



# Small Business Tax Saving Strategies for the 2011 Filing Season

Few business sectors embody today's entrepreneurial spirit, drive for innovation and unwavering perseverance more than the small business community. From creating the majority of net new jobs in the country to employing more than half of private industry's workforce, its 29 million members not only personify the American dream but they also serve as the growth engine of the U.S. economy.

Although uncertainty continues to cloud the financial forecast, small businesses have remained a powerful force in the U.S. economy. Bolstering their position are a number of tax laws that have presented small businesses with opportunities for reducing taxes, lowering expenses and encouraging investment. However, understanding the full range of the latest tax laws, and correctly applying them when preparing tax returns, can be a daunting task, especially when meeting new business demands and growing competition, which are consuming a greater amount of small business owners' time and resources.

*Small Business Tax Saving Strategies for the 2011 Filing Season* provides an overview of key tax-law provisions that may affect your business, and the latest information and practical strategies for minimizing your tax bill. Information is current as of Feb. 1, 2011.

Should you have any questions or concerns as you prepare your 2010 tax return or evaluate your business's financial situation throughout the year, a CPA tax professional can help by reviewing your overall position and providing you with the expert tax-planning counsel you need today and in the years ahead.



## Select 2010 Tax Provisions

### Section 179 Expense Deduction

The Section 179 expense deduction is an expensing provision that applies to tangible business property placed in service during the tax year.

For 2010, business owners can write off the entire cost of tangible personal property used in their business, up to \$500,000 in the first year, regardless of whether the purchase was made with cash or credit. The \$500,000 limit applies on a per-taxpayer basis and is in effect through 2011.

Property eligible for the deduction ranges from computer software to office equipment. For 2010, up to \$250,000

of the total available deduction may be used for qualified restaurant property, leasehold improvement property and retail improvement property.

The deduction is reduced by every dollar spent over \$2 million. Therefore, if a company spends \$2.5 million or more on eligible property, its Section 179 expense deduction will be zero.

The Section 179 expense deduction cannot be greater than the business's taxable income and does not apply to inherited property or property initially purchased for personal use, even if the property is later changed to business use.

**Benefits:** *Provides immediate tax relief on newly purchased equipment, benefits cash flow and promotes investment by small businesses.*

*Property eligible for the Section 179 expense deduction ranges from computer software to office equipment.*

### Personalized Company Name

Address, City, State, ZIP code  
website, email, phone, fax



## Future Planning

### 1099 Reporting Requirement

All persons engaged in a trade or business who make payments in any tax year aggregating \$600 or more must provide the payee with a Form 1099-MISC for the year and send a copy to the IRS. However, payments to corporations are excepted from these reporting obligations (other than payment of legal fees or medical or health-care services that are otherwise reportable).

For payments made after Dec. 31, 2011, the exception for payments to corporations is eliminated. Thus, all payments aggregating \$600 or more made to corporations are subject to the information-reporting requirements.

Also, for payments made after Dec. 31, 2010, individuals receiving rental income from real estate are considered to be engaged in a trade or business of renting property.

Therefore, unless they fall into an authorized exception, they must file the appropriate information returns for reportable payments of \$600 or more that they make in the course of that business.

Congress is considering legislation to remove this requirement.

### Bonus Depreciation

There is a special first-year bonus depreciation allowance available for eligible property acquired after Dec. 31, 2007. This rule allows business owners to deduct 50 or 100% of the property's cost in the year it is placed in service, with any remaining cost subject to regular depreciation rules.

The allowance generally applies to tangible personal property, including certain leasehold improvements, office equipment and computer software that was first purchased by the business owner (not used property), has a recovery period of 20 years or fewer and is placed in service from 2008 through 2012.

The first-year bonus depreciation allowance is determined by when the property was placed in service, as presented below:

- Jan. 1, 2010, through Sept. 8, 2010: 50%
- Sept. 9, 2010, through Dec. 31, 2011: 100%
- Jan. 1, 2012, through Dec. 31, 2012: 50%

**Benefits:** Provides immediate tax relief, improves cash flow and provides additional capital that small business owners can use to reinvest in the business.



### S Corporation Built-in Gains

The built-in gains tax applies to S corporations that have converted from a C corporation. The tax applies to certain property held by the S corporation at the time of the conversion. If the property is sold less than 10 years after the conversion, the S corporation must pay a tax on the gain (net recognized built-in gain) equal to 35% (the highest corporate tax rate).

For tax years beginning in 2010, the recognition period imposed on an S corporation's net built-in gain is reduced to seven years.

For tax years beginning in 2011, no tax is imposed on an S corporation's net built-in gain, if the asset has been held for at least five years.

**Benefits:** Lowers the tax burden on S corporations and may provide additional capital for business investment.

### Employer-Provided Cell Phones

The IRS categorizes specific assets as "listed property" that is subject to both special record-keeping and depreciation rules. Listed property includes transportation vehicles (automobiles, motorcycles and boats), computers and peripherals as well as other assets that businesses provide employees that can also be used in personal, nonbusiness ways.

