



DONALD D. WILSON JR., P.A.  
CERTIFIED PUBLIC ACCOUNTANT

## Highlights of the Small Business Jobs Act of 2010

On September 27, the President signed into law H.R. 5297, the Small Business Lending Funding Act. The tax title of this bill, the "Small Business Jobs Act of 2010," includes a number of important tax provisions for businesses large and small, and changes for individuals as well. While a handful of these tax provisions are effective either on the day after the date that the bill was signed or in 2011, the vast majority of these provisions are effective retroactively and have an immediate impact on the 2010 tax year.

*Immediate and retroactive changes.* Several of the Act's provisions are triggered by the enactment date (the date it was signed into law by the President, Sept. 27, 2010):

- The 100% gain exclusion for qualified small business stock (QSBS) for regular tax and alternative minimum tax (AMT) purposes applies for QSBS acquired after Sept. 27, 2010 and before Jan. 1, 2011.
- The provision allowing retirement plan distributions to be rolled over to a designated Roth account applies for distributions made after Sept. 27, 2010.
- The new sourcing rule for guarantees applies for guarantees issued after Sept. 27, 2010.
- The elimination of the requirement for a pre-levy collection due process (CDP) hearing for certain Federal contractors applies for levies issued after Sept. 27, 2010.

Many of the Act's provisions are retroactively effective (i.e., not just effective from the date the President signed the Act into law) and so have more of an impact on the 2010 tax year:

... The increased [Code Sec. 179](#) expensing (\$500,000 limit, with \$2 million phaseout threshold) and the qualified real property expensing (\$250,000 limit) apply for tax years beginning in 2010 and 2011.

... Revived 50% bonus depreciation (and a new long-term contract accounting rule for bonus depreciation) and an additional \$8,000 luxury auto depreciation limit applies for qualified property placed in service in 2010 (as well as 2011 for certain aircraft and long production period property).

... Cell phones are no longer "listed property" (subject to strict substantiation rules) for tax years beginning after 2009.

... An increased startup expense deduction (\$10,000 limit, with \$60,000 phaseout threshold) applies for tax years beginning after 2009 and before 2011.

... Eligible small business credits that are determined in a taxpayer's first tax year beginning in 2010 but are unused are eligible for 5-year carryback.

... Eligible small business credits determined in tax years beginning in 2010 can offset AMT liability and, to an increased extent, regular tax liability for credits determined in tax years beginning after 2009.

... Health insurance costs for a taxpayer and his family are deductible in computing 2010 self-employment tax.

... The controversial [Code Sec. 6707A](#) penalty for a failure to report a tax shelter transaction is completely restructured for penalties assessed after 2006.

*Prospective changes.* A number of the Act's provisions apply after 2010: the temporary reduction in the S corporation's built-in gain period (from 7 to 5 years); the partial annuitization of nonqualified annuities; permitting [Code Sec. 457](#) governmental plan to include a qualified Roth contribution program; the information reporting requirement for rental income from realty, and the increased information return penalty and failure to furnish payee statement penalty. And, the accelerated estimated tax for large corporation (assets of at least \$1 billion) applies to estimated tax otherwise due in July, Aug., or Sept. 2015.

### **ACCELERATED CAPITAL COST RECOVERY PROVISIONS IN THE SMALL BUSINESS JOBS ACT OF 2010**

- Substantially increased expensing deduction for 2010 and 2011.
- Up to \$250,000 of qualified real property eligible for expensing in 2010 and 2011.
- Other [Code Sec. 179](#) expensing changes.
- Bonus first-year depreciation extended through 2010. First-year depreciation cap for 2010 autos and trucks boosted by \$8,000.
- Special long-term contract accounting rule for bonus depreciation on certain property placed in service after 2009.
- Deduction for startup expenses increased.

### **LIBERALIZED TAX CREDIT RULES AND OTHER BUSINESS TAX BREAKS IN THE SMALL BUSINESS JOBS ACT OF 2010**

- 5-year carryback of eligible small business credits.
- Eligible small businesses may offset AMT with general business credits in 2010 tax years.
- 100% gain exclusion for qualified small business stock for regular tax and AMT.
- Temporary reduction in S corporation built-in gain period.
- Major rewrite for penalty for failure to report shelter transactions.
- Health insurance costs for self and family are deductible in computing 2010 self-employment tax.
- Cell phones removed from listed property category.

## **RETIREMENT PLANNING INCENTIVES AND REVENUE RAISERS IN THE SMALL BUSINESS JOBS ACT OF 2010**

- Partial annuitization of nonqualified annuity allowed after 2010.
- Code Sec. 457 plans can include a qualified Roth contribution program.
- Retirement plan distributions may be rolled over to a designated Roth account.
- Information reporting required for rental income from realty after 2010.
- Information return penalties increased.
- Increased per statement rates and maximum and minimum payee statement penalty.
- New rules set out how to source guarantee income.
- No pre-levy CDP hearing required for certain federal contractors.
- Accelerated 2015 estimated tax payment for large (\$1 billion) corporations.

