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Tax Law Alert

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Taking the PATH (Act) to Tax Extenders

On December 18th President Obama signed into law The "Protecting Americans from Tax Hikes" (PATH) Act of 2015, which makes certain tax extenders permanent and retroactively extends others for two or more years. The PATH Act provides greater certainty for both businesses and individuals. The following is a synopsis of certain provisions that I feel are most relevant for such taxpayers.

- **Section 179 Expensing** – The maximum expensing deduction of $500,000 for qualified business property has been permanently restored with a phase-out threshold of $2 million. Both amounts will be indexed for inflation.

- **Research and Development Credit** – The R&D credit is made permanent (with certain modifications) and available to taxpayers with specified increases in business-related qualified research expenditures and for increases in payments to universities and other qualified organizations.

- **Qualified Small Business Stock (QSBS)** – The 100% tax exclusion for non-corporate investors in QSBS held for five years was retroactively extended and made permanent.

- **S Corporations** – The period for recognizing built-in gain (BIG) upon the conversion of C Corp to an S Corp is made permanent at five years. In addition, the basis adjustment in stock when an S Corp makes a charitable donation of property has been permanently extended.

- **Bonus Depreciation** – Bonus depreciation for qualified business property is retroactively extended for 2015 and 2016. It is phased out beginning in 2017 at 50%; decreases to 40% for 2018 and 30% for 2019; and completely expires thereafter (unless extended). In addition, the election to accelerate the use of AMT credits in lieu of bonus depreciation continues.

- **15-year Cost Recovery** – The provision allowing taxpayers to use a straight-line cost recovery period of 15 years for qualified leasehold improvements, restaurant property and retail improvements has been permanently extended.

- **Work Opportunity Tax Credit (WOTC)** – The WOTC has been extended (with minor modifications) through 2019 to encourage employers to hire certain long-term unemployed individuals, including military veterans.

- **New Market Tax Credit** – The PATH Act authorizes allocation of $3.5 billion of new market tax credits for each year from 2015 through 2019.

- **Controlled Foreign Corporations** – The look-through treatment of payments of dividends, interest, rents and royalties between related controlled foreign corporations has been extended through 2019.

- **Affordable Care Act (ACA)** – The ACA excise tax on high-priced health insurance plans (known as "Cadillac" plans) has been delayed for two more years until 2020. In addition, a moratorium on the ACA excise tax on medical devices has been imposed on the sale of certain medical devices for two years (2016 and 2017) and the health insurance provider fee for one year (2017).

- **State and Local Sales Tax Deduction** – The ability of taxpayers to elect to claim an itemized deduction for state and local sales taxes in lieu of deducting state and local income taxes has been permanently extended.

- **American Opportunity Tax Credit (AOTC)** – The PATH Act makes permanent an enhanced AOTC, with a maximum deduction of $2,500 and with AGI phase-out amounts of $80,000 for single filers and $160,000 for married filing jointly.

- **Qualified Tuition and Related Expenses Deduction** – Taxpayers may claim a deduction for tuition and fees (subject to phase outs) in lieu of two other higher education credits available to parents of college students through 2016.

- **Child Tax Credit** – The enhanced Child Tax Credit is made permanent allowing for a refundable portion with a reduced income threshold amount of an unindexed $3,000.

- **Charitable Distributions from IRAs** – The provision for individuals age 70 ½ or older to be allowed to make tax-free distributions from their IRAs to qualified charities, with a limit of $100,000 per taxpayer, has been permanently extended.

- **Qualified Conservation Contributions** – The special rule allowing the contribution of capital gain real property for conservation purposes, with the contribution to be taken against 50% of the base, has been permanently extended.

- **Earned Income Credit (EIC)** – Certain enhancements in the EIC for lower-income taxpayers, including the increased 45% credit percentage for taxpayers with three or more qualifying children, have been made permanent.

- **Employee Transit Expenses** – The tax-free monthly benefit for mass transit passes, vanpooling and parking fees has been permanently equalized at $250 ($255 for 2016) and will be indexed for inflation beginning in 2016.

- **Teachers' Classroom Expense Deduction** – The $250 above-the-line deduction for qualified out-of-pocket expenses (now to include "professional development expenses") of elementary and secondary school teachers has been made permanent and will be indexed for inflation beginning in 2016.

- **Mortgage Debt Exclusion** – The exclusion for mortgage forgiveness of up to $2 million ($1 million for a married taxpayer filing separately) on a taxpayer's principal residence has been extended with certain modifications through 2016.

- **Mortgage Insurance Premiums** – The ability of taxpayers to deduct mortgage insurance premiums as deductible interest subject to AGI phase-outs has been extended through 2016.

- **Residential Energy Credits** – A lifetime credit of up to $500 for 10% of qualified expenses has been extended through 2016.

- **Savings Incentive Match Plan for Employees (SIMPLE)** – Taxpayers are permitted tax-free rollovers from employer-sponsored qualified plans to a SIMPLE plan.

- **Section 529 Plans** – The ability to use funds in a Section 529 Plan towards the purchase of computers and related equipment as a qualified expense has been made permanent.

- **Achieving a Better Life Experience (ABLE) Accounts** – Tax-free rollovers from a 529 Plan account to an ABLE Account are allowed, and the prior requirement that ABLE Accounts may be established only in the taxpayer's state of residence has been removed.

- **Partnerships** – The PATH Act made some technical corrections and clarifications to the partnership audit rules, including a new IRC Section 6225(c)(3) relating to a "specified passive activity loss" for partners in certain publicly traded partnerships.

- **Real Estate Investment Trust (REITs)** – The PATH Act includes favorable tax provisions for REITs, including tax-free spin-offs.

- **Taxpayer Bill of Rights** – The Taxpayer Bill of Rights has been made a permanent part of the Internal Revenue Code.

At over 200 pages, the PATH Act is more extensive than previous tax extender laws. This Tax Law Alert provides only a brief synopsis of certain provisions that I have singled out as most relevant to businesses and individuals. If you have questions on any provisions of the PATH Act, please call me directly at (860) 240-1052.

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This issue of the Tax Law Alert was written by Christopher J. Rixon, Chair of the Tax Group at Reid and Riege, P.C. The Tax Group works with business lawyers on issues of choices of entities, formation and operation, as well as taxable and/or tax-free transactions. The Group is involved with decisions involving capitalization, working with commercial and transactional lawyers in structuring and determining levels of equity, debt and various hybrids. The Tax Group is also called upon to work outside the Business Law Practice Area with respect to issues of pensions and profit sharing arrangements, trusts and estates, personal wealth planning, real estate transactions and financing, litigation and settlement agreements, health care and nonprofit law. The attorneys in Reid and Riege's Business Law Practice Area provide general counsel and transactional representation to businesses, their owners and the institutions who finance them. That representation may involve the formation and ownership of a new business, the transition of an existing family business from one generation to the next, structuring buy-sell arrangements between owners of a business or the disputes that sometimes arise among owners of a business.

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