



Small Business Tax Saving Strategies  
for the 2012 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 also serve as the growth engine of the U.S. economy.

Although uncertainty continues to cloud the nation's 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 in employees and equipment. 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 2012 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 Dec. 12, 2011.

Should you have any questions or concerns as you prepare your 2011 tax return – or as you evaluate your business's financial situation throughout the year – a CPA can help, by reviewing your overall position and providing you with the expert tax planning counsel you need today and in the years ahead. By combining unrivaled education, training and experience with a focus on your financial situation, a CPA can recommend sound strategies designed to make your goals a reality.

## Select 2011 Tax Provisions - Expense Related

### SECTION 179 EXPENSE DEDUCTION

Rather than capitalizing and depreciating the cost of property purchased for use in a business, the cost may be immediately deducted as a Section 179 expense. The deduction applies to most tangible personal business property placed in service during the tax year, including computers, office furniture, vehicles, and machinery. The deduction also is available in 2011 for the cost of certain real property: qualified restaurant property, leasehold improvement property and retail improvement property.

For 2011, business owners can use this deduction to write off up to \$500,000 of the cost of business property, regardless of whether the purchase was made with cash or credit. The deduction is reduced by every dollar spent more than \$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, although any unused depreciation can be carried forward, and the deduction does not apply to inherited property or property initially purchased for personal use, even if the property is later changed to business use.

The \$500,000 and \$2 million limits will, in 2012, return to prior thresholds of \$125,000 and \$500,000, adjusted for inflation. The IRS just released these inflation adjusted numbers. They are \$139,000 and \$560,000.

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

### BONUS DEPRECIATION

If the cost of business property cannot be immediately deducted as a Section 179 expense, the cost may be depreciated, allowing deductions over several years. For property placed in service before 2013, a special bonus depreciation allowance grants a larger deduction in the first year, with any remaining cost subject to regular depreciation rules in later years.

Bonus depreciation allows business owners to deduct the entire cost of the property placed in service in 2011, and half of the cost of property placed in service in 2012. The allowance generally applies to tangible personal property with a recovery period of 20 years or fewer, certain leasehold improvements, office equipment and purchased computer software, but only if the property is new, not used.

Deciding how best to maximize the tax benefits between bonus depreciation and section 179 depreciation is a question itself with variables that will depend on individual business circumstances.

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

### FUTURE PLANNING

- Have I created the most tax efficient type of business? For example, does it make sense to be a C Corp instead of an LLC if higher income tax rates are enacted next year?
- What is the best way to save for retirement that minimizes my taxes?
- What does the IRS consider a reasonable salary?
- I may expand my business across state lines — what do I need to consider about multi-state taxes?
- How do I eventually leave my business to a family member and avoid a huge tax bill?



## WHAT IS THE ALTERNATIVE MINIMUM TAX

The AMT is designed to ensure that certain taxpayers pay a minimum amount of tax. When the AMT is triggered, some tax advantages are recaptured and a two-tiered tax rate (a flat tax, in the case of corporations) applies to ordinary income above a certain exemption amount. Although tax planning aims to minimize your tax liability by taking advantage of various beneficial provisions, claiming tax breaks without also planning for their impact on AMT may end up triggering a significantly larger tax bill.

A certain amount of income is exempt from the AMT. The exemption amounts for individuals and other non-corporate taxpayers are not indexed for inflation, but Congress has consistently increased the exemption amounts through legislation. The current political climate is unpredictable, however, and unless Congress acts before Dec. 31, 2012, the exemption amounts will decrease to their pre-2001 thresholds. You may wonder why your estimated tax payments for 2012 are significantly higher. That is because until Congress approves the AMT indexing proposal for 2012, the law requires that estimates be made under the law as it stands, meaning a higher AMT for many.

## START-UP AND ORGANIZATIONAL EXPENSES

Small business owners typically incur a wide range of costs in the launch of their business. 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. The tax law allows business owners to deduct some of these costs in the year the business starts, and others must be deducted over the course of future years.

In 2011, a taxpayer may deduct up to \$5,000 of start-up expenses incurred during the tax year, decreased from \$10,000 in 2010. The balance must be amortized over 180 months, beginning in the month that the business was launched. However, the deduction phases out dollar-for-dollar in 2011 if costs are greater than \$50,000, with no immediate deduction available when start-up costs are greater than \$60,000. In that case, all costs must be amortized over 180 months.

Also, certain organizational costs incurred in the setup 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:** *It promotes entrepreneurship and makes additional capital available to business owners that can be used for other purposes.*

## Employee-Related

### EXPIRED DEDUCTION 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. For 2011, the tax is based on net earnings from self-employment and is comprised of two components: a Social Security tax of 10.4 percent on the first \$108,600 of your net earnings, and a Medicare tax of 2.9 percent on all of your net earnings.

In 2010, self-employed persons could deduct health insurance costs incurred for themselves, their spouse, their dependents and any child of the taxpayer who, as of the end of the tax year, had not attained age 27. This provision expired, however, and the deduction is disallowed for 2011. While this deduction can no longer be used to offset the employment tax, it can be subtracted from your gross income to help lower your liability.

