

Will your business get a boost from recovery plan?

Tax provisions designed for small businesses

On February 17 President Obama signed the American Recovery and Reinvestment Act of 2009 into law. The stated purposes of the ARRA are "to preserve and create jobs and promote economic recovery, to assist those most impacted by the recession, to provide investments needed to increase economic efficiency by spurring technological advances in science and health, to invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits, and to stabilize state and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases." Unfortunately, the ARRA has already failed in one goal when California finally passed its budget with a bunch of tax increases. Hopefully, the remainder of the goals will not fail also.

Four of the tax provisions contained in the ARRA that are designed to benefit small businesses, which include:

Bonus Depreciation Deductions

Normally when a business acquires

an asset, the business is allowed to recoup the cost of that capital expenditure over a number of years by the use of a depreciation deduction. In 2008 Congress temporarily allowed businesses to recoup the costs of capital expenditures faster than the customary depreciation schedule would permit



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by allowing businesses to immediately write off 50 percent of the cost of depreciable property acquired in 2008 for use in the United States, in addition to the normal first-year depreciation deduction. The ARRA would expand this bonus depreciation deduction to capital expenditures incurred after December 31, 2007 and before January 1, 2010.

Small Business Expensing

Internal Revenue Code (IRC) Section 179 provides small businesses the ability to immediately expense the cost of certain capital expenditures in the year of acquisition. The 2008 Economic Stimulus Act increased the amount of IRC Section 179

expensing for tax year 2008 to \$250,000 and increased the threshold for reducing the deduction to \$800,000. This increased expensing deduction applied to property placed in service in 2008. The ARRA extends this temporary increase in the deduction for capital expenditures incurred in taxable years beginning in 2009.

NOL Carryback

Prior to enactment of the ARRA, for federal tax purposes, net operating losses may be carried back to the 2 years before the year that the loss arose (the "carry back period") and carried forward to each of the next 20 years after the year that the loss arose (the "carry forward period"). The ARRA extends the carry back period to 3, 4, or 5 years for a net operating loss incurred in a tax year that began or ended in 2008. However, this extended carry back period is only applicable for "eligible small businesses." An "eligible small business" is defined as a sole proprietorship, corporation or partnership that meets a \$15 million gross receipts test for the tax year in which the loss arose. The \$15 million gross receipts test is met for any tax year if the average annual gross receipts for



the business for the three-taxable year period ending with the 2008 loss year does not exceed \$15 million. Under this rule, the gross receipts are reduced by returns and allowances made during such year. Predecessors of the eligible small business are treated as the business for purposes of the gross receipts test. If the business was not in existence for the entire three-year period, then the test is applied for the period during which the business was in existence. If

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you are dealing with a short year period for purposes of the gross receipts test, then the short year period will be annualized by multiplying the gross receipts for the short period by 12 and dividing the result by the number of months in the short period.

In addition to the having to meet the gross receipts test, for purposes of qualifying for the extended carry back period, IRC Section 448(c) mandates that certain corporations, partnerships, and sole proprietorships, trusts, and estates related to the taxpayer be treated

as a single employer in applying the gross receipts test. This aggregation rule for purposes of computing the gross receipts is taken from IRC Section 52 and looks to see if the taxpayer is part of a "controlled business." A controlled business includes: (1) a parent-subsidiary group; (2) a brother-sister corporate group; and (3) a combined group under common control.

Incentive for hiring unemployed veterans and disconnected youth

IRC Section 51 allows businesses to

claim a work opportunity tax credit equal to 40 percent of the first \$6,000 of wages paid to employees of one of nine targeted tax groups (i.e., qualified IV-A recipient, a qualified veteran, a qualified ex-felon, a high risk youth, a vocational rehabilitation referral, a qualified summer youth employee, a qualified food stamp recipient, or a qualified SSI recipient). The ARRA adds two additional classifications of workers: unemployed veterans and disconnected youths. Pursuant to the ARRA an unemployed veteran would be someone: (1) having served on active

duty in the Armed Forces for more than 180 days or having been discharged or released from active duty in the Armed Forces for a service connected disability; (2) having been discharged or released from active duty in the Armed Forces at any time during the five-year period ending on the hiring date; and (3) having received unemployment compensation under state or federal law for at least four weeks during the one-year period ending on the hiring date.

Pursuant to the ARRA, a disconnected youth would be a person between the ages of 16 and 25 who had not been regularly employed or attended secondary, technical or post-secondary school in the previous six months, and is not readily employable due to the lack of a sufficient number of basic skills.

Although the ARRA contains other important non-tax provisions intended to help the economy in general, will the aforementioned tax incentives really provide a stimulus to the majority of small businesses?

The ARRA bonus depreciation and increased amounts for IRC Section 179 expensing can be very helpful, but that presumes that the small business has the capital on hand to purchase the equipment or has access to the credit markets or the banks are willing to lend money. The benefit of bonus depreciation and increased IRC Section 179 expensing will hinge on banks and creditors providing capital to the small businesses to acquire new equipment.

The work opportunity tax credit is nice, but where it is so targeted it is likely to benefit very few businesses. The estimated cost of expanding this credit is projected to be \$20.8 million a year for ten years. That's a pretty small benefit given the overall cost of the ARRA.

The expansion of the carry back period for net operating losses will provide a great benefit for those businesses that incurred a net operating loss in 2008 and survived. This provision will definitely help businesses that profited greatly within the last five years, like the real estate development industry. The question to be answered is will businesses put those tax refunds back into the economy by purchasing new equipment or expanding their business, or will these businesses sit on those refunds?

Pursuant to IRS Circular 230, any tax advice expressed herein is not intended or written to be used, and cannot be used, by any taxpayer to avoid U.S. federal tax penalties. If you have any questions as to whether or not any tax provision can benefit your business you should consult with your tax attorney or certified public accountant.

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