American Recovery and Reinvestment Act of 2009

The American Recovery and Reinvestment Act (the "Recovery Act") was signed in to law on February 17, 2009. Designed to stimulate a lagging economy, the provisions written directly for taxpayers provide new tax benefits for both businesses and individuals alongside extensions of key tax benefits originally set to sunset in 2009.

Business Impact – tax breaks and benefits

Small businesses may elect longer NOL carryback period.

In general, net operating losses (NOLs) may be carried back two years and forward 20 years (different rules apply for certain specialized types of losses).

For NOLs arising in a tax year beginning or ending in 2008 and 2009, the Recovery Act permits small businesses to elect to increase the NOL carryback period from two years to three, four, or five years. A small business for this purpose is a trade or business whose average annual gross receipts are $15 million or less for the three tax year period (or shorter period of existence) ending with the tax year before the year in which the loss arose. The longer NOL carryback period gives small businesses that experienced losses the ability to get refunds of income taxes paid in earlier years.

Reduced estimated taxes in 2009 for individuals with small businesses.

To the extent that tax isn't collected through withholding, taxpayers generally must make quarterly estimated payments of the "required annual payment." The required annual payment is the lesser of: (1) 90% of the tax shown on the return or (2) 100% of the tax shown on the preceding year's return (110% if adjusted gross income (AGI) for the preceding year exceeded $150,000).

The Recovery Act provides that in 2009, individuals whose AGI on the preceding year's return is less than $500,000 ($250,000 if married filing separately) and who generated at least 50% of the gross income shown on the previous year's return from a small trade or business (one that employed no more than 500 people, on average) qualify for reduced estimated tax payments. The payment for qualifying individuals is the lesser of (1) 90% of the tax shown on the return for the tax year, or (2) 90% of the tax shown for the preceding tax year.

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Liberal expensing limits continued for another year.

The Recovery Act gives a one-year lease on life to enhanced expensing rules, which allow qualifying businesses the option to currently deduct the cost of business machinery and equipment, instead of recovering its cost via depreciation over a number of years.

For tax years beginning in 2009, the maximum amount that a business may expense is $250,000, and the expensing election begins to phase out when a business buys more than $800,000 of expensing-eligible assets. These dollar limits are the same as those that were in effect for 2008. Had the Recovery Act not been passed and signed into law, the dollar limits would have dropped this year to $133,000 and $530,000 respectively.

Bonus first year depreciation extended for another year.

Bonus depreciation was scheduled to sunset for most assets placed in service after 2008. Fortunately, the Recovery Act extends for another year the ability for businesses to take an extra “bonus” depreciation deduction for the first year new assets are placed in service.

The bonus first-year depreciation deduction generally equals 50% of the cost of qualified property (most types of tangible property other than buildings and their structural components, improvements to certain types of leased property, and most software) acquired and placed in service during 2009. Certain types of property with a long life, and certain types of aircraft, may be placed in service before Jan. 1, 2011, and still qualify for the 50% bonus first year depreciation allowance. Also, note that the otherwise allowable first-year depreciation deduction for business autos first placed in service in 2009 is increased by $8,000 in the Recovery Act.

Extended election to speed up recognition of accumulated AMT and R&D credits instead of claiming bonus depreciation.

Corporations not in position to take advantage of bonus depreciation may have instead benefited from 2008’s law allowing accelerated recognition of part of their accumulated pre-2006 research tax credits or certain alternative minimum tax credits.

The Recovery Act extends this election so that it is available for property placed in service in 2009 (or 2010 for certain longer lived assets). Please note that this alternative choice is highly specialized and requires a detailed analysis of a corporation's tax situation.

Deferred tax on debt forgiveness income when debt is repurchased.

A business generally will wind up with debt discharge income if it repurchases its debt for less than the outstanding amount of the debt. For debt that's repurchased in 2009 or 2010, the Recovery Act permits the tax that's owed on such debt discharge income to be paid over five years, beginning with 2014.

S corporation built-in gain holding period shortened temporarily.

