

## TAX UPDATE - BOB CUMBERWORTH

### AutoTeamAmerica 2010 Tax Conference – Terri Harris Power Point

#### 2010 SMALL BUSINESS JOBS ACT

- Enhanced small business expensing (Section 179 expensing)
  - Under the new law, for tax years beginning in 2010 and 2011, the \$250,000 limit is increased to \$500,000 and the investment ceiling to \$2,000,000.
  - The new law also makes certain property eligible for expensing. For property placed in service in any tax year beginning in 2010 or 2011, the up-to-\$500,000 of property expensed can include up to \$250,000 of qualified real property (qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property).
- 100% exclusion of gain from the sale of small business stock for qualifying stock acquired after date of enhancement and before January 1, 2011.
- General business credits of eligible small businesses for 2010 allowed to be carried back five years
  - Under the new law, for the first tax year of the taxpayer beginning in 2010, eligible small businesses can carry back unused general business credits for five years. Eligible small businesses consist of sole proprietorships, partnerships and non-publicly traded corporations with \$50 million or less in average annual gross receipts for the prior three years.
- General business credits of eligible small businesses in 2010 aren't subject to AMT
  - The new law allows eligible small businesses to use all types of general business credits to offset their AMT in tax years beginning in 2010.
- S corporation holding period
  - The 2010 Small Business Jobs Act temporarily shortens the holding period of assets subject to the built-in gains tax to 5 years if the 5<sup>th</sup> tax year in the holding period precedes the tax year beginning in 2011
- Extension of 50% bonus first-year depreciation
  - The new law extends the first-year 50% write-off to apply to qualifying property placed in service in 2010.
- Boosted deduction for start-up expenditures
  - The new law allows taxpayers to deduct up to \$10,000 in trade or business start-up expenditures for 2010. The amount that a business can deduct is reduced by the amount by which startup expenditures exceed \$60,000.
- Limitation on penalty for failure to disclose certain reportable transactions (including listed transactions) on a return.
  - The new law limits the penalty to 75% of the decrease in tax resulting from the transaction. The minimum penalty is \$10,000 for corporations and \$5,000 for individuals (for failure to report a listed transaction, the maximum penalty is \$200,000 and \$100,000, respectively.) These changes are retroactively effective to penalties assessed after December 31, 2006.

- **Deductibility of health insurance for the purpose of calculating self-employment tax.**
  - The new law allows business owners to deduct the cost of health insurance incurred in 2010 for themselves and their family members in calculating their 2010 self-employment tax.
- **Cell phones removed from listed property category**
  - This means that cell phones can be deducted or depreciated like other business property, without onerous recordkeeping requirements.
- **Information reporting required for rental property expense payments**
  - For payments made after December 31, 2010, the new law requires persons receiving rental income from real property to file information returns with IRS and service providers reporting payments of \$600 or more during the tax year for rental property expenses.
- **Increased information return penalties**
  - Effective for information returns required to be filed after December 31, 2010.
- **Allow rollovers from elective deferral plans to designated Roth accounts**
  - The new law allows 401(k), 403(b), and governmental 457(b) plans to permit participants to roll their pre-tax account balances into a designated Roth account. The amount of the rollover will be includible in taxable income except to the extent it is the return of after-tax contributions. If the rollover is made in 2010, the participant can elect to pay the tax in 2011 and 2012.

## **THE PATIENT PROTECTION AND AFFORDABLE CARE ACT TAX PROVISIONS**

### **2010 Tax Provisions**

- **Small Business Tax Credit**

### **2011 Tax Provisions**

- **W-2 Reporting**
  - Employers must disclose the value of the benefit provided for each employee's health insurance coverage on the employee's annual Form W-2
  - Reportable value = aggregate premium for all plans employee is enrolled.
  - The IRS announced that it will defer the new requirement for employers to report the cost of coverage under an employer-sponsored group health plan, making that reporting by employers optional in 2011

### **2012 Tax Provisions**

- **1099 Reporting**
  - Businesses that pay > \$600 during the year to corporations providing property and services must file an information report (presumably a Form 1099) with each corporation and with the IRS
  - Individuals: test applies only to transactions entered into in connection with a trade or business or with an activity engaged in for the production of income.

