Temporary Tax Savings

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Extension of Bush-era cuts offers relief for small businesses

The “Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010” signed into law on December 17, 2010, was a sweeping tax package that included, among many other items, an extension of the Bush-era tax cuts for two years, estate tax relief, a two-year “patch” of the alternative minimum tax (AMT), a 2-percentage-point cut in employee-paid payroll taxes and in self-employment tax for 2011, new incentives to invest in equipment, and a host of retroactively resuscitated and extended tax breaks for both individuals and businesses.

Thanks to the Tax Relief Act, current income tax rates will be retained for 2011 and 2012, with a top rate of 35 percent on ordinary income, and 15 percent on qualified dividends and long-term capital gains.

After a one-year hiatus, the estate tax will be reinstated for 2011 and 2012 with a top rate of 35 percent. The exemption amount will be $5 million per individual in 2011, and will be indexed to inflation in following years. The estates of those who died in 2010 can choose to follow either the rules of 2010 or 2011.

Alternative minimum tax

A two-year AMT “patch” for 2010 and 2011 will keep the alternative minimum tax exemption near current levels, and allow personal credits to offset AMT. The Act provided an AMT “patch” intended to prevent the AMT from encroaching on middle-income taxpayers by providing higher exemption amounts and other targeted relief for 2010 and 2011. Without the patch, an estimated 21 million additional taxpayers would have owed AMT for 2010.

The Act increased the 2010 exemption amounts to $47,450 for individuals and $72,450 for married taxpayers filing jointly. For 2011, the amounts have been increased to $48,450 for individuals and $74,450 for married taxpayers filing jointly.

Writing it all off

On the business side, imagine an immediate write-off that, unlike first-year “expensing” write-offs under Section 179, is not limited for use by only small landscape and lawn care contractors and businesses or capped at a certain dollar level. The 2010 Tax Relief Act boosted a 50 percent “bonus” depreciation to 100 percent for qualified investments made after September 8, 2010, and before January 1, 2012. The new law also allows a 50 percent bonus depreciation for qualified property placed in service after December 31, 2011, and before January 1, 2013.

Earlier last fall, the Small Business Jobs Act increased the Section 179, first-year expensing dollar and investment limits to $500,000 and $2 million, respectively, for 2010 and 2011. The Tax Relief Act provided a $125,000 dollar limit and a $500,000 investment limit for tax years beginning in 2012 and expiring after December 31, 2012. That means that a turf or lawn care business may immediately deduct a Section 179 expense, up to $500,000 of newly acquired business property, new or used, placed in service during the tax year. The Section 179 expensing write-off is reduced, dollar for dollar, by any property acquisitions in excess of the $2 million investment ceiling, limiting the write-off to smaller businesses.

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In addition to extending the Section 179 write-off for off-the-shelf computer software, the Tax Relief Act restores a unique 15-year write-off period for improvements made to leased, business property, restaurant buildings and improvements, as well as improvements made to “retail” property.

Inadvertent tax breaks redux

In the past, generous tax breaks for gas-consuming heavy SUVs almost inevitably raised the ire of Congress. However, when Congress passed and the president signed into law last December’s Tax Relief Act, the result was that tax breaks for these assets became even more generous. Although probably unintended, the limited-time 100 percent “bonus” depreciation allowance included a new, heavy SUV purchased and used for business.

Heavy SUVs – those built on a truck chassis and rated at more than 6,000 pounds gross (loaded) vehicle weight – have long been exempt from the “luxury-auto” dollar caps because they fall outside of the tax law’s definition of a passenger auto. Today, however, the entire purchase price of those heavy SUVs can be written-off in the year they are “placed-in-service.” A turf or lawn care professional who buys and places in service a new heavy SUV after September 8, 2010, and before January 1, 2012, and uses it 100 percent for business purposes, may write-off its entire cost in the placed-in-service year.

