Protecting Americans From Tax Hikes Act of 2015

On December 18th, President Obama signed into law The Protecting Americans From Tax Hikes Act of 2015— the PATH Act. The product of eleventh-hour negotiations between Congressional leaders and the White House, the legislation makes permanent many popular tax incentives for individuals and businesses, providing tax certainty for those who were annually concerned if tax benefits were going to be extended. The Act also modifies some of the expiring tax breaks, and extends the rest for either two or five years, retroactive to the beginning of 2015. Some benefits are indexed to inflation; some are not. Here are some important highlights for business owners and higher-income taxpayers.

IRC Section 179 Small Business Expensing

The Act permanently sets the IRC Section 179 expensing limit at $500,000, with a dollar for dollar phase-out of the maximum deductible amount for purchases in excess of $2 million. Both amounts are indexed for inflation beginning in 2016. The Act permanently allows off-the-shelf software to be treated as Sec 179 property. The Act also makes permanent the special Section
179 expensing for certain real property—qualified leasehold improvement property, qualified restaurant property, and qualified improvement property—and removes the $250,000 cap related to this category of expenditure beginning in 2016.

Research Tax Credit

The research credit may be claimed for increases in business-related qualified research expenditures and for increases in payments to universities and other qualified organizations for basic research. Generally, the research credit equals 20% of the excess of the tax year’s qualified research expenses over a base amount. The Act permanently extends and enhances this tax provision. Also, beginning in 2016 eligible small businesses with $50 million or less in gross receipts may claim the credit against alternative minimum tax (AMT) liability, and startups with less than $5 million of gross receipts may claim up to $250,000 per year of their credit against their employer FICA tax liability.

Qualified Conservation Contributions

The Tax Code contains several rules to encourage the donation of appreciated capital gain real property to qualified charities for conservation purposes that are protected in perpetuity. The Act permanently extends the enhanced benefits for a contribution of a conservation easement. As a result, if you make a qualified conservation contribution, you may continue to claim a deduction of up to 50 percent of your Adjusted Gross Income (AGI), and the contribution may be carried forward up to 15 succeeding tax years. Conservation tax benefits claims have attracted significant IRS audits and scrutiny, so attention to detail is essential.

Charitable Distributions from Individual Retirement Accounts

The Act permanently extends the ability of individuals aged 70½ or older to transfer up to $100,000 from an IRA directly to a charitable organization without recognizing income or claiming a charitable contribution deduction. The transfer counts towards satisfying the minimum required distribution from a traditional IRA. The tax-free treatment reduces a taxpayer's AGI, which in turn lowers the floor for deducting medical expenses and miscellaneous deductions, and minimizing AGI may enable a taxpayer to stay below the threshold for the 3.8% surtax on net investment income ($250,000 married, $200,000 single).

Qualified Leasehold/Retail Improvements/Restaurant Property
The Act retroactively extends and makes permanent the 15-year straight line recovery period for depreciating qualified leasehold improvements, qualified retail improvements and qualified restaurant property placed in service after December 31, 2014. Without this extension, this property would be treated as nonresidential real property and depreciated using the straight-line method over 39 years.

Reduced Recognition Period for S Corporation Built-in Gains
An S corporation generally is not subject to tax, but instead passes through its income to its shareholders. However, when a C corporation is converted to an S corporation, the S corporation is subject to tax at the highest corporate rate if the corporate assets are sold at a gain during the built-in gain recognition period. The Act retroactively and permanently extends the shortened built-in gain recognition period of 5 years, which was set to increase back to 10 years. Other personal tax benefits that are permanently extended include, but are not limited to,

- Enhanced Child Tax Credit
- Enhanced American Opportunity Tax Credit
- Deduction of state and local general sales taxes in lieu of state and local income taxes
- Above-the-line deduction for certain out-of-pocket classroom expenses of elementary and secondary school teachers
- Transit benefits parity for employer-provided mass transit and parking benefits

Other business incentives that are permanently extended include the following:

- 100 percent exclusion for gain on sale of qualified small business stock
- Enhanced deduction for charitable contributions of food inventory
- Basis adjustment to stock of S corporations making charitable donations of property
- Employer wage credit for activated military reservists
- Subpart F exceptions for active financing income

The Act extends the following business tax incentives for five years through 2019. Congress decided that these provisions should not be made permanent, but were sufficiently important to be relied upon by taxpayers for longer than the usual two-year extension period:

Bonus Depreciation
To be eligible for bonus depreciation, qualified property must be depreciable under the Modified Accelerated Cost Recovery System (MACRS) and have a recovery period of 20 years or less, including computer software other than that covered by Code Section 179, or qualified leasehold improvement property. The property must be new and its original use must commence with the taxpayer. The additional first-year depreciation deduction is allowed for both regular tax and alternative minimum tax (AMT) purposes. The Act permanently extends bonus depreciation for qualified property purchased and placed in service from 2015 through 2019, allowing a 50% deduction for property placed in service from 2015 through 2017. The deduction is reduced to 40% in 2018 and 30% in 2019.

Work Opportunity Tax Credit
The Act retroactively extends through 2019 the Work Opportunity Tax Credit (WOTC), which rewards employers that hire individuals from targeted groups with a tax credit. Under the revived WOTC, employers hiring an individual within a targeted group (generally, otherwise hard-to-employ workers) are eligible for a credit generally equal to 40 percent of first-year wages up to $6,000. With respect to individuals who begin work for an employer after December 31, 2015, the credit also applies to employers who hire individuals who have been unemployed for 27 weeks or more.

A number of other tax incentives that were due to expire after 2014 are extended for two years through 2016. They include, among others:

- Above-the-line deduction for qualified tuition and fees for post-secondary education
- Deduction of mortgage insurance premiums as qualified residence interest
- Exclusion from gross income of discharge of qualified principal residence indebtedness
- Credit for nonbusiness energy property
- Credit for alternative fuel vehicle refueling property

There are a host of detailed, specific energy provisions for both individual and businesses, but most solar incentives are phased out completely after 2021.

The Act imposes a two-year moratorium on the ACA medical device tax and, with the Omnibus budget bill, delays the ACA excise tax on so-called “Cadillac” health insurance plans. The IRS receives a small increase in funding for 2016 to be used specifically for customer service, refund fraud prevention and cyber security enhancements. The Act prohibits IRS employees from using personal email for official business; the bill provides for termination of IRS employees when they delay or fail to perform work to benefit a political purpose.

Although the main focus of the PATH Act of 2015 involves the more than 50 temporary provisions known collectively as the "Tax Extenders", the Act contains numerous other provisions relating to tax administration, the Tax Court, the Affordable Care Act, Real Estate Investment Trusts (REITs), and more. The Act's tax measures touch nearly every individual and business. If you have any questions about how the legislation affects you, please contact your Bennett Thrasher representative.