A Recap–The American Recovery and Reinvestment Tax Act of 2009

By Robert E. Ward and Richard S. Chisholm

The much-anticipated economic stimulus package, the American Recovery and Reinvestment Act of 2009, has now been in effect for six months. Robert E. Ward and Richard S. Chisholm reexamine and outline the significant provisions of the historic Act.

Tax Relief for Individuals and Families

Act Sec. 1001–Making Work Pay Credit

The American Recovery and Reinvestment Tax Act of 2009 (P.L. 111-5) (ARRTA or "the Act") creates the Making Work Pay Credit, which provides eligible individuals with a tax credit of $400 ($800 in the case of a joint return). However, if the taxpayer's earned income is less than $6,451.62 ($12,903.24 in the case of a joint return), the Making Work Pay Credit is limited to 6.2 percent of the taxpayer's earned income. Individuals eligible for the Credit include any individual with earned income other than (1) a nonresident alien, (2) an individual with respect to whom another individual may claim a dependency deduction, or (3) an estate or trust.

For purposes of the Making Work Pay Credit, earned income is defined in the same manner as it is for the Earned Income Tax Credit, with two distinctions. First, earned income for purposes of the Making Work Pay Credit does not include net earnings from self-employment that are not taken into account in computing taxable income. Second, the Credit includes combat pay. The Credit is phased out at a rate of two percent of the individual's modified adjusted gross income in excess of $75,000 ($150,000 in the case of a joint return). An individual's modified adjusted gross income, for purposes of calculating the Credit, is the individual's adjusted gross income increased by any amount excluded from gross income under Code Secs. 911, 931 or 933.

Once the amount of the Credit has been computed, it is reduced by any amount the taxpayer receives under Act Sec. 2201 (addressing economic recovery payments to recipients of Social Security, Supplemental Security Income, Railroad Retirement Benefits and Veterans Disability Compensation or Pension benefits) or Act Sec. 2202 (addressing special credits received for certain government retirees).

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 36A added; Code Sec. 6211(b)(4)(A) amended; Code Sec. 1324(b)(2) amended.

Act Sec. 1002–Temporary Increase in Earned Income Tax Credit

The Act increases the Earned Income Tax Credit (EITC) percentage for taxpayers with three or more qualify-

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ing children from 40 to 45 percent of earned income. This increase is only available for tax years beginning in 2009 and 2010. The phase-out for taxpayers qualifying under this provision, however, remains the same as under prior law. As a result, the maximum amount of the EITC for families with three or more qualifying children remains at $5,656.50.

Under Code Sec. 32(b)(2)(B), the EITC is phased out as the taxpayer's earned income for a particular tax year increases. As a relief provision for married taxpayers filing joint returns, the Code increases the threshold at which the phase-out begins by $3,000 for tax years beginning after 2007. The Act increases the $3,000 amount to $5,000 for 2009 and 2010. In addition, the Act provides an inflation adjustment for the $5,000 amount beginning in 2010.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2010.
- **Code Secs. Affected—**New Code Sec. 32(b)(3) added.

Act Sec. 1003–Temporary Increase of Refundable Portion of Child Credit

Code Sec. 25 allows individuals to claim a maximum Child Tax Credit (CTC) of $1,000 for each qualifying child under age 17. A portion of the CTC may be refundable if the taxpayer's earned income is less than $10,000. For 2009 and 2010, the Act reduces the $10,000 amount to $3,000.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 24(d)(4).

Act Sec. 1004–American Opportunity Tax Credit

The Act creates the American Opportunity Tax Credit, which is, in effect, an alteration of the Hope Scholarship Credit for tax years 2009 and 2010. The provision makes several changes to the Hope Scholarship Credit (HSC).

The amount of the HSC is increased by doubling the allowance for qualified tuition and related expenses from $2,000 to $4,000. The computation of the HSC is changed so that the amount which may be claimed in any tax year is 100 percent of the "qualified tuition and related expenses" paid by the taxpayer during the tax year up to $2,000, plus 25 percent of such expenses in excess of $2,000 but not exceeding $4,000. The number of years in which the HSC may be taken for post-secondary education is increased from two years to four years. Required course materials are expressly included within the term "qualified tuition and related expenses." Adjusted gross income limits above which the HSC is phased out have been increased by raising the denominator within the limitations formula from $40,000 to $80,000 ($80,000 to $160,000 in the case of a joint return). For taxpayers subject to the Alternative Minimum Tax, special limitations are imposed. Forty percent of the Hope Scholarship Credit has been made refundable if the taxpayer is *not* a child to whom the "kiddie tax" of Code Sec. 1(g) applies.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2010. The amendment to Code Sec. 24(b)(3)(B) is subject to the sunset of the Economic Growth and Tax Relief Reconciliation Act of 2001.
- **Code Secs. Affected—**Prior Section 25A(i) has been renamed Code Sec. 25A(j), and new Code Sec. 25A(i) has been added; Code Sec. 24(b)(3)(B) amended; Code Sec. 25(e)(1)(C)(ii) amended; Code Sec. 26(a)(1) amended; Code Sec. 25B(g)(2) amended; Code Sec. 904(i) amended; Code Sec. 1400C(d)(2) amended; Code Sec. 1324(b)(2) amended.