If proof is needed, keep in mind that under the 2010 Tax Relief Act, the bonus first-year depreciation percentage is 100 percent (instead of the old 50 percent rate) for bonus-depreciation-eligible "qualified property" placed in service after September 8, 2010, and before January 1, 2012. Under the rules, qualified property includes property to which (MACRS) depreciation applies that has a recovery period of 20 years or less. Autos and light trucks are five-year MACRS property, and thus qualify for bonus depreciation (assuming business use exceeds 50 percent of total use).

Extending leased property and other write-offs

Before passage of the Tax Relief Act, improvements or modifications to leased business property, qualified restaurant property and qualified retail improvement property that was placed in service before 2010 was included in the 15-year MACRS class for depreciation purposes – that is, it was depreciated over 15 years under the MACRS, standardized depreciation system.

The 2010 Tax Relief Act retroactively extended those rules for two years through 2011. In other words, the 15-year write-off can be applied, retroactively, to qualified expenditures for improving leased business property, including modifications made to equipment leased by the lawn care or turf operation.

Temporary payroll cuts for the self-employed

Under the old rules covering payroll taxes, employees paid a 6.2 percent Social Security tax on all wages earned up to $106,800 (in 2011) and self-employed individuals paid 12.4 percent Social Security self-employment taxes on all their self-employment income up to the same threshold.

The Tax Relief Act reduced the employee share of OASDI (Social Security tax) from 6.2 percent to 4.2 percent for wages earned in calendar year 2011 up to $106,800, a savings of up to $2,136. Self-employed turf and lawn care professionals will pay 10.4 percent on self-employment income up to the threshold. The new payroll tax holiday is estimated to inject $120 billion into the economy in 2011.

In order to garner their share of the $120 billion in tax savings, self-employed lawn care contractors and turf professionals would calculate the deduction for employment taxes without regard to the temporary rate reduction (that is, one-half of 15.3 percent of self-employment income). However, the 2010 Tax Relief Act provides an enhanced percentage representing the employer portion of the deduction.

Help with payroll costs

The Work Opportunity Tax Credit, or WOTC, is intended to encourage employers to hire individuals from targeted groups. The WOTC allows employers who hire members of certain targeted groups to get a credit against income tax equal to a percentage of the new hire's first-year wages. That can be up to $6,000 per employee ($12,000 for qualified veterans; and $3,000 for qualified summer youth employees). Where the employee is a long-term family assistance (LTFA) recipient, the WOTC is a percentage of first and second year wages, up to $10,000 per employee.

Generally, the percentage of qualifying wages is 40 percent of first-year wages; it’s 25 percent for employees who have completed at least 120 hours, but less than 400 hours of service for the employer. For LTFA recipients, it includes an additional 50 percent of qualified second-year wages. Under pre-Act law, wages for purposes of the credit doesn’t include any amount paid or incurred for an individual who began work after August 31, 2011. The 2010 Tax Relief Act extended the WOTC to include individuals who begin work before January 1, 2012.

Business incentives

Many pundits have speculated that unemployment has remained high due to businesses fearing expiration of the Bush-era tax cuts. The passage of the Tax Relief Act of 2010, along with its tax cuts, combined with other incentives, may have already encouraged some small businesses to begin hiring again. For example, in addition to extending the incentives for investing in equipment, the 2010 Tax Relief Act contained a 2 percentage point cut in employee-paid payroll taxes and in self-employment tax for 2011.

And, remember, in 2011, turf and lawn care professionals and businesses will be allowed to expense a full 100 percent of their capital expenditures, instead of depreciating over time, and hopefully addressing the pent up demand to upgrade and invest. Additionally, the Act delayed an increase in capital gains tax rates.

Unfortunately, omitted from the new law was a repeal of the controversial expansion of the Form 1099 reporting requirements. Overall, however, the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 is well on its way to providing an estimated $858 billion in tax savings for turf and lawn care professionals.

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