2012 Year-End Tax Planning for Businesses

To all clients and friends of Louis Tommasino CPA, APC,

Recently, end of year tax planning for businesses has been complicated by uncertainty over the future availability of many tax incentives. The 2012 year end is no different. In 2010, Congress extended many business incentives for one or two years. These incentives are about to expire. In addition, many of the "Bush-era" tax cuts are scheduled to sunset at the end of 2012. It is unclear if Congress will provide further extensions as they debate across-the-board spending cuts scheduled to take effect in 2013. In addition, businesses must prepare to comply with healthcare reform. This combination of events provides tax planning considerations unique to 2012 that requires a multi-year strategy taking into account a variety of scenarios and outcomes.

For instance, in recent years, Congress has used bonus depreciation to encourage economic growth. Currently, a special 50-percent first year bonus depreciation allowance is provided for qualified property. This allowance is scheduled to expire after 2012 (2013 in the case of certain longer production period property and certain transportation property). The equipment eligible for bonus depreciation must be placed in service and not merely purchased before the end of the year to be eligible for 2012. Placed-in-service generally requires installation and ready-for use in the business.

Bonus depreciation also relates to vehicle depreciation dollar limits. For 2012, the first-year depreciation allowed for vehicles subject to luxury-vehicle limits is increased by $8,000. Unless the bonus depreciation is extended, 2012 will be the final year in which substantial first-year write-offs for the purchase of a business vehicle may be available.

In addition to bonus depreciation, taxpayers may also take advantage of the generous dollar limitation and investment limitations for Code Sec. 179 expensing. For 2012, the dollar limitation is $139,000 with a $560,000 investment ceiling on the purchase of all otherwise qualifying property. These limitations drop to $25,000 and $200,000, respectively in 2013.

Purchased property may qualify for both Code Sec. 179 expensing and bonus depreciation. Code Sec. 179 expensing should be taken first, followed by bonus depreciation and then regular first-year depreciation. For example, a 2012 purchase of $400,000 in assets that qualify as five-year property would be entitled to a $139,000 Code Sec. 179 deduction, a $130,500 bonus depreciation and a $26,100 regular depreciation deduction assuming a half-year convention.

Repair Regulations

For tax years beginning on or after January 1, 2012, the rules for capitalizing improvements to tangible property are provided as part of a group of regulations known as the "repair regulations." The regulations are broad and far-reaching - they apply to every business taxpayer that uses tangible property, whether owned or leased. Neither the form of entity that operates the business, nor the entity's foreign or domestic status, plays a role in determining their relevance. Manufacturers, wholesalers, distributors, and retailers – are all affected.

In general, these regulations attempt to provide standards for distinguishing repairs from capitalized improvements based on principals developed over the years in court cases and IRS rulings. A change by a taxpayer to conform to the repair regulations is an accounting method change, and a corresponding adjustment is generally required. This adjustment serves to put the taxpayer on the same accounting method for all amounts incurred both prior to and after the effective date of the regulations. Therefore, taxpayers adopting an accounting method change under the capitalization regulations must examine repairs and capitalized expenses for prior years in order to calculate the adjustment.

Taxpayers with an "applicable financial statement," such as a certified audited financial statement, may claim a current deduction for the cost of acquiring items of relatively low-cost property, including materials and supplies, if specific requirements are met. The aggregate cost which may be expensed annually under a taxpayer's expensing policy is subject to a ceiling equal to the greater of .1 percent of gross receipts or 2 percent of total depreciation and amortization reported on the financial statement.

"Bush-era" tax Cuts

The "Bush-era" tax cuts is the collective term for the tax measures enacted in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA). EGTRRA and JGTRRA made over 30 major changes to the Tax Code which are scheduled to sunset at the end of 2012. The following are highlights of the major changes for business and investment in 2013 resulting from the sunset –

- Reduced maximum capital gains rate expires
- Lower capital gain tax rates for qualified five-year gain will be revived
- Exclusion of gain on sale of small business stock treated as AMT preference item will increase
- Taxation of qualified dividends at capital gain rates will no longer apply
- Credit for employer-provided child care facilities and services expire
- Accumulated earnings tax rate increases to 39.6 percent
- Personal holding company tax rate increases to 39.6 percent
- Repeal of collapsible corporation rules expires

Health Care

On June 28, 2012, the U.S. Supreme Court upheld the constitutionality of the Patient Protection and Affordable care Act (PPAC). As part of its primary purpose to facilitate health care reform, the PPAC includes key tax provisions that affect businesses. Many business and employers waited to fully implement these provisions until the Supreme Court determined the fate of the health care reform law. Now, however, businesses must comply with the rules under PPAC.

Although it was optional in 2011, Form W-2 reporting is mandatory for 2012 and thereafter. Employers must disclose the aggregate cost of applicable employer-sponsored coverage provided to employees annually on the employee's Form W-2. Regardless of whether the employee or the employer pays for the coverage, the aggregate cost of the coverage reported is determined under rules similar to those used in determining applicable premiums for purposes of the COBRA continuation coverage requirements of group health plans.

Planning

Many taxpayers are wondering how they may be able to prepare for 2013 and beyond, and what to do before then. The short answer is to quickly become familiar with the expiring tax incentives and what may replace them after 2012, and to plan accordingly. We can help you align traditional year-end techniques with strategies for dealing with uncertainties created by Congress's delay in addressing sunsetting tax rates and the extension of other major tax benefits. Please call our office for an appointment.

Sincerely,

Louis Tommasino

Louis Tommasino CPA