



Impact of ARRA on Pennsylvania: The Effect of Individual and Business Tax Credits and Incentives

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Introductions

- The Pennsylvania Institute of Certified Public Accountants (PICPA) is a professional association of more than 19,000 CPAs working together to improve the profession and better serve the public interest.
- Membership includes practitioners in public accounting, industry, government, and education.
- Headquartered in Philadelphia, PICPA has a government relations office in Harrisburg and a regional office in Pittsburgh.



Introductions

- Representatives from the Federal Tax Committee (“FTC”) of the PICPA:
 - Nicholas J. Crocetti, CPA and FTC Chair
 - Margie Navarro, CPA and FTC Member
 - Edward R. Jenkins, CPA, FTC Member, and PICPA Liaison to the IRS



Objectives

- After this presentation you should:
 - Appreciate the background in which the American Recovery and Reinvestment Act of 2009 (“ARRA”) was enacted
 - Be familiar with the tax credits and incentives included in the ARRA that benefit individuals in Pennsylvania (“PA”)
 - Be familiar with the tax credits and incentives included in the ARRA that benefit businesses in PA
 - Understand the impact of those credits and incentives on PA individuals and businesses



ARRA Background

- Economy was crashing
- Destabilized financial institutions and industries
 - 99 banks failed in 2009, 128 since 2008
- Monetary policy exhausted with the reduced Federal discount rate
 - Monetary policy was chief economic policy tool for many decades
 - New administration and Congress came in with no monetary policy tools left
- Action was needed
 - Much of consumer and investor behavior and economic decision making is based upon perception
 - By doing something, Congress thought they could enhance consumer and investor perceptions and confidence



ARRA Background

The only tools left were fiscal policy and the ARRA contains many selective and targeted benefits to stimulate the segments of the economy that Congress thought would help pull the economy out of a tail spin



ARRA Background

- Fiscal policy is rooted in Keynesian economics, an economic philosophy that presumes the government is responsible for “managing” the economy
- Theoretically, a multiplier effect exists to magnify the effect of stimulation
- Stimulative fiscal policy has winners and losers; because the government uses taxpayers’ money to re-distribute to the sectors the government wishes to stimulate



ARRA Background

Our presentation today is intended to highlight tax credits and incentives in the ARRA for individuals and businesses; and specifically to help the Commission appreciate the winners and losers from ARRA in Pennsylvania.



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Credits and Incentives for Individuals

Making Work Pay Credit - Credit of 6.2% of earned income up to a maximum of \$400 single (\$800 joint) for tax years 2009 and 2010

- **Background**

- Second round of stimulus payments
- Paid by reducing withholding
- Refundable

- **Limits**

- Phases out above \$75k (\$150k joint MAGI)

- **Special**

- Coordination with pensioners' benefit
- Definition of "Earned Income"

- **Problems**

- Under withholding

- **PA Estimated Effect:**
\$2,245,000,000



Credits and Incentives for Individuals

Earned Income Tax Credit

Temporary increase in EITC for taxable years 2009 and 2010

Background

- Increases phase-out figure and indexed for inflation
- Refundable credit
- Three schedules before change
- Adds an additional level for three or more children
- Adds another 5% to the credit

- Limits
 - Phases out above specified ranges for each level
 - No MFS
 - Investment income $< \$2,950$
- Qualifications: three or more children
- Special:
 - Definition of “Earned Income”
- Problems – Under withholding
- PA Estimated Effect: No reliable estimate



Credits and Incentives for Individuals

Child Tax Credit

Temporarily reduce the earnings threshold for the refundable portion of the child tax credit for taxable years 2009 and 2010

Background

- Credit is \$1,000 per child who is under the age of 17
- To extent CTC exceeds taxpayer liability, CTC is refundable up to 15% of earned income in excess of a threshold

- Limits

- Threshold was indexed to increase in 2009, \$10,000 for 2008.
- ARRA changes threshold to \$3,000 for 2009 and 2010
- Phases out above \$75k (\$110k joint)