Act Sec. 1005–Computer Technology and Equipment Allowed As a Qualified Higher Education Expense for Code Sec. 529 Accounts in 2009 and 2010

ARRTA amends Code Sec. 529 so that the term "qualified higher education expenses" includes "expenses paid or incurred in 2009 and 2010 for the purchase of any computer technology or equipment … or Internet access and related services if such technology, equipment, or services are to be used by the beneficiary and the beneficiary's family during any of the years the beneficiary is enrolled at an eligible educational institution." The Act expressly excludes from the term "qualified higher education expenses" those expenses for "computer software designed for sports, games, or hobbies unless the software is predominantly educational in nature."

- **Effective Date—**Effective for expenses paid or incurred after December 31, 2008.

- **Sunset—**Ineffective for expenses incurred after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 529(e)(3)(A) amended.

Act Sec. 1006–Extension of and Increase in First-Time Homebuyer Credit; Waiver of Requirement to Repay

ARRTA extends the sunset of the Code Sec. 36 First-Time Homebuyer Credit (FTHC) from July 1, 2009, to December 1, 2009. The Act also increases the maximum FTHC allowed from $7,500 to $8,000 (from $3,750 to $4,000 for married taxpayers filing separately) and waives recapture for those taxpayers purchasing a principal residence after December 31, 2008, but before December 1, 2009. Taxpayers who sell their principal residence within 36 months of the date of purchase will, however, be subject to immediate acceleration and recapture of the Credit. Additionally, the Act removes the prohibition against purchases financed by mortgage revenue bonds.

The Act also coordinates the first-time homebuyer credit for the District of Columbia provided by Code Sec. 1400C ("the D.C. Homebuyer Credit") with the FTHC under Code Sec. 36. Under the Act, the D.C. Homebuyer Credit is disallowed for taxpayers who purchase a residence after December 31, 2008, and before December 1, 2009, and claim the FTHC.

- **Effective Date—**Effective for residences purchased after December 31, 2008.
- **Sunset—**Ineffective for residences purchased after December 1, 2009.
- **Code Secs. Affected—**Code Sec. 36 amended; Code Sec. 1400C amended.

Act Sec. 1007–Suspension of Tax on Portion of Unemployment Compensation

The Act allows taxpayers to exclude up to $2,400 of unemployment compensation collected during 2009 from gross income.

- **Effective Date—**Effective for unemployment compensation collected after December 31, 2008.
- **Sunset—**Ineffective for unemployment compensation collected during any tax year beginning after December 31, 2009.
- **Code Secs. Affected—**Code Sec. 85(c) added.

Act Sec. 1008–Additional Deduction for State Sales Tax and Excise Tax on the Purchase of Certain Motor Vehicles

ARRTA creates a new deduction for "qualified motor vehicle taxes," which include state or local sales and excise taxes imposed on the purchase of certain new passenger automobiles, light trucks, motorcycles and motor homes. Passenger automobiles and light trucks must be treated as a motor vehicle for purposes of Title II of the Clean Air Act and have a weight rating of not more than 8,500 pounds. Motorcycles claiming the deduction must similarly have a weight rating of not more than 8,500 pounds. The deduction is limited to taxes imposed on the first $49,500 of the vehicle's purchase price and is reduced by a fraction based upon the taxpayer's modified gross income over $125,000 ($250,000 in the case of a joint return).

The Act proscribes qualified motor vehicle taxes from being included in the cost of the vehicle purchased. Taxpayers electing under Code Sec. 164(b)(5) to deduct state and local sales taxes are also precluded from taking a deduction for qualified motor vehicle taxes.

The deduction allowed for qualified motor vehicle taxes may be taken by nonitemizers and is considered an addition to the basic standard deduction. The qualified motor vehicle tax may also be deducted in computing the Alternative Minimum Tax.

- **Effective Date—**Effective for all purchases on or after the date of enactment in tax years ending after such date.
- **Code Secs. Affected—**Code Sec. 164(a)(6) added; Code Sec. 164(b)(6) added; Code Sec. 63(c) amended; Code Sec. 56(b)(1)(E) amended.