### **SEP Compliance Traps to Avoid**

Despite a SEP's simplicity, employers can and do at times get themselves in trouble with the operation of their plans. For example, the IRS recently released a list of five common mistakes that employers make when it comes to SEPs:

1. Failing to keep their plan document current—SEPs are generally adopted simply by completing a short IRS Form 5305-SEP (or by completing a financial institution's prototype plan form). When the IRS issues a new Form 5305-SEP (the most recent is from 2004), employers need to update their plan by completing the new form.
2. Failing to cover all eligible employees—In a recent court case, a SEP failed to qualify because one of two employees (the wife of the president of the company and the only other employee) didn't receive a contribution under the plan even though she was eligible.
3. Failing to cover eligible employees in related businesses that are under common control.
4. Failing to use the right compensation number for employees when calculating the amount of their contribution.

5. Failing to limit contributions to a particular employee's account to no more than the maximum allowed (normally the lesser of 25% of covered compensation or, for 2008, \$46,000).

For our clients that currently have SEPs, if you have any concerns about whether your plan is meeting all of the eligibility requirements, please call us and we'd be happy to discuss this. If you currently don't offer a retirement plan, but would like to consider a SEP or another option [such as a SIMPLE IRA or a 401(k) plan], we're available to discuss that as well.

## Temporary employee/self-employed payroll tax cut for 2011.

The Federal Insurance Contributions Act (FICA) imposes two taxes on employers, employees, and self-employed workers—one for Old Age, Survivors and Disability Insurance (OASDI; commonly known as the Social Security tax), and the other for Hospital Insurance (HI; commonly known as the Medicare tax).

Under pre-Act law, the FICA tax rate for employees and employers is 7.65% each—6.2% for OASDI and 1.45% for HI. Under the Self Employment Contributions Act (SECA) tax, self-employment income of self-employed taxpayers is subject to a tax of 15.3%—12.4% for OASDI and 2.9% for HI. There is a maximum amount of compensation subject to the OASDI tax (the wage base), but no maximum for HI. The wage base is \$106,800 for 2010 and 2011.

Under pre-Act law, for computing the income tax of an individual, allows an above-the-line deduction equal to 50% of the amount of the SECA tax imposed on the individual's self-employment income for the tax year.

Under [Code Sec. 1402\(a\)\(12\)](#), a taxpayer is allowed a deduction in computing net earnings from self-employment equal to: (1) net earnings from self-employment as determined before taking the [Code Sec. 1402\(a\)\(12\)](#) deduction into account, multiplied by (2) one-half the sum of the OASDI tax rate and the HI tax rate. This deduction is allowed in computing net earnings from self-employment in lieu of the [Code Sec. 164\(f\)](#) above-the-line deduction of one-half of the self-employment tax. Thus, the [Code Sec. 164\(f\)](#) deduction can't be taken in computing self-employment tax liability. The [Code Sec. 1402\(a\)\(12\)](#) deduction is designed to put the self-employed in the same position as employees in that they don't have to pay self-employment tax on about half of the amount of the tax itself.

**New law.** For remuneration received during 2011, the Act reduces the employee OASDI tax rate under the FICA tax by two percentage points to 4.2%. Similarly, for self-employment income for tax years beginning in 2011, the Act reduces the OASDI tax rate under the SECA tax by two percentage points to 10.4% percent. (Act Sec. 601) As a result, for 2011, employees will pay only 4.2% Social Security tax on wages up to \$106,800 and self-employed individuals will pay only 10.4% Social Security self-employment taxes on self-employment income up to \$106,800.

**Observation:** The maximum savings for 2011 will be \$2,136 (2% of \$106,800) per taxpayer. If both spouses earn at least as much as the wage base, the maximum savings will be \$4,272.

The Act provides rules for coordination with deductions for employment taxes, as follows.

The [Code Sec. 164\(f\)](#) income tax deduction allowed for tax years beginning in 2011 is computed at the rate of 59.6% of the OASDI tax paid, plus one half of the HI tax paid. (Act Sec. 601(b)(2))

The new percentage (59.6%) replaces the rate of one half (50%) allowed under pre-Act law for this portion of the deduction. The new percentage is necessary to continue to allow the self-employed taxpayer to deduct the full amount of the employer portion of SECA taxes. The employer OASDI tax rate remains at 6.2%, while the employee portion falls to 4.2%. Thus, the employer share of total OASDI taxes is 6.2 divided by 10.4, or 59.6% of the OASDI portion of SECA taxes. (Committee Report)

However, the two-percentage-point reduction is not taken into account in determining the [Code Sec. 1402](#) SECA tax deduction allowed for determining the amount of the net earnings from self-employment for the taxable year. (Act Sec. 601(b)(1)) Thus, the deduction for 2011 remains at 7.65% of self-employment income (determined without regard to the deduction).