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With four specific services, The Center provides complete unbiased planning. The Center does not sell any products; its main purpose is to provide advice. Local experts are retained to implement the plans developed by the Center. The Center for Financial, Legal & Tax Planning is located at 4501 W. DeYoung Street, Suite 200, Marion, Illinois 62959. Phone 618-997-3436; Fax 618-997-8370.

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American Jobs Creation Act: *Explanations and Strategies*

Be aware! The American Jobs Creation Act of 2005 became law as of October 22, 2004. Because of this new Act, business taxpayers have new opportunities to cut their tax burden. This article will describe major portions of the Act and describe useful strategies to utilizing the Act to your advantage.

The benefits of this tax bill are more targeted than its predecessors. An example of this involves manufacturing. This Act makes a vengeful attempt to help manufacturing through the use of lower rates. Along with the targeted benefits, the American Jobs Creation Act of 2004 patches loopholes. The result will make the tax code more complex. Let's look at some details.

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Financial Background

The American Jobs Creation Act is the fifth major tax cut in four years and contains tax cuts of $145 billion. Unlike previous tax bills, this tax cut is projected to be fully paid for within the 10-year budget period. The use of phase-ins and phase-outs were once again used to achieve this balance.

Manufacturer's Deduction

Given the beating United States manufacturers have taken in the past ten years regarding job creation, Congress has created new deductions for manufacturers. Most manufacturers in the United States are 35% taxpayers. This means any 3% drop in income drops their income taxes by approximately 1%.

The Act lowers the tax rate for a number of years. In 2005 and 2006, manufacturers will be allowed to deduct 3% of their income against their federal income tax to achieve a lower rate. In 2007, 2008, and 2009, the rate will be 6%. In 2010, the rate will max out at 9%. The effect of the deductions is that the top corporate rate will drop from 35% to 32%.

Lawmakers have also expanded the definition of "manufacturing" substantially to include many more businesses that were before never thought of as manufacturers. Manufacturers now include software, film, and even energy production, but do not include companies that are involved in the transportation or resale of the goods.

Strategy: Manufacturing is not for everyone. However, if you are interested in starting or investing in a manufacturing business, now may be the time to do so. The low tax rates will result in both lower taxes and higher returns on investment. Additionally, it may be advantageous to open a C Corporation to manufacture goods. Because the tax treatment may be more favorable than that of other types of businesses, C Corporations may see a surge in number.

Small Business Expense/Depreciation

Congress has extended the $100,000 Section 179 deduction through 2007. Without the deduction, the provision would have only been in effect until December 2005.

Strategy: It is still a good time to buy equipment. If you are faced with a tax liability, try to eliminate it with a large purchase of equipment for your business.

SUV Loophole

When Congress passed a cap limiting the amount companies can deduct for automobiles, Congress never anticipated SUVs becoming popular. The result was a loophole allowing business owners to deduct the purchase of large SUVs, but not allowing them to deduct economical automobiles. Formerly, businesses could take advantage of this loophole if the gross capacity of the vehicle was over 6,000 pounds.

No longer is that the case. Congress has now lifted the gross vehicle weight of a vehicle to 14,000 pounds to qualify for an immediate deduction.

Strategy: This loophole is not entirely closed. Certainly vehicles such as Hummers, Suburbans, and other large SUVs have been eliminated from the list of vehicles which can be deducted. However, Congress neglected the fact that ultra large SUVs have made their debut. Though it may seem ridiculous, Freightliner and International have SUVs with gross vehicle weights of over 14,000 pounds. The price tags on these vehicles range upwards of $80,000. Though it may seem ludicrous to buy one of these vehicles, they get excellent gas mileage, have excellent resale value, are safe, and qualify for the tax deduction. As a result, the cash flow cost to you is reduced to $53,000, disregarding the resale or trade-in value.

If these ultra large SUVs don't suit your business, you can still take deductions for vehicles if they relate to your business no matter what their gross weight is. Such examples include hearses for funeral homes, trucks with gross vehicle weights of under 14,000 pounds in a mechanic's business, and other specialty vehicles if they relate to a business.

S Corporations

S Corporations have also been reformed. The number of owners now able to own one S Corporation has been increased from 75 to 100. All family members in one family are considered to be one shareholder. This is good news in light of the proliferation of Subchapter S Corporations and the growth that they have seen over the years.

Strategy: S Corporations are still a good idea! Opening one today and selling investments to partners is a good idea.

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Sales Taxes

In a surprise move, Congress made states' sales taxes deductible. Taxpayers must itemize to get the deduction just as they have had to do state and local income taxes. Taxpayers can either substantiate the expense with receipts or use tables. The sales tax deduction is now an alternative to deducting state income taxes.

Strategy: This provision is relatively useless if you live in a state with an income tax. However, if you live in a state with an income tax, you can still take special advantage of this provision. You can do this by making a purchase of a large product this year, such as a yacht, plane, or large camper.

Farmers

Farmers also benefit from this bill. When weather forces farmers to sell livestock prematurely, they now have four years to defer gains instead of having to book the revenue within two years. Farmers are also allowed special averaging for the Alternative Minimum Tax. In a more controversial move, Congress has added a $10 billion buyout for tobacco farmers.

Strategy: Now is a great time to get out of farming if you desire to do so. The capital gains rates and ordinary gains rates are low. In addition to that, interest rates are at 50-year lows. The combined result is that land can sell for more and still be taxed to the seller at a lower rate than in past years.

Tax Shelters

As part of their major crack-down on tax shelters, Congress has made substantial penalties higher than what they were previously. The statute of limitations has been extended and other rules to break abusive shelters have been established.

Strategy: If you are in an illegal tax shelter, get out of it. Granted, the time for forgiveness from the IRS has passed, but dealing with these situations actively as opposed to passively is a strategic advantage in this situation.

Partnerships

Partnerships have been the most affected by direct provisions of the Act. The Act no longer allows partnerships to shift built-in losses to subsidiaries. In the event an asset is transferred or distributed to a partner, the basis of the assets must be adjusted.

There has also been some confusion as to whether the partnership must recognize discharge of indebtedness as income. The answer throughout the Act is now a resounding yes.

Strategy: While it may be convenient to use partnerships for tax strategies, only use partnerships for legitimate business purposes. There are other ways to take losses and gains while minimizing tax liabilities.

Conclusion

Through the American Jobs Creation Act of 2004, Congress has created this rule with the purpose of targeting particular issues. Consequently this Act has added quite a bit of complexity to the tax code. Contact the professionals at The Center for further assistance regarding administration and tax planning if needed.