

Small Business and Work Opportunity Tax Act of 2007, Part 1

Congress passed HR 2206 on May 24, 2007. On the very next day, May 25, President Bush signed the Bill. As a result, the controversial “**U.S. Troops Readiness, Veterans’ Care, Katrina Recovery, and Iraq Accountability Appropriations Act of 2007**” became law. Part of this controversial legislation was a little known tax act - **the Small Business and Work Opportunity Tax Act of 2007, [the 2007 SBA]**. This new legislation, on one hand, was designed to provide about \$5 billion of tax incentives (in 4 to 5 years) to small businesses, plus some qualified larger ones. On the other hand, it also created certain provisions to raise nearly \$5 billion new taxes to equalize the give away. .

Tax breaks are given in 4 basic categories: Small business tax incentives, Work opportunity tax credits, S Corporations’ relief, and the expansion of the GO Zone incentives. Plus certain unexpected changes for the 2006 Pension Protection Act.

(A) Provisions affecting small businesses.

(1) *Extend and enhance Section 179 small business expensing.* The (Code Sec. 179) expensing limit is increased from \$112,000 to \$125,000 for 2007. The investment-based expensing phase-out also increased from \$450,000 to \$500,000 for 2007. further, these figures will be indexed after 2007. This high level of expensing amount is extended to the end of 2010. In addition, if the amount of qualified expensing for one year is disallowed because the taxpayer did not have sufficient taxable income could be carried forward to future years .

The expensing deduction is not available to estates, trusts, and certain non-corporation lessors.

(2) *Federal minimum wages and tip credits.* Under the new law [2007 SBA], the Federal minimum level will be increased from \$5.15 per hour to \$7.25 per hour in three \$0.70 increments over the next two years. The first increase will occur on October 1, 2007. On that day, the Federal minimum wage will be \$5.85 per hour. One year after, on October 1, 2008, it will increase to \$6.55 an hour, and then to \$7.25 on October 1, 2009. This increase in minimum wages will not affect employers in California. The California state wide minimum wage will be increased to \$8.00 per hour on January 1, 2008. However, many other States having lower or no State minimum wage level will be impacted most. In order to alleviate some of the burden on small businesses, the new law, for all practical matter, **freezes** the Federal minimum wage at the current \$5.15 per hour level for the purposes of FICA tip credits. How can this “**freeze**” benefit small employers ?

Firstly, IRC Section 45B provides an income tax credit for FICA (Social Security and Medicare) taxes paid by food or beverage employers on certain amounts of employees’ tips. Generally, the IRC Section 45B tip credit is equal to the total FICA taxes that the employer paid on tips received by employees **minus** the amount of tips used to satisfy

the minimum wage requirement. If the minimum hourly wages increased by \$.70 per hour, the amount of tips needed to be used to satisfy the minimum wage will be \$.70 more per hour. Likewise, the amount needed to be subtracted from the total tips reported will also be \$.70 more per hour. Thus, the tax credit allowed will be smaller. If for FICA credit purpose, the minimum wage level freeze at \$5.15 per hour, the increase in Federal minimum wage level will have no impact on employers' FICA tax credits.

(3) ***Simplify family business tax.*** An unincorporated business that is jointly owned by a married couple in a Community Property state, there is no requirement for the married couple to file as a partnership. They are permitted to file as a sole proprietorship (under both laws, prior to or after the 2007 SBA). However, if an unincorporated business that is jointly owned by a married couple in a Common Law state, prior to the effective date of 2007 SBA, both the married couple and the business were subject to penalties for failing to file as a partnership. The new law allows married couple in a Common Law state to file as sole proprietorship. It also ensures that both spouses receive credit for paying Social Security and Medicare taxes.

(4) ***Waive individual and corporate AMT limitations on tip credits.*** Prior law limited a small business' ability to claim the tip credit by imposing a limitation that such credits could not be used to offset taxes that would be imposed under the alternative minimum tax (AMT). The new law provides a permanent waiver of the individual and corporate AMT limitations for purpose of the tip credit.

Next month we will talk about other incentives under the new law, i.e. the work opportunity tax credits and the S Corporation relief.