## 2013 Tax Provisions

- **Modified Itemized Deductions for Medical Expenses:**
  - Threshold for itemized deductions increased to 10% from 7.5%
- **Increase Medicare payroll taxes**
  - Increase of .9% (includes self-employed) on employee portion only above threshold amount
- **What is the Threshold Amount?**
  - \$250,000 in case of joint return/surviving spouse; \$200,000 for single
  - Not indexed for inflation
- **Based on combined wages of employee and his/her spouse in case of joint return.**

Example:

Wages	\$1,250,000	
Medicare Tax	$\$1,250,000 * 1.45\% =$	\$18,125
Extra Tax	$\$1,000,000 * .9\% =$	\$9,000

- **Medicare Investment Income Tax**
  - 3.8% on *lesser of* net investment income or modified adjusted gross income above \$250,000 (“threshold amount”)
  - Net investment income: all non-wage income other than trade or business income
    - Interest, dividends, annuities, royalties, capital gains and rents
  - Will not apply to income based on distributions from tax preferred retirement plans
  - No distinction between short-term and long-term capital gains
  - Exclusions: interest on tax exempt bonds, veterans’ benefits and excluded gain from the sale of a principle residence, 1031 exchanges other exclusions from income.
  - The threshold amount are not indexed for inflation
  - The tax is subject to the estimated tax provisions
  - The tax is not deductible in computing income tax liability
  - Does not apply to sole proprietor, partnership or S corporation engaged in trade or business

Example 1:

MAGI	\$50,000	
Invest, Income	\$200,000	\$7,600
Total Income	\$700,000	
Excess Threshold Amount	\$450,000	\$17,100
Tax Liability	\$7,600	

Example 2:

MAGI	\$50,000	
Invest, Income	\$210,000	\$7,980
Total Income	\$260,000	
Excess Threshold Amount	\$10,000	\$380
Tax Liability	\$380	

## **2014 Tax Provisions**

- Employer Mandate – Coverage
- Individual Mandate - Coverage

## **SCHEDULE UTP UNCERTAIN TAX POSITION STATEMENT**

- A corporation must file Schedule UTP with its income tax return if:
  - The corporation files Form 1120, U.S. Corporation Income Tax Return; Form 1120-F, U.S. Income Tax Return of a Foreign Corporation; Form 1120-L, U.S. Life Insurance Company Income Tax Return; or Form 1120-PC, U.S. Property and Casualty Insurance Company Income Tax Return
  - The corporation has assets that equal or exceed \$100 million;
  - The corporation or a related party issued audited financial statements reporting all or a portion of the corporation's operations for all or a portion of the corporation's tax year;
  - The corporation has one or more tax positions that must be reported on Schedule UTP
- Schedule UTP requires the reporting of each U.S. federal income tax position taken by an applicable corporation on its U.S. federal income tax return for which two conditions are satisfied
  - The corporation has taken a tax position for U.S. federal income tax return for the current tax year or for a prior tax year
  - Either the corporation or a related party has recorded a reserve with respect to that tax position for U.S. federal income tax in audited financial statements, or the corporation or related party did not record a reserve for that tax position because the corporation expects to litigate the position.

## **EXPIRING TAX PROVISIONS AFTER 2010**

### **TEXAS FRANCHISE TAX**

- Increased Audit Activity**
- Service Industry Entities Generally Do Not Qualify for the Cost of Goods Sold Deduction – Tax Policy News**
  - Franchise Tax Rule 3.588(c)(8) does allow a cost of goods deduction for transactions that contain elements of both a sale of tangible personal property and a service; however, an entity may only subtract as cost of goods sold the costs otherwise allowed in relation to the tangible personal property sold.
  - For example, an auto body shop offers the service of car repair and in the process of the repair, replaces some of the car's parts. If the auto body shop elects to use the cost of goods sold to determine margin, the shop can only deduct the cost of the car parts. The labor related to the repair of the car is not allowed as a cost of goods sold.