An S corporation generally is not subject to tax; instead, it passes through its income or loss items to its shareholders, who pay tax on their pro-rata shares of the S corporation's income. However, if a business that was formed as a C corporation elects to become an S corporation, the S corporation is taxed at the highest corporate rate (currently 35%) on all gains that were “built-in” at the time of the election if the gains are recognized during a “holding period” defines as the first ten S corporation years. (Similar rules apply if an S corporation receives property from a C corporation in certain nontaxable transfers.)

The Recovery Act shortens the holding period to seven year for tax years beginning in 2009 and 2010.

Bigger exclusion for sale of qualified small business stock.

Before the Recovery Act, individuals could exclude 50% of their gain on the sale of qualified small business stock (QSBS) held for at least five years (60% for certain empowerment zone businesses). To qualify, a QSBS must meet a number of conditions (e.g., its gross assets can't exceed $50 million and it must meet active business requirements).

Under the Recovery Act, the percentage exclusion for QSBS sold by an individual increases to 75% for stock acquired after Feb. 17, 2009 and before Jan. 1, 2011.

More workers eligible for work opportunity tax credit (WOTC).

Employers that hire workers from one or more targeted groups (e.g., long term family assistance recipients) can claim a tax credit that varies with the type of person hired. For individuals beginning work for the employer after Dec. 31, 2008, the Recovery Act creates a new targeted group for the WOTC, consisting of unemployed veterans and disconnected youth who begin work for the employer in 2009 or 2010.

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Individual Impact – new tax benefits for qualifying taxpayers

Expanded credit for first-time home buyers.

Last year, Congress provided taxpayers with a refundable tax credit that was equivalent to an interest-free loan equal to 10% of the purchase of a home (up to $7,500) by first-time home buyers. The provision applied to homes purchased on or after April 9, 2008 and before July 1, 2009. Taxpayers receiving this tax credit were required to repay any amount received under this provision back to the government over 15 years in equal installments (or earlier if the home was sold). The credit phases out for taxpayers with AGI in excess of $75,000 ($150,000 in the case of a joint return).

The Recovery Act enhances the credit by eliminating the repayment obligation for taxpayers that purchase homes on or after January 1, 2009. It also extends the credit through the end of November 2009, and bumps up the maximum value of the credit from $7,500 to $8,000.

Tax break for new car purchasers.

The Recovery Act allows taxpayers to deduct state and local sales taxes paid on the purchase of a new automobile, including light trucks, SUVs, motorcycles and motor homes. The tax break phases out starting with taxpayers earning $125,000 per year ($250,000 for joint returns). The deduction is allowed to those who itemize their deductions as well as to non-itemizers. However, the deduction cannot be taken by a taxpayer who elects to deduct state and local sales taxes in lieu of state and local income taxes.

Alternative minimum tax (AMT) patch.

To hold the number of taxpayers subject to the AMT at bay, the Recovery Act increases the AMT exemption amounts for 2009 to $46,700 for unmarried individuals, to $70,950 for joint returns, and to $35,475 for married individuals filing separate returns.

The Recovery Act also provides some relief by extending the AMT income range over which the exemptions phase out. In 2009, the range is $112,500 t0 $299,300 for unmarried individuals, $150,000 to $433,800 for joint returns and $75,000 to $216,900 for married individuals filing separate returns.

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Economic recovery payment.

The Recovery Act provides for a one-time payment of $250 to retirees, disabled individuals and Social Security beneficiaries and SSI recipients receiving benefits from the Social Security Administration and Railroad Retirement beneficiaries, and to veterans receiving disability compensation and pension benefits from the U.S. Department of Veterans' Affairs. The one-time payment is a reduction to any allowable Making Work Pay credit.

Refundable credit for certain federal and state pensioners.

The new law provides a one-time refundable tax credit of $250 in 2009 to certain government retirees who are not eligible for Social Security benefits. This one-time credit is a reduction to any allowable Making Work Pay credit.

"Making Work Pay" credit.

The Recovery Act provides an individual tax credit in the amount of 6.2% of earned income not to exceed $400 for single returns and $800 for joint returns in 2009 and 2010. The credit is phased out at adjusted gross income (AGI) in excess of $75,000 ($150,000 for married couples filing jointly). The credit can be claimed as a reduction in the amount of income tax that is withheld from a paycheck or through a credit on a tax return. Under the credit, workers can expect to see perhaps $13 a week less withheld from their paychecks starting around June. In 2010, the credit will decrease to approximately $7.70 per week.