**Downside:** *Self-employed persons may pay more taxes in 2011 than in 2010 because the deduction is no longer available.*

## FUTA TAX

Generally, all employers pay FUTA tax to support federal and state programs that pay benefits to unemployed workers. The amount of FUTA tax owed by an employer is a percentage of the total amount of wages paid by the employer during the year, limited to the first \$7,000 of wages paid to each employee during the year. The FUTA tax rate was set at 6.2 percent for many years, but it was reduced to 6.0 percent as of July 1, 2011.

If an employer is required to pay for a state unemployment program, the employer will be allowed a credit against FUTA tax. The credit is limited to 5.4 percent of wages, producing an effective FUTA tax rate of 0.6 percent in 2011 (for all of 2011, not just as of July 1).

**Benefit:** *Employers pay lower FUTA taxes in 2011.*

## WORKER RETENTION CREDIT

An employer may take an additional general business tax credit for each worker hired after March 18, 2010, and before Jan. 1, 2011, if the worker was previously unemployed and is retained for at least one year. Thus, although the credit is available for employees hired in 2010, the credit can only be claimed for tax years beginning in 2011.

The credit is equal to the lesser of \$1,000 or 6.2 percent of the wages the taxpayer paid to the retained worker during the one-year period.

**Benefit:** *Employers receive a higher general business credit.*

## SMALL BUSINESS HEALTH INSURANCE CREDIT

Beginning in 2010, a credit is available for small business owners who pay at least half of 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 affect the extent to which the credit can be applied. Unfortunately, determining whether you are eligible the credit may be difficult, as the credit requires significant information analysis and complex calculations.

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

The credit can be claimed for each tax year in which the employer qualifies in 2010–2013 and for any two years after that. It can also offset the Alternative Minimum Tax (AMT).

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

## DO I NEED TO REPORT MY FOREIGN ASSETS? WHY YOU NEED TO CARE

If you own a bank account, real estate, business or other similar asset located in a foreign country, and you have not disclosed your ownership to the IRS, you may be subject to onerous penalties. A CPA will help you come into full compliance and may be able to limit any applicable penalties.



## FILING DEADLINE FOR FORM 1040

April 15 is, of course, the due date for filing Form 1040. In 2012, however, the deadline for filing your 2011 1040 is moved to April 17, a Tuesday, to accommodate a weekend and a holiday in the District of Columbia.

## Information Reporting

### NEW 1099 REPORTING REQUIREMENTS

After 2011, merchants conducting credit card, debit card or gift card transactions will receive a Form 1099-K from the card processing company, who will also file a copy with the IRS. Payments made through a third party such as PayPal or eBay, will be reported only if the payee receives more than \$20,000 in aggregate and the total number of payment transactions exceeds 200. Although the 1099-K reporting requirement does not oblige merchants to file any new information with the IRS, the reporting requirement will increase the information the IRS receives with respect to merchants and requires merchants to establish new accounting procedures. Backup withholding may apply to a merchant if the merchant does not provide a correct taxpayer identification number (TIN), such as an employer identification number (EIN), to the card processing company, but the IRS has delayed this requirement until after 2012.

Businesses were almost subject to two other new reporting requirements, but after pushback from the business community, the AICPA and others, these rules were repealed before they could come into full effect. The first provision would have required that businesses who make payments to a service provider aggregating \$600 or more to report payments (on 1099 MISC) to corporations starting in 2011. The second provision would have required individuals receiving rental income from real estate to file information returns for payments made after Dec. 31, 2010.

**Downside:** *The IRS will have more information on the gross receipts of merchants who accept credit cards.*

### NEW 1099 REPORTING PENALTIES

A penalty may be imposed for persons who fail to file a correct and timely information statement with the IRS or who fail to furnish a correct and timely payee statement. The amounts of these penalties have increased for returns filed on or after Jan. 1, 2011. Both penalties are now \$100 per return, reduced to \$30 for returns fewer than 30 days late and to \$60 for returns 30 or more days late that are filed before Aug. 1. The penalties are capped at a certain amount, depending on the amount of the per-return penalty and the gross receipts of the business. The penalties may be waived for reasonable cause or increased in cases of intentional disregard.

**Downside:** *Businesses may be subject to increased penalties.*

## General

### 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 percent (the highest corporate tax rate).

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. The recognition period is scheduled to reset to 10 years for tax years beginning in 2012.

**Benefit:** *It lowers the tax burden on S corporation shareholders.*

### NET OPERATING LOSSES

When a business's deductions exceed its income, a net operating loss (NOL) arises, which may be carried either back or forward to offset gain in past or future years. Significant planning is required to maximize an NOL. Factors that must be taken into account include the business's tax liability in past years, anticipated gains in future years, the expected tax rates in future years, whether the entire NOL will be used before it expires in 20 years, and whether the business is, or will be, subject to the AMT.

Additionally, a decision may need to be made about whether to take the Section 179 expense deduction or to generate an NOL. The Section 179 deduction cannot create an NOL and cannot be carried back to prior years in some cases, it may be advantageous to instead depreciate the relevant cost and create an NOL carryback.

The decision to claim bonus depreciation may be affected by the presence of NOLs. If an NOL carryforward is about to expire, it may be beneficial to forgo bonus depreciation in favor of the regular depreciation rules. State tax laws add an additional layer of complexity to this decision, because some states have more restrictive NOL carryover rules.

## OBTAIN PROFESSIONAL ADVICE

When the right tax and financial advice is essential, talk to someone with an unmatched level of knowledge, experience and education. A CPA 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.



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