Congress Extends the Bush Tax Cuts and Expands Incentives to Purchase Depreciable Property

12.20.2010

12.20.2010

President Obama signed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "Tax Relief Act") which extends the so-called "Bush tax cuts" through 2011 and 2012. The Bush tax cuts are the product of two acts, the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA") and the Jobs and Growth Tax Relief Reconciliation Act of 2003 ("JGTRRA"). Both EGTRRA and JGTRRA were scheduled to sunset on December 31, 2010. The Tax Relief Act extends the sunset date of EGTRRA and JGTRRA to December 31, 2012.

The Tax Relief Act represents a major compromise between President Obama and congressional Republicans and Democrats. While Democrats favored no extension of the Bush tax cuts, Republicans wanted a permanent extension of the tax cuts. The 2-year extension signifies a short-term victory for congressional Republicans, but it hardly provides the permanence that they initially sought.

In addition to extending the Bush tax cuts and providing for a 2% cut in payroll and self-employment taxes, the Tax Relief Act expands and extends certain tax incentives offered to businesses through the 2010 Small Business Jobs Act (the "Small Business Jobs Act"). For more information on the Small Business Jobs Act, please see our recent tax alert on the subject: 2010 Small Business Jobs Act Provides Tax Incentives for Businesses Large and Small.

Tax Cuts for Individuals

The Tax Relief Act includes the following individual income tax and payroll tax provisions:

- The Bush tax cuts for individuals will continue through 2011 and 2012. Consequently, the highest tax rate on ordinary income will remain at 35%, and the tax rate on qualified dividends and long-term capital gains will remain at 15%.
- The employee portion of Social Security is reduced from a 6.2% rate of tax to a 4.2% rate of tax (12.2% to 10.2% for self-employed individuals) through 2011.

- There is a "patch" of the alternative minimum tax for 2010 and 2011, keeping the exemption near current levels.

The extension of the Bush tax cuts provides the most important tax planning opportunity. Individuals will have 2 years to take advantage of the 15% tax rate on long-term capital gain income and the 35% tax rate on ordinary income.

Incentives for Businesses to Purchase Depreciable Property

The Tax Relief Act contains incentives to purchase certain qualifying depreciable property. The Tax Relief Act primarily expands the following incentives that Congress put into place in the Small Business Jobs Act earlier this year:

- The Small Business Jobs Act provides for 50% first-year bonus depreciation for qualified property that is placed in service by December 31, 2010 (and on or before December 31, 2011 for aircraft and other property with a long production period). The Tax Relief Act extends and expands this first-year bonus depreciation to 100% of the cost of qualified property placed in service on or after September 9, 2010 and by December 31, 2011 (by December 31, 2012 for certain longer-lived and transportation property).
- The Tax Relief Act further provides for 50% first-year bonus depreciation for qualified property placed in service on or after January 1, 2012 and by December 31, 2012 (by December 31, 2013 for certain longer-lived and transportation property).

The Tax Relief Act provides the following moderate expansion of the expensing of qualifying property under Code ?179 for small and mid-size businesses, which was implemented mostly in the Small Business Jobs Act:

- The Small Business Jobs Act permits businesses to expense immediately up to $500,000 of depreciable tangible personal property and off-the-shelf software placed in service during tax years beginning in 2010 and 2011. Under the Small Business Jobs Act, a phase out begins when a business places in service more than $2 million of such property during the tax year. Eligibility to expense such property is completely phased out when a business places in service more than $2.5 million of eligible property. For tax years beginning in 2012, the maximum Code ?179 expense deduction was scheduled to drop to $25,000, and the phaseout would begin at $200,000.
- The Tax Relief Act extends the Code ?179 tax incentives for small and mid-size businesses provided in the Small Business Jobs Act by providing that, for taxable years beginning in 2012, the maximum Code ?179 expense deduction drops to $125,000, and the phaseout begins at $500,000. For taxable years beginning after 2012, the phaseout amounts drop to their previously established limits of $25,000 and $200,000, respectively.

Businesses of all sizes can take advantage of the new 100% first-year bonus depreciation for purchases of qualifying depreciable property placed in service on or before December 31, 2011 (by December 31, 2012 for certain longer-lived and transportation property), as well as the new 50% first-year bonus depreciation for qualified property placed in service on or after January 1, 2012 and by December 31, 2012 (by December 31, 2013 for certain longer-lived and transportation property). The benefits of the Tax Relief Act's further expansion of Code ?179 expensing is limited to small and mid-size businesses.

Conclusion

The Tax Relief Act provides both individuals and businesses with tax planning opportunities for the 2011 and 2012 tax years.

For more information about this topic, please contact any member of the Williams Mullen Tax Law Team.

Related People

Related Services

- Tax Law