up to $500,000, until the cost of the property exceeds $2 million. At that point, the $500,000 deduction would begin to phase out.

Generally, expensing under Code Sec. 179 and bonus depreciation have enjoyed broad bipartisan support and have been extended, even though the additional amount of depreciation or the Code Sec. 179 dollar and investment limits often change. Several bills have been introduced to extend and/or enhance Code Sec. 179 expensing. Similarly, bills have been introduced that call for extension of bonus depreciation.

The overall economic benefit of both bonus depreciation and Code Sec. 179 expensing has been called into question by numerous studies, according to several 2013 reports by the Congressional Research Service (CRS). For example, a July CRS report stated that the cost of extending the partial expensing of investment property and Code Sec. 179 expensing would exceed more than $346 billion over the 10-year period between 2014 and 2023. However, a February CRS report indicated that the expensing allowance and bonus-depreciation deductions likely have only a minor effect on increasing business investment. With the cost high and the benefits in question, the fate of bonus depreciation and Code Sec. 179 expensing could be uncertain as Congress continues to discuss comprehensive tax reform.

15-year straight-line cost recovery for qualified leasehold, restaurant, and retail improvements. The 2012 Taxpayer Relief Act extended, through 2013, the 15-year recovery period for qualified leasehold improvements, qualified retail improvements, and qualified restaurant property.

125 E. De La Guerra St., Ste. 201, Santa Barbara, CA 93101 Phone: 805.563.0821

Pending legislation, if passed by Congress, would permanently extend the 15-year recovery period for this class of property.

Work opportunity tax credit. The 2012 Taxpayer Relief Act extended the work opportunity tax credit through 2013. The credit rewards employers that hire individuals from targeted groups. Employers hiring an individual within a targeted group (generally, otherwise hard-to-employ workers) are eligible for a credit generally equal to 40 percent of first-year wages up to $6,000, higher in the case of some qualified veterans.

Soon after the 2012 Taxpayer Relief Act was passed, Senate Finance Committee Chair Max Baucus, D-Mont., introduced legislation proposing the permanent extension of work opportunity tax credit, along with an expansion of the credit to encourage employers to hire recently discharged veterans.

Research tax credit. The Code Sec. 41 research credit may be claimed for increases in business-related qualified research expenditures, and for increases in payments to universities and other qualified organizations for basic research. The credit applies to the excess of qualified research expenditures for the tax year over the average annual qualified research expenditures measured over the four preceding years. The credit expired after 2011, but the 2012 Taxpayer Relief Act retroactively extended it through 2013.

The research tax credit enjoys significant bipartisan support in Congress. President Obama has also called for making permanent the credit. One obstacle to extension is its cost, which the Joint Committee on Taxation has estimated to be $14.3 billion over 10 years.

Reduced recognition period for S corporation built-in gains tax. In general, an S corporation shareholder is not subject to tax on corporate distributions. However, if a C corporation converts to an S corporation and then liquidates, the built-in-gains tax provisions under Code Sec. 1374 are designed to prevent that C corporation from avoiding payment of a corporate-level tax on its distributions made during a recognition period. The recognition period was originally 10 years, but was reduced to seven years and then five years by various pieces of legislation. The 2012 Taxpayer Relief Act temporarily extended the five-year recognition period.

This would mean, for example, that a C corporation that had converted to an S corporation in 2007 can make distributions in 2013 without having them become subject to the built-in gains tax.

House Ways and Means Committee Chair Dave Camp, R-Mich., proposed two options for business taxation in his third discussion draft on tax reform, which he released in March 2013. The first option, which was less radical because it did not propose a complete rewrite of the current business tax structure, included a five-year recognition period for built-in gains. Pending legislation in Congress would also permanently extend the five-year recognition period.

More Expiring Incentives

A number of other business tax incentives are scheduled to expire after 2013. These include, among others:

- Employer wage credit for activated military reservists;
- Special rules for qualified small business stock;

- Treatment of certain regulated investment company (RIC) dividends;
- Accelerated depreciation for business property on Indian reservations;
- Railroad track maintenance credit;
- Low-income housing tax credit rate;
- Code Sec. 199 deduction for Puerto Rico;
- Indian employment tax credit;
- Seven-year recovery for motorsports entertainment complexes;
- Credit for new energy efficient homes;
- Incentives for biodiesel, renewable diesel and alternative fuels;
- Election to expense advance mine safety equipment;
- Energy efficient appliance credit for manufacturers;
- American Samoa economic development credit;
- Mine rescue team training credit; and
- Special expending rules for costs of film and television productions.

Please give our office a call if you have any questions, or if you'd like to discuss further.