THE D. J. MARCUS LAW FIRM LLC

Small Business Jobs Act and Your Small Business

Adapted from a blog post at http://djmarcuslaw.com/blog

Extension of SBA Recovery Loans

This program, officially called the America's Recovery Capital Loan Program, is designed to provide small businesses with a lifeline to make payments of principal and interest, in full or in part, on one or more existing, qualifying small business loans for up to six months. These loans are interest-free to the borrower, carry a 100 percent guaranty from the SBA to the lender, and require no fees paid to SBA. If you're wondering why a lender would participate in the ARC program, the SBA pays interest to the lender for the duration of the loan. Loan proceeds are provided over the six-month period and repayment of the loan is deferred for twelve months after the final disbursement. Repayment can extend up to five years. You can find out more about qualifying for an ARC loan by downloading the FAQ (pdf).

The program was originally created in the Recovery Act and has already been extended four times, the latest extension designed to end on September 30th of this year. However, the program has now been extended again to December 31st and another $14 billion has been added to the program capacity.

So, if your business has been profitable in the past and has been making loan payments or is just beginning to miss payments, but is not yet in default on loan obligations, this could be the program for you.

Increase in maximum loan size for SBA programs

Let's begin by breaking down the different types of loans that the Small Business Jobs Act modified. There are three types of SBA loans - 7(a), 504, and Express - for which the Act increased loan size limits.

7(a) loans are the most flexible and most frequently used SBA loans. It's the SBA's primary program to help start-up and existing small businesses obtain financing when they might not be eligible for business loans through commercial lending channels. The SBA, again, does not loan directly, but partially guarantees loans made by commercial lenders. Businesses tend to use this program more than other SBA loans because it can be used for a variety of general business purposes, including working capital, machinery and equipment, furniture and fixtures, land and building (including purchase, renovation and new construction), leasehold improvements, and debt refinancing (under special conditions). The loans mature, generally, in ten years for working capital and in twenty-five years for fixed assets.

504 loans come in two flavors - regular and manufacturing. These loans are designed to promote economic development with a community an can be used for purchasing land and improvements, construction or renovation of facilities, or purchasing long-term machinery or equipment. They cannot be used for working capital or inventory, or for consolidating, repaying or refinancing debt. There is a size restriction for 504 loans - businesses may not have a net worth of more than $7.5 million or an

average net income, after taxes, of over $2.5 million in the two years prior to an application. Under the umbrella of promoting economic development within a community, the applicant business can show a few different goals: job creation or community development; or public policy. Public policy goals fall under multiple categories, which you can explore on the 504 program website. The SBA differentiates financially between manufacturing and non-manufacturing jobs, generally requiring one non-manufacturing job created for every $65,000 in loan funds or one manufacturing job for every $100,000 in loan funds.

The Small Business Jobs Act permanently increased loans limits on 7(a) and 504 loans from $2 million to $5 million and to $5.5 million for 504 manufacturing loans.

Express Loans are different, in that they are smaller and designed for a quick application turnaround - usually within 36 hours of the application submission. The loans follow the 7(a) qualification standards and have similar use restrictions. The limits for Express loans have been temporarily increased from $350,000 to $1 million; the extension expires September 27th, 2011.

Small Business Lending Fund

The Small Business Lending Fund provides up to $30 billion in funding to small banks - banks with less than $10 billion in assets - at interest rates meant to encourage small business loans. As banks make more loans to small businesses, the interest rate decreases. The money is leftover from the TARP funds and being shifted to try to reinvigorate stalled, small business, commercial lending. These banks will be provided funding through Treasury Department preferred stock purchases. The program has a host of restrictions for bank participation that appear to be intended to protect the government's investment.

State Small Business Credit Initiative

Again, discussed in depth here.

Small Business Tax Credits

These eight changes to small business taxes are probably the most complicated for a small business owner. I'll go over each

Capital gains tax cut to 0% on certain investments - The Recovery Act allowed investors to exclude 75% of their profits if they invested in eligible small businesses between mid-February 2009 and the end of this year. Before that, a 1993 law granted a 50% exclusion to investors who made risky investments in so-called C corporations (a common structure for high-growth start-ups) with less than $50 million in assets, a rule that's still in place. This new rule allows venture capital firms and other investors to exclude all profits from investments in certain small businesses. It also excludes the Alternative Minimum Tax if investors choose to take the exclusion. This exclusion is valid on investments made before January 1st, 2011. After that, it drops back to the 50% level.