- Qualifications: available for up to five children
- PA Estimated Effect: No reliable estimate



Credits and Incentives for Individuals

American Opportunity Tax Credit (AOTC) Amends Hope Credit for 2009 and 2010

Background

- Credit coordinates with other education provisions
- Hope Credit was for first two years of post-secondary education (“PSE”) to a maximum of \$1,800
- Formula was 100% of the first \$1,200 of qualified education expenses (“QEE”) and 50% of the next \$1,200

Background (cont’d)

- AOTC is 100% of the first \$2,000 of QEE plus 25% of the next \$2,000 of QEE
- New maximum is \$2,500
- Applies to all four years of PSE
- 40% of credit now refundable
- Adds textbooks to QEE
- Limits
 - Phases out at MAGI above \$80k (\$160k joint) for 2009
 - No MFS
- PA Estimated Effect: \$592,000,000



Credits and Incentives for Individuals

First-Time Home Buyer Credit

Background

- Credit was \$7,500 (\$3,750 MFS) to be repaid over 15 years
- New credit level is \$8,000 (\$4,000 MFS)
- Credit repayment is waived
- First-time home purchases from July 1, 2009 through December 1, 2009

PA Estimated Effect: No reliable estimate

Exclusion of up to \$2,400 of Unemployment Compensation Income from AGI

Background

- Unemployment compensation received is taxable
- First \$2,400 is now excluded
- Effective for years beginning in 2009

PA Estimated Effect: \$180,000,000



Credits and Incentives for Individuals

Sales Tax Deduction on car and truck purchases “above the line”

Background

- Itemizers could deduct, non itemizers could not
- Coordinated above the line deduction now permitted

Limits

- Phases out at \$125,000 of MAGI (\$250,000 joint)
- Maximum sales tax base (purchase price) is \$49,500
- Applies 1/1/09 to 12/31/09

PA Estimated Effect: No reliable estimate

Alternative Minimum Tax (AMT) Relief

Background

- Exemption amounts increased to \$46,700 (\$70,950 joint) instead of \$46,200 and \$69,950 for 2009
- Can use non-refundable personal credits to offset AMT

PA Estimated Effect: No reliable estimate

Certain Energy Credits Enhanced – Not Included in Scope of Presentation



Credits and Incentives for Individuals

Recovery Payments to Retirees and the Disabled

Background

- Recognizes that retirees and disabled persons are also affected by the economic circumstances
- Payment of \$250 to each recipient
- Applies to Social Security Insurance, Railroad Retirement Benefits, and Veterans Benefits recipients

Government Retiree Benefit Background

- Coordinates with the Recovery Payments to Retirees under §2201
- Tax credit of \$250 (\$500 joint) for 2009
- Covers government retirees not covered by SS, RRB or VA.

PA Estimated Effect of Both:
\$471,000,000



Credits and Incentives for Individuals

Premium Assistance for COBRA Continuation Coverage

Provides a 65% COBRA premium reimbursement for up to nine months for terminated employees

Background

- Recognizes that unemployed persons place further strain on health care providers and systems.
- Lack of health insurance coverage can snowball for displaced workers
- Former employee pays 35% of the COBRA payment

Background (cont'd)

- Remaining COBRA payment is reimbursed to employer by a reduction of payroll tax liabilities

Limit

- Phases out at \$125,000 (\$250,000 joint) AGI

Problem: Company reimbursement of the 65% government subsidy via payroll tax liability reduction

PA Estimated Effect: No reliable estimate



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Credits and Incentives for Businesses

Bonus Depreciation Extended

Background

- Special 2008 provision permitted an additional cost recovery allowance (depreciation) of 50% of the cost of property placed in service
- Concept is to promote business investment in capital equipment to stimulate capital goods production and employment; effectively providing a source of cash financing via a substantial tax bill reduction

Background (cont'd)

- Additional allowance reduced adjusted basis on which the regular MACRS is calculated
- ARRA extends the bonus depreciation to 2009
- Can create an NOL to be carried back

PA Estimated Effect: No reliable estimate but benefit is significant and the benefit depends upon capital investment in 2009



