



RECOVERY ACT CONTAINS MANY TAX BREAKS FOR BUSINESSES

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This first article in a three part series highlights the tax benefits provided by The American Recovery and Reinvestment Act of 2009.

Signed into law by President Obama on February 17, 2009, the American Recovery and Reinvestment Act of 2009 contains sweeping changes to the nation's tax laws. Those changes related businesses include:

- Larger Cost Recovery Deductions
- Relief for Financially Troubled Businesses
- Tax Cuts and Credits Related to Small Businesses

Deductions

The Recovery Act allows businesses to deduct the cost of assets purchased for use in a business. It provides a bonus depreciation deduction, allowing businesses to deduct 50% of the cost of most property (other than buildings and real estate) that is first used in 2009.

For example, in 2009 Business X purchases an asset for \$1 million that normally depreciates over five years. The Recovery Act entitles Business X to a \$500,000 bonus deduction in addition to the normal depreciation deduction of \$100,000 for the 2009 tax year. It then deducts the remaining \$400,000 paid over the following four years.

Another provision in the Recovery Act dealing with deductions increases the limits of annual expense deductions for a wide array of assets with values ranging from \$133,000 to \$250,000 in order to help small businesses more quickly recover the cost of these assets. It allows certain businesses the choice to exchange bonus and accelerated depreciation for previously unused tax credits from prior tax years.

The Recovery Act also makes it easier for businesses to deduct the cost of automobiles by increasing the first year depreciation deduction from \$2,960 to \$10,960 for cars and from \$3,160 to \$11,160 for trucks.



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Financially Troubled Businesses

The Recovery Act allows financially troubled businesses an increased ability to deduct losses. A business with deductions in excess of income generates a net operating loss. Under pre-Recovery Act law, such losses could be carried back and used to offset tax liability for the two preceding tax years. The Recovery Act allows certain small businesses the option to carry losses incurred in 2008 back for up to five years. Consequently, many businesses will generate a refund for taxes paid in prior years.

The Recovery Act also provides tax relief for businesses that are able to renegotiate their debt. Normally, a business with forgiven debt realizes taxable income equal to the amount of the forgiveness. For example, if a business owes \$1 million and the lender agrees to reduce the loan amount to \$500,000, the business will have taxable income of \$500,000. The Recovery Act allows businesses to defer paying tax on that income and then pay the tax in installments over five years. So, if the debt restructuring occurs in 2009, the business can wait until 2014 to begin reporting the income and paying tax. The business then pays the tax in five annual installments beginning with its 2014 tax return.

Tax Cuts and Credits Related to Small Businesses

The Recovery Act substantially reduces tax on the sale of stock in a small business corporation. Under pre-Recovery Act law, individual shareholders could exclude 50% of the gain realized on the sale of stock in a small business that meets certain requirements. The Recovery Act allows taxpayers to exclude 75% of such gain.

The Recovery Act also loosens the requirements for making quarterly estimated tax payments for individuals who are small business owners. Under the Recovery Act, estimated payments and other tax withholdings must equal or exceed 90% of the tax liability shown on the individual's return for the preceding year. Under prior law, to avoid penalties, such payments needed to exceed 110% of the prior year's tax return in some cases.

Aimed at job creation, the Recovery Act allows businesses a tax credit for first year wages paid to certain veterans and individuals between the ages of 16 and 25 who are not in school and have not been employed for the preceding six months.

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