

American Recovery & Reinvestment Act: Answers to your Questions

UPDATE per the Worker Homeownership and Business Assistance Act 2009

What exactly does American Recovery and Reinvestment Act mean for my business?

Significant temporary tax incentives have been put in place to help businesses take advantage of challenging economic times. Some of these temporary benefits help company performance by reducing taxable income. By lowering your taxable income, bonus depreciation and Sec. 179 can dramatically cut your 2009 tax bill, thereby freeing up cash in the near term.

That sounds too good to be true. What's the catch?

There is no catch. By lowering your taxable income companies can utilize the cash flow generated to purchase new equipment, pay existing debt, to invest in other aspects of the business, or to simply save for future use.

How does bonus depreciation work?

Companies that buy new equipment in 2009 can depreciate 50 percent of the cost in the first year, plus the percentage of the remaining basis in the equipment that would ordinarily be depreciable under the Modified Accelerated Cost Recovery System (MACRS). For a \$100,000 piece of equipment with a seven-year MACRS life, the first year depreciation under these incentives would be \$57,143: \$50,000 bonus depreciation, plus 14.3 percent of the remaining \$50,000 in basis.

What if my company is facing a loss this year and there is no taxable income?

The benefit of bonus depreciation is that it can be elected to help create a net operating loss or drive an existing one even further. Creating a taxable loss for this year provides an opportunity to seek out taxes paid in previous years to actually receive a *refund*. If there is no tax paid historically to seek a refund against, the net operating loss can be used to carry forward against any future taxes owed.

NEW: Worker, Homeownership, and Business Assistance Act of 2009 signed on November 6, 2009 gives any company the ability to carry back net operating losses 5 years from tax years 2008 or 2009.

IMPACT: A business that carries back a net operating loss to a prior profitable year can obtain a quick refund from the IRS for that prior year. This will provide additional cash that the business can use to pay expenses, maintain operations, and make new investments.

What type of equipment is eligible?

To be eligible for bonus depreciation, the following requirements must be met:

- The equipment purchased must be new.
- The equipment must be depreciable under MACRS and have a depreciation recovery period of 20 years or less. The Act also allows the use of bonus depreciation for certain types of software and leasehold improvements. Check with your tax professional.
- The original use of the equipment must commence with the taxpayer claiming bonus depreciation after Dec. 31, 2008.
- The equipment must be purchased between Dec. 31, 2008 and Dec. 31, 2009. Equipment for which a binding purchase contract was in effect before Dec. 31, 2008 is not eligible.
- The equipment must be delivered by Dec. 31, 2009.

How long do I have to take advantage of bonus depreciation?

To qualify, the new equipment must be purchased and delivered before Dec. 31, 2009.

Note: Bonus depreciation is expiring 12/31/09.

Do I have to use bonus depreciation?

No. Bonus depreciation is elective (meaning it's your choice whether to use it). Bonus depreciation also applies for regular and alternative minimum tax purposes.

How did the American Recovery and Reinvestment Act change the Sec. 179 expensing law?

The Act dramatically increased the expensing limits under Sec. 179 of the Internal Revenue Code for any taxable year beginning in 2009. For the 2009 tax year, companies can expense up to \$250,000 as long as total purchases do not exceed \$800,000. For each dollar over, the eligible expensing amount correspondingly drops by one dollar. Companies that spend more than \$1,050,000 on tangible personal property cannot take advantage of Sec. 179 (but they can still use bonus depreciation).

Note: The temporary increase of Section 179 is expiring 12/31/09.

To qualify for Sec. 179, does the equipment have to be new?

No. Unlike bonus depreciation, Sec. 179 expensing can be applied to both new and used equipment.

Can Sec. 179 and bonus depreciation be combined?

Yes. Companies eligible for Sec. 179 can also combine it with bonus depreciation for even bigger tax savings. (Sec. 179 cannot be used to create a net operating loss like bonus depreciation can.)

In Summary:

- If your company is **breaking even or losing money** in 2009, the bonus depreciation may provide you with a refund for taxes paid in previous years.
- The net operating loss carry back has been increased from 2 to five years.
- There is no limit as to the size of the firm that can benefit from the enhanced tax loss carry back.
- If your company is **making money** in 2009, maximize your deduction by first taking advantage of Sec. 179 and then utilizing the bonus depreciation for the balance of the purchase amount over \$250,000.
- The combination of Sec. 179 and bonus depreciation deductions generated by capital equipment investments can produce a paper loss in 2009 that can be used as far back as tax year 2004 to create a refund of taxes already paid.
- Under current law, bonus depreciation evaporates Jan. 1, 2010, and Section 179 deductions are reduced from \$250,000 to \$128,000.
- To qualify for both 2009 bonus depreciation and Sec. 179 \$250,000 deduction, capital equipment must be in service prior to Dec. 31, 2009.

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