Dear Client:

In recent years, end-of-the-year tax planning for businesses has been complicated by uncertainty over the future availability of many tax incentives. This year is no different. In 2010, Congress extended many business tax incentives for one or two years. Now, those incentives have expired or are scheduled to expire. Whether they will be extended beyond 2012 is unclear as Congress debates the fate of the Bush-era tax cuts and the across-the-board spending cuts scheduled to take effect in 2013. Taxpayers need to be aware of the expiring provisions and explore developing a multiyear tax strategy that takes into account various scenarios for the future of these incentives.

Code Sec. 179 gives businesses the option of claiming a deduction for the cost of qualified property all in its first year of use rather than claiming depreciation over a period of years. The dollar limitation for 2012 is $139,000 with a $560,000 investment ceiling. Under current law, the Code Sec. 179 dollar limit is scheduled to drop to $25,000 for 2013 with a $200,000 investment ceiling.

Businesses should consider accelerating purchases into 2012 to take advantage of the still generous Code Sec. 179 expensing. Qualified property must be tangible personal property, which you actively use in your business, and for which a depreciation deduction would be allowed. As long as you start using your newly purchased business equipment before the end of the tax year, you get the entire expensing deduction for that year.

In July 2012, the Senate voted to increase the Code Sec. 179 dollar amount to $250,000 with an $800,000 investment limitation for tax years beginning after December 31, 2012. The House voted to increase the Code Sec. 179 dollar amount to $100,000 with a $400,000 investment limitation for tax years beginning after December 31, 2012. They have not yet agreed upon a compromise.

Bonus depreciation (50% first-year deduction) is scheduled to expire after 2012. Unlike the Section 179 expense deduction, the bonus depreciation deduction is not limited to smaller companies or capped at a certain dollar level. Qualified property must be depreciable under Modified Accelerated Cost Recovery System (MACRS) and have a recovery period of 20 years or less. The property must be new, not used, and placed in service before January 1, 2013.

Bonus depreciation is limited for each defined "luxury vehicle" to $11,360. Sport utility vehicles and pickup trucks with a gross vehicle weight rating in excess of 6,000 pounds are exempt from the luxury vehicle depreciation caps.

Comprehensive repair and capitalization regulations issued by the IRS in late 2011 may open up planning opportunities. Although many of you have already adopted your own "de minimus" expensing policies, a new de minimis expensing rule has officially been released allowing a taxpayer to deduct certain amounts paid or incurred to acquire or produce a unit of tangible property. In order to qualify for the "de minimus" expensing, the taxpayer must have an Applicable Financial Statement (AFS), written accounting procedures for expensing amounts paid or incurred for such property under certain dollar amounts, and treat the amounts as expenses on its AFS in accordance with its written accounting procedures. An overall ceiling limits the total expenses that a taxpayer may deduct under the de minimis rule.

The de minimis expensing rule applies to amounts paid or incurred (to acquire or produce property) in tax years beginning on or after January 1, 2012. An AFS is a certified audited financial statement that is prepared in accordance with GAAP and is given to creditors and equity holders or used to make significant management decisions. This official ruling is important because it opens the door to more interpretation and flexibility surrounding the capitalization of asset purchases.

Let's look at an example. A taxpayer purchases 10 VoIP phones for its business at $200 each for a total cost of $2,000. Each phone is a unit of property and is not a material or supply. The taxpayer has an AFS and a written policy at the beginning of the tax year to expense amounts paid for property costing less than $500. The taxpayer treats the amounts paid for the phones as an expense on its AFS. Assume further that the total aggregate amount treated as de minimis and not capitalized, including the amounts paid for the phones, are less than or equal to the greater of 0.1 percent of total gross receipts or 2 percent of the taxpayer's total financial statement depreciation. The result: the de minimis rule applies and the taxpayer is not required to capitalize any portion of the $2,000 paid for the 10 phones.

Dividends under current law receive tax-favorable tax rates which are scheduled to expire after 2012. Qualified dividends are eligible for a maximum 15 percent tax rate for taxpayers in the 25 percent and higher brackets; zero percent for taxpayers in the 10 and 15 percent brackets.

If Congress takes no action, qualified dividends will be taxed at the ordinary income tax rates after 2012 (with the highest rate scheduled to be 39.6%). Corporations may want to explore declaring a qualified dividend to shareholders before January 1, 2013.

Expired business tax extenders and incentives

Many temporary business tax incentives expired at the end of 2011 or will expire at the end of 2012. Confronted with the federal budget deficit and across-the-board spending cuts scheduled to take effect in 2013, lawmakers could allow some of the business tax extenders to expire permanently. The 100% exclusion for gain on sale of qualified small business stock, shorter recovery periods for qualified leasehold, restaurant and retail properties, expensing of brownfields remediation costs and the Work Opportunity Tax Credit are some of the bigger incentives that may disappear. Certain extenders, however, have bipartisan support, and are likely to be extended, especially the research tax credit.

Small employer health insurance credit is available through 2015. Employers with 10 or fewer full-time employees (FTEs) paying average annual wages of not more than $25,000 may be eligible for a maximum tax credit of 35 percent on health insurance premiums paid for tax years beginning in 2010 through 2013. The credit completely phases out if an employer has 25 or more FTEs and/or pays $50,000 or more in average annual wages.

The credit is scheduled to climb to 50 percent of qualified premium costs for tax years beginning in 2014 and 2015. However, an employer may claim the tax credit after 2013 only if it offers one or more qualified health plans through a state insurance exchange.

Today's uncertainty makes doing nothing or adopting a wait and see attitude very tempting. Instead, multi-year tax planning, which takes into account a variety of possible scenarios and outcomes, should be built into your approach.

Please contact our office for more details on developing a tax strategy in uncertain times that includes consideration of certain tax-advantaged steps that may be taken before December 31, 2012.

Sincerely yours,

Sciarabba Walker