Credits and Incentives for Businesses

Section 179 Capital Asset Expensing Election Extended

Background

- Special 2008 provision permitted an increase in the amount of Section 179 expensing to \$250,000 from \$125,000
- 2008 provision increased the dollar limitation of total capital expenditures from \$500,000 to \$800,000
- ARRA extends those provisions to 2009

Background (cont'd)

- Concept is to promote business investment in capital equipment to stimulate capital goods production and employment; effectively providing a source of cash financing via a substantial tax bill reduction
- Can't create an NOL

Limit: 2008 limit on total capital expenditures of \$800,000 extended to 2009

PA Estimated Effect: No reliable estimate and benefit depends upon capital spending



Credits and Incentives for Businesses

Five-Year Carryback of NOL for Smaller Businesses

Background

- Normal NOL carryback limitation is two years, then losses carry forward twenty
- ARRA permits 2008 NOL to be carried back up to five tax years to recover taxes paid therein; unabsorbed losses then carry forward twenty

Background (cont'd)

- Concept is to infuse cash into companies with losses; effectively providing a source of cash financing of those losses via a recoupment of prior year taxes

PA Estimated Effect: No reliable estimate



Credits and Incentives for Businesses

Deferral of Income Recognition Arising from Cancellation of Indebtedness

Background

- Normal COI income is included in taxable income in the year of discharge; unless certain circumstances exist like bankruptcy or insolvency
- Concept is to avoid a cash drain for taxes in struggling companies that receive a discharge from indebtedness

Background (cont'd)

- ARRA permits deferral of COI recognition for discharges occurring in 2009 and 2010. COI is recognized ratably over a five year-period beginning with four (discharges 2010) or five years (discharges in 2009) from the year of deferral.

PA Estimated Effect: No reliable estimate but JCT expects a significant impact nationally



Credits and Incentives for Businesses

Additional Research Credits

Background

- Corporations can elect to claim additional Research to Minimum Tax Credits instead of bonus depreciation
- Concept is to create a monetary incentive to invest in capital equipment, effectively providing a source of partial financing

Background (cont'd)

- The research or minimum tax credit limitation is increased by the bonus depreciation amount, which is equal to 20% of the bonus depreciation for eligible property placed in service.

PA Estimated Effect: No reliable estimate



Credits and Incentives for Businesses

Work Opportunity Credit Enhanced

Background

- Credit is available on an elective basis for employers hiring individuals from one of nine targeted groups and it is based upon the amount of qualified wages paid to those employees
- Credit is generally 40% of the qualified wages up to \$6,000 (\$12,000 for certain veterans)

Background (cont'd)

- ARRA adds a tenth group, unemployed veterans and “disconnected” youth
- Applies to specified individuals hired in 2009 and 2010

PA Estimated Effect: No reliable estimate



Credits and Incentives for Businesses

Partial Exclusion for Gain from Certain Business Stock

Background

- Prior to ARRA the gain from specified small business stock enjoyed favorable tax treatment through reduced rates and the exclusion was limited to 50% of the gain
- ARRA expands the exclusion to 75% of the gain and enhances the applicable tax rates

PA Estimated Effect: No reliable estimate

S Corporation Build In Gains Tax Holding Period Changed

Background

- BIG occurs when a C corporation elects Subchapter S tax treatment and the corporation owns substantially appreciated assets
- No corporate level gain is recognized on S conversion if the assets are not converted within 10 years
- ARRA reduced the holding period from 10 years to seven

PA Estimated Effect: No reliable estimate



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PA Effect – The Cost to Residents

We must repay the borrowings of the Federal government plus interest

- JCT estimate of ARRA spending:
\$326,412,000,000 net over the years 2009-2019
- US population at 7/1/08: 304,059,724
- Approximate per capita cost \$1,073
- PA cost \$13,306,229,007 for our 12,400,959 residents



PA Effect – Costs

We all lose due to the complexity of the Internal Revenue Code and the attendant compliance costs for government and taxpayers



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That's a Wrap

- Questions?