The special rules for listed property are intended to distinguish between business and personal use, which can create taxable income to an employee or a business owner when an employer-provided benefit is used for personal purposes. Listed property must be used more than 50 percent for business purposes to qualify for depreciation, and deductions will be severely limited.

For tax years after 2009, cell phones are no longer included as listed property and therefore employees do not need to adhere to listed property's heightened documentation rules for personal and business use. However, documentation is still required. An employer's policy

*Business owners and officers must maintain some documentation to demonstrate the business use of listed property, to ensure that the property is not treated as a fringe benefit.*



must clearly reflect that the cell phone or similar equipment is necessary for business purposes and is needed for the employee to perform his/her duties. Business owners and officers must maintain some documentation to demonstrate the business use of listed property, to ensure that the property is not treated as a fringe benefit.

**Benefit:** *Removes the need for employees to report taxable income from an employer-provided cell phone if the phone is used primarily for business purposes.*

#### **Small Business Health Insurance Credit**

For 2010, there is a new credit for small business owners who contribute to their employees' health insurance coverage. However, a number of criteria, including the number of employees, average wages, premium amounts paid and average premiums by the state for certain coverage, all factor in to the extent to which the credit can be applied.

To qualify for the credit, which can reach 35% of the employer's contribution, the employer needs to have the equivalent of 25 or fewer full-time employees and average annual full-time wages of less than \$50,000. Small businesses with 10 or fewer full-time employees and average annual full-time wages of less than \$25,000 can receive the full credit.

The credit, which also applies to 2011, 2012 and 2013 tax years, can be claimed

for each tax year in which the employer qualifies, and it can offset the Alternative Minimum Tax (AMT).

**Benefit:** *Encourages small business owners to help pay for their employees' health coverage, and in the process, reduces their own tax liability.*

#### **Start-Up and Organizational Expenses**

Small business owners typically incur a wide range of costs in the launch of their business. The tax law allows them to deduct some of those costs in the year that the business starts and others they must amortize, or deduct, over the course of succeeding years.

These start-up costs include expenses incurred when investigating whether to start or buy a business and which business to start or buy. Costs range from market analysis and feasibility studies to advertising, consultant fees, attorney fees and accountant fees.

For 2010, a taxpayer is deemed to have made the election to deduct the first \$10,000 in start-up expenses paid or incurred during the year and to amortize the balance over 180 months, beginning in the month that the business was launched. However, the deduction phases out dollar-for-dollar if costs are greater than \$60,000, with no immediate deduction available when start-up costs are greater than \$70,000. All costs in that case must be amortized over 180 months.

## **Business Tax Credits**

### **Worker Retention Credit**

For tax years ending after March 18, 2010, an employer may take an additional general business tax credit for each formerly unemployed worker retained for at least one year. The credit is equal to the lesser of \$1,000 or 6.2% of the wages the taxpayer paid the retained worker during a specified 52-week period.

To qualify for the credit, the worker must begin employment after Feb. 3, 2010, and before Jan. 1, 2011, and not have been employed more than 40 hours during the 60-day period ending on the date the individual begins employment.

The worker must also not be employed to replace another employee, unless the former employee left employment voluntarily or for cause, or be engaged in agricultural labor. Other requirements pertain to the length of employment and amount of wages paid.

### **Tax Credits Extended through Dec. 31, 2011**

- Alcohol Used as Fuel
- Alternative Fuel Vehicle Refueling Property
- Biodiesel and Renewable Diesel Fuel
- Differential Wage Payment
- Indian Employment
- Mine Rescue Team Training
- New Energy-Efficient Home
- New Markets Tax
- Railroad Track Maintenance
- Refined Coal Production Facilities\*
- Research

\* For the production of electricity from renewable sources, see Code §45.

Also, certain organizational costs (up to \$5,000, subject to a dollar-for-dollar phaseout if costs are greater than \$50,000) incurred in the set up of a C or S corporation or a partnership can be deducted under the same rules for business start-up costs. Organizational costs include legal and accounting fees relating to the creation of the entity.

**Benefits:** *Promotes entrepreneurship and makes additional capital available to business owners that can be used for other purposes.*

### **Deductions for Health Insurance When Computing Self-Employment Tax**

In general, the self-employed (sole proprietor, partner or LLC member) must pay self-employment tax on business earnings. The tax is based on net earnings from self-employment and is equal to 15.3% (the social security tax rate of 12.4% plus the Medicare insurance tax rate of 2.9%). Typically, in determining net earnings from self-employment, several deductions are disallowed, including those for health insurance (even though health deductions are available in computing income tax).

*From payroll to sales tax to deductions, a CPA can educate you about year-round planning and tax season preparation.*



However, for 2010, self-employed persons may deduct health insurance costs incurred in 2010 for themselves, their spouse, their dependents and, effective starting March 30, 2010, any child of the taxpayer who, as of the end of the tax year, has not attained age 27.

**Benefit:** *Self-employed persons will pay less in taxes because the deduction will lower taxable income.*

### **Obtain Professional Advice**

A CPA tax professional understands the business of taxes and finances and can provide trusted advice and services for your small business during the tax season and throughout the calendar year.

**CPA**

**PCPS**

Private Companies Practice Session

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