Increase and extension of the ability to immediately expense capital investments - The Act increases the amount of capital investments that businesses would be eligible to immediately write off to $500,000, for 2010 and 2011. It also raises the level of investments at which the write-off phases out to $2 million. Prior to the passage of the bill, the expensing limit would have been $250,000 this year, and only $25,000 next year. This expensing, called Section 179, allows businesses to take investments that would otherwise be depreciated over a period of years and immediately receive a tax credit for the expense.

Extension of the 50% bonus depreciation created in the Recovery Act - Section 168 depreciation has been extended for tax year 2010 for business assets put into service before the end of the year. This means you can depreciate an asset by an extra 50%, after claiming Section 179 expensing (above) and before taking regular depreciation. Talk to your accountant about this one.

Deduction for self-employed health benefits - This deduction allows self-employed individuals to deduct their health insurance costs as a business expense for payroll tax purposes. You have to meet three criteria: File an IRS Form 1040 Schedule C tax form or Schedule E with earned income this includes sole proprietors, single member LLCs, and sole owner S Corporations; pay self employment taxes via IRS Form 1040 Schedule SE; and pay for individual or family health coverage in 2010.

Deduction of business cell phone plans - The Act removes cellular telephones and similar telecommunications equipment from the Code's definition of "listed property." The IRS required businesses to satisfy substantiation rules for an employer to fully deduct the costs of cell phones and for employees to fully exclude the value of cell phones from taxable income. Basically, you had to prove you were using the phone for business by keeping strict records of your cell phone use. By delisting cell phones, the IRS is no longer requiring substantiation for employees claiming exclusion from taxable income and for employers claiming deductions.

Increase in the deduction that entrepreneurs can claim for startup expenses - This section of the Act temporary increases in the deduction that entrepreneurs can claim for startup expenses from $5000 to $10,000. The $10,000 deduction is reduced by the amount of total start-up costs that exceeds $60,000. Qualifying trade or business startup expenses include costs related to investigating, creating, or acquiring an active trade or business. Qualifying costs cannot be directly related to capital or equipment.

Carry back of general business expense credits for up to five years - For credits determined in the businesses first tax year after December 31st, 2009, the carry back has been extended from one year to five years. These credits can include investment tax credits, R&D credits, work opportunity credits, etc. A qualifying small business can be a corporation without publicly traded stock, a partnership, or a sole proprietorship that has average annual gross receipts of $50 million or less for the prior three tax year periods. Businesses can use credit to offset both regular and AMT liabilities.

Limit on penalties for reporting errors - The Act makes the penalty for failing to disclose a reportable transaction proportionate to the amount the tax owed is reduced by the failure to disclose. A "reportable transaction" includes confidential transactions, transactions with contractual protection, transactions involving large losses and transactions listed by the IRS as potentially abusive. Previously, the maximum annual penalty for failing to disclose reportable transactions was $200,000 for corporations and $100,000 for individuals. The act now limits the penalty to 75 percent of the tax decrease with a minimum penalty of $10,000 ($5,000 for individuals). The relief applies to penalties assessed after December 31, 2006. This retroactive date may create refund opportunities for taxpayers that previously paid penalties for failure to disclose reportable transactions.

On the other side of the coin, the Act increases some Failure to File penalties for 1099s required under current rules and those imposed in the future by Section 9006 of the Health Care Bill (PPACA). The penalty for filing a 1099 not more than 30 days late increases from $15 to $30 (first tier); the penalty for filing a 1099 more than 30 days late and before August 1st increases from $30 to $60 (second tier); the penalty for filing a 1099 on or after August 1st increases from $50 to $100 (third tier); and the penalty for intentional failure to file increases from $100 to $250 (third tier). The maximum penalty also increases from $25,000 to $75,000 for the first-tier penalty, from $50,000 to $200,000 for the second-tier penalty, and from $100,000 to $500,000 for the third-tier penalty.

So, there we go. Next post will discuss how your small business can actually take advantage of these items.