Unemployment compensation exclusion.

A provision in the Recovery Act temporarily suspends federal income tax on the first $2,400 of unemployment benefits received by a recipient in 2009.

Expanded earned income tax credit.

The Recovery Act provides tax relief to families with three or more children and increases marriage penalty relief. The changes apply for 2009 and 2010.

Expanded child tax credit.

The Recovery Act increases the eligibility for the refundable child tax credit in 2009 and 2010 by lowering the earned income threshold to $3,000 (from $8,500 in 2008).

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Expanded and revised higher education tax credit.

The Recovery Act creates a $2,500 higher education tax credit that is available for the first four years of college. The credit is based on 100% of the first $2,000 of tuition and related expenses (including books) paid during the tax year and 25% of the next $2,000 of tuition and related expenses paid during the tax year, subject to a phase-out for AGI in excess of $80,000 ($160,000 for married couples filing jointly). 40% of the credit is refundable. The new credit temporarily replaces the Hope credit.

Computers as an education expense.

The Recovery Act permits computers and computer technology to qualify as qualified education expenses in 529 education plans for tax years beginning in 2009 and 2010.

(end Recovery Act – Individual Impact)

Energy Projects

In addition to the Recovery Act tax reductions and extension provision, the Recovery Act also includes a package of tax incentives specifically designed to encourage investments in renewable energy projects or more-efficient technologies by both individuals and businesses.

Residential energy property.

The Recovery Act removes the dollar limitations on certain energy credits, e.g., for qualified solar water heating property ($2,000 cap); for qualified small wind energy property ($4,000 cap); and qualified geothermal heat pumps ($2,000).

Energy-efficient existing homes.

The Recovery Act extends the tax credit for improvements to energy-efficient existing homes through 2010. For 2009 and 2010, the amount of the tax credit is increased from 10% to 30% of the amount paid or incurred by the taxpayer for qualified energy efficiency improvements during the tax year. The property-by-property dollar caps on the tax credit are also eliminated, and an aggregate $1,500 cap applies to all property qualifying for the credit.

Vehicles.

The Recovery Act provides a tax credit for purchases of plug-in electric drive vehicles ranging from $2,500 to $7,500 depending on battery capacity. The new law also restores and updates the electric vehicle credit for plug-in electric vehicles that would not otherwise qualify for the larger plug-in electric drive vehicle credit and provides a tax credit for plug-in electric drive conversion kits.

Long-term extension and modification of renewable energy production tax credit.

The Recovery Act extends the placed-in-service date for wind facilities for three years (through December 31, 2012). It also extends the placed-in-service date through December 31, 2013 for certain other qualifying facilities: closed-loop biomass; open-loop biomass; geothermal; small irrigation; hydropower; landfill gas; waste-to-energy; and marine renewable facilities.

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Temporary election to claim the investment tax credit in lieu of the production tax credit.

Facilities that produce electricity from solar facilities are eligible to take a 30% investment tax credit in the year the facility is placed in service. Facilities that produce electricity from wind, closed-loop biomass, open-loop biomass, geothermal, small irrigation, hydropower, landfill gas, waste-to-energy, and marine renewable facilities are eligible for a production tax credit, payable over a ten-year period. The Act provides a temporary election to claim the investment tax credit in lieu of the production tax credit.

Business energy credit.

The Recovery Act enhances the business energy credit by eliminating the cap on small wind property and repealing the basis reduction requirement for subsidized energy financing.

Tax credits for alternative fuel pumps.

The Recovery Act provides an increase for 2009 and 2010 in the 30% alternative refueling property credit for businesses (capped at $30,000) to 50% (capped at $50,000).

Credit for investment in advanced energy facilities.

The Recovery Act establishes a new manufacturing investment tax credit for investment in advanced energy facilities, such as facilities that manufacture components for the production of renewable energy, advanced battery technology, and other innovative next-generation green technologies.

More funding for bonds.

The new law authorizes additional funds for new clean renewable energy bonds and qualified energy conservation bonds.

We hope this information is helpful to you and your business. If you would like more information about the details or application of the provisions of the Recovery Act, please contact your Sensiba San Filippo representative or Karen Yang at kyang@ssfllp.com 925.271.8700.