Jobs and Growth Relief Act: Business Incentives

Benefits to Individuals

The 2003 Jobs and Growth Relief Act, designed to be an economic stimulant, has as one of its clear objectives, providing tax relief to the consumer. Consumer spending is a key to economic recovery. There are a number of provisions which should accelerate consumer spending.

One highly publicized provision is the immediate increase of the child tax credit from $600 per child to $1000. A married couple with adjusted gross income of less than $110,000 should have received a refund of $400 per child. Those who did not can receive this benefit when they file their 2003 income tax return.

The provision with the most impact on individuals are the individual income tax rate reductions. The 27%, 30%, 35%, and 38.6% tax rates have been lowered to 25%, 28%, 33% and 35% respectively in 2003.

Other benefits for individuals include an attempt to alleviate the "marriage penalty," by making the standard deduction for joint filers twice that of single filers, and increasing the size of the 15% bracket for joint filers to twice that of single filers. These changes minimize the inequity of joint filers paying more taxes than they would if they were filing separately.

Long term capital gains (from stock held for more than a year) has been reduced to 15% and income from qualifying dividends, which were taxed using ordinary income tax rates, has also been reduced to 15%.

Business Incentives

Depreciation "Bonus"

While considerable attention in reporting the new tax law has been paid to the benefits to the individual taxpayer, the changes that affect businesses, particularly small businesses, also should have substantial effects. These changes primarily affect depreciation.

Traditionally taxpayers recover the cost of assets used in a trade or business through annual depreciation deductions on their tax returns. The allowable deduction is calculated using rules called the "Modified Accelerated Cost Recovery System (MACRS). Factors in the calculation are cost, the recovery period (5-7 years for most machinery and equipment), the depreciation method, and the placed in service convention applicable to that type of property.

In 2002 Congress introduced a first year 30% "bonus" depreciation, allowing business to take 30% of the cost basis of the qualified property as a depreciation expense in addition to

the regular depreciation. The "bonus" applied to property acquired after September 10, 2001 and before September 11, 2004 and that was placed in service before January 1, 2005. The bonus depreciation is subtracted from the basis when calculating the regular depreciation.

The 2003 Act expands this bonus depreciation. Taxpayers can elect an additional first year depreciation of 50%. Under the new law the original use of the property must have commenced after May 5, 2003, and the property must be acquired after May 5th and before January 1, 2005.

Many states, including Pennsylvania, did not allow the original 30% bonus, and those who did may not increase it to 50%. It may be necessary to calculate depreciation separately for federal tax and state tax purposes.

Section 179 Expensing

Small Businesses can take advantage of the election under Section 179 of the tax code to expense the cost of depreciable assets in the year of acquisition under certain restrictions. Prior to this year there was a limit of $25,000 which could be expensed, and that amount was reduced dollar for dollar if the cost of depreciable property in that year exceeded $200,000. Also the amount expensed could not exceed the profits of the business, calculated before expensing depreciation. Clearly the law was designed to benefit profitable small businesses with modest capital investments.

The 2003 law increases the amount that can be expensed in the first year to $100,000 for property placed in service during tax years 2003, 2004, 2005. The annual investment limit has been raised to $400,000.

These liberalized depreciation rules will often require tax planning by small businesses to ensure that a current deduction can be fully utilized and results in the optimum tax benefit.

Dividends and Capital Gains

The changes in the taxable rates on income from dividends could have an effect on the decisions of C-corporations to distribute or increase dividends. Also lower capital gains tax rates represent a benefit to sellers of stock in closely-held businesses.

In addition to its effect on individual taxpayers, the Tax Act of 2003 should provide significant benefits to smaller businesses, promoting capital investment and expansion.

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