Year-End Tax Planning Considerations for Businesses

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In the wake of this year's elections and current economic climate, year-end tax planning is more important than ever. Here are our top 5 Tax Tips for businesses as we head to the close of 2012 from Keiter Tax Partner, Gary G. Wallace, CPA.

Tax Accounting Method Changes

Accrual basis business taxpayers may take advantage of allowable tax accounting methods to provide more tax beneficial timing of income and deductions. One example, is the opportunity for an accrual basis taxpayer to accelerate the deductibility of certain prepaid expenses. Another example, is the opportunity to defer income recognition of qualifying advance payments. The Internal Revenue Service allows a taxpayer to change a method by submitting Form 3115 to effectuate the change. Some changes may be completed without IRS approval while others require advance consent. A careful review of methods may be a beneficial planning exercise.

Dividend Payouts

Unless Congress takes action, the current federal individual tax rates on qualified dividends of 15 percent are set to return to pre-2003 rates. After 2012, the tax rates are scheduled to increase significantly to 39.6%, in addition to the possible new Medicare surtax of 3.8 percent.

For C corporations, distributing special dividends before 2013 may provide significant savings to individual shareholders as the top rates on dividends may more than double if legislative relief is not enacted.

Bonus Depreciation (§168) and §179 Expensing

Qualified depreciable property, having a recovery period of 20 years or less, and which is new and placed in service before January 1, 2013 is eligible for an additional 50 percent first-year bonus depreciation in 2012. However, this allowance is scheduled to expire after 2012. Businesses may want to consider accelerating planned purchases of qualified property before the end of 2012. Bonus depreciation is not mandatory, however, and certain taxpayers (flow-through businesses) may want to consider an election out of bonus depreciation in order to spread depreciation deductions evenly over future years due to the prospect of rising tax rates for individuals.

Substantial first-year write-offs are also available for the purchase of qualifying business vehicles placed into service in 2012. 2012 will be the final year for this deduction unless it is extended.

Under Code Section §179, businesses can claim a deduction for the entire cost of qualified property in its first year, as opposed to depreciating the cost over a number of years (qualified property must be tangible personal property, actively used in business, and for which a depreciation deduction would be allowed). Currently in 2012, the deduction is limited to $139,000, reduced by any amount over the $560,000 ceiling for qualified §179 property. For 2013, the dollar limit for the deduction is scheduled to drop to $25,000, with a $200,000 ceiling. Taxpayers may want to accelerate purchases of qualifying property into 2012 to take advantage of the §179 rules.

*Note: The §179 deduction is limited to the taxpayer's trade or business taxable income, and that any excess may be carried forward (unlike bonus depreciation, which may generate NOLs).

Tax Credits

The Work Opportunity Tax Credit is not available in 2012, with the exception that it has been extended for unemployed veterans and unemployed veterans with service connected disabilities. The qualified veteran must begin work for the employer before January 1, 2013.

The research tax credit expired after 2011; however, Congress may extend the credit before year-end 2012 on in 2013 and apply the extension retroactively to January 1, 2012.

Prospects for Tax Relief

Now that President Obama has been re-elected, difficult negotiations will begin between Republicans and Democrats over the fate of the Bush-era tax cuts, nearly $100 million in automatic spending cuts, and over 50 expiring tax extenders. Obama wants to increase tax rates for wealthy individuals and families, while keeping tax rates low for lower income taxpayers, as well as lower the corporate tax rate and reduce the nation's deficit overall.

Obama's proposal to reduce the maximum corporate tax rate from 35 percent to 28 percent is offset by a

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proposal to eliminate certain business tax preferences for oil and gas producers, eliminate loopholes, and broaden the base.

As for §179 expensing and bonus depreciation, it is unclear at this time whether these will be extended beyond 2012 and to what extent.

The aforementioned tax credits are likely to be extended, although conflicts among Congress and the White House may further limit the chances of extension.

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