Alternative Minimum Tax Relief

Act Sec. 1011–Extension of Alternative Minimum Tax Relief for Nonrefundable Personal Credits

The Act provides an extension through 2009 of the Alternative Minimum Tax relief previously granted by Congress in the form of special rules for "nonrefundable personal credits" that had been set to expire at the end of 2008. These rules permit a taxpayer to reduce regular and alternative minimum tax liabilities by the amount of the Dependent Care Credit, the

Credit for Elderly and Disabled, the Credit for Interest on Certain Home Mortgages, the Hope Scholarship and Lifetime Learning Credits, the Credit for Certain Nonbusiness Energy Property, and the D.C. First-time Homebuyer Credit). The Act extends the availability of these Credits for both regular and alternative minimum tax purposes through 2009.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2009.
- **Code Secs. Affected—**Code Sec. 26(a)(2) amended.

Act Sec. 1012–Extension of Increased Alternative Minimum Tax Exemption Amount

The Act extends and increases the Alternative Minimum Tax exemption amounts set to expire at the end of 2008 through 2009. For a surviving spouse or those filing a joint return, the $69,950 exemption for 2008 is raised to $70,950 for 2009. For unmarried individuals and those who are not a surviving spouse, the $46,200 exemption for 2008 is raised to $46,700 for 2009.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2009.
- **Code Secs. Affected—**Code Sec. 55(d) amended.

Energy Incentives

Act Sec. 1101–Extension of Credit for Electricity Produced from Certain Renewable Resources

Code Sec. 45 allows a tax credit for electricity produced from certain renewable resources. Code Sec. 45(d) generally requires facilities to be placed in service prior to January 1, 2009. The Act extends the period for installation for wind facilities that produce electricity through December 31, 2012, and the period for biomass, geothermal energy, solar energy, landfill gas, trash combustion and qualified hydropower facilities through December 31, 2013. Additionally, the Act extends the installation period for marine and hydrokinetic renewable energy facilities through December 31, 2013.

- **Effective Date—**Effective for property placed into service after the date of the enactment.
- **Code Secs. Affected—**Code Sec. 45(d) amended.

Act Sec. 1102–Election of Investment Credit in Lieu of Production Credit

The Act coordinates the relationship between tax credits available under Code Sec. 45 for electricity produced from certain renewable resources ("the Production Credit") and the Energy Credit under Code Sec. 48. Generally, the Energy Credit is more advantageous inasmuch as the taxpayer is allowed to apply a tax credit equal to 30 percent of the taxpayer's cost basis in qualifying energy property placed in service during the tax year.

The Act allows taxpayers to claim the Energy Credit in lieu of the Production Credit for certain property. In order to do this, the taxpayer must make an irrevocable election to treat certain depreciable tangible property that is part of a qualified investment credit facility as energy property under Code Sec. 48. Such an election will preclude any Production Credit for the property under Code Sec. 45. The Act defines qualified investment credit facilities to which the property must be associated as (1) wind facilities placed into service between January 1, 2009, and December 31, 2012, and (2) closed-loop biomass facilities, open-loop biomass facilities, geothermal or solar energy facilities, landfill gas facilities, trash facilities, qualified hydropower facilities and marine and hydrokinetic renewable energy facilities placed into service between January 1, 2009, and December 31, 2013.

- **Effective Date—**Effective for facilities placed into service after December 31, 2008.
- **Code Secs. Affected—**Code Sec. 48(a)(5) added.

Act Sec. 1103–Repeal of Certain Limitations on Credit for Renewable Energy Property

Code Sec. 48 provides a tax credit for certain property identified in the statute equal to 30 percent of the cost of such property in the year in which it is placed in service. Included among the types of qualifying energy property under Code Sec. 48 are qualified small wind energy property (wind turbines) described in Code Sec. 48. Prior law limited the Energy Credit for this type of asset to $4,000.

The Act removes this cap and also removes the provisions of prior law, which reduce the cost basis of the property for purposes of computing the Credit if the property is financed by subsidized energy financing or with proceeds from private activity bonds.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Code Secs. Affected—**Code Sec. 48(c)(4)(B) deleted; Code Sec. 48(a)(4) amended; Code Sec. 25C(e)(1) amended; Code Sec. 25D(e) amended; Code Sec. 48A(b)(2) amended; Code Sec. 48B(b)(2) amended.

Act Sec. 1104–Coordination with Renewable Energy Grants

Under the spending provisions of the Act, the Secretary of Energy is authorized to provide grants to persons who place in service certain facilities for the production of electricity, as well as certain microturbines, heat and power systems, and geothermal heat pump devices that qualify for the Energy Credit under Code Sec. 48 or Code Sec. 45. The Committee Reports accompanying the Act indicate that these grants are intended to "mimic the operation of the credit under Code Sec. 48. For example, the amount of the grant is not includable in gross income. However, the basis of the property is reduced by 50 percent of the amount of the grant. In