

Economic Stimulus Package Includes Powerful Tax Incentives for Investment

The Economic Stimulus Act of 2008 signed into law by President Bush on February 13, 2008 includes two significant business related tax incentives that may lower your cost of investing in new equipment and spur new orders from customers. Increased expensing limits for small businesses and a 50 percent "bonus" depreciation provision will provide a benefit to businesses of all sizes. In fact, small businesses that qualify for the increased expensing can also take advantage of the bonus depreciation. The two provisions along with examples are briefly described below.

Expanded Expensing (Sec. 179) for Small Businesses

Companies that purchase less than \$800,000 of capital assets in a year now can expense (i.e., deduct currently) the first \$250,000 of capital investment, effective for purchases made in 2008 (the prior limits for 2008 were \$128,000 and \$510,000 respectively).

Example

For example, a qualifying business owner who buys a \$250,000 machine can deduct the total cost of the equipment the year it's purchased. If the equipment costs more than \$250,000, but the company spends less than \$800,000 on capital equipment during 2008, the company can couple expanded expensing with accelerated depreciation (see below). Under these provisions, a \$300,000 machine that is MACRS 5-year property would qualify for a \$280,000 first year deduction (93 percent of the cost of the asset); and a \$500,000 machine could qualify for a \$400,000 first year deduction (80 percent of the cost of the asset).

Accelerated Depreciation for All Businesses

The new law also includes a new 50 percent expensing allowance (also known as bonus or accelerated depreciation) that generally applies to capital equipment purchased and placed in service during 2008. This incentive is available to all companies, regardless of the size of their investment.

Under this provision, companies are eligible for a "bonus" first-year depreciation totaling 50 percent of the cost of the investment and can depreciate the remaining basis of the asset under the regular depreciation rules. Smaller companies get even more of a "bonus." As described above, they can first take advantage of expensing and then also use the 50 percent expensing allowance.

QUALIFIED PROPERTY

In order for property to qualify for the bonus depreciation deduction, it must meet the following requirements.

First, the property must be one of the following types of property: (1) property to which the general rules of MACRS apply having a recovery period of 20 years or less, (2) water utility property, (3) computer software other than computer software recovered under section 197, or (4) be qualified leasehold improvement property.

Second, the original use of the property must commence with the taxpayer after December 31, 2007. Original use means the first use to which the property is put by anyone.

Third, the property must be purchased within the applicable time period (after December 31, 2007 and before January 1, 2009).

Finally, the property must be placed in service before December 31, 2007 and before January 1, 2009. With respect to self-constructed property, an extended placed-in-service date is allowed if the production period exceeds two years or has an estimated production period exceeding one year and a cost exceeding \$1 million.

Example

The 50 percent bonus depreciation deduction is computed first. The bonus deduction reduces the adjusted basis of the property before computing the amount otherwise allowable as depreciation deduction under section 167(a). For example, assume that on March 1, 2008, a calendar year taxpayer acquires and places in service qualified property that costs \$1,000,000. Under the new law, the taxpayer is allowed a first year bonus depreciation deduction of \$500,000. The remaining \$500,000 of adjusted basis is recovered in 2008 and subsequent years pursuant to the depreciation rules of present law.

Assuming the qualified property was MACRS five-year property, the taxpayer would be allowed to recover 20 percent of the remaining adjusted basis of \$500,000 -- or \$100,000 -- in 2008. The total depreciation deduction for the MACRS five-year class life property would be equal to \$600,000 (\$500,000 + \$100,000) or 60 percent of the adjusted basis of the property originally placed in service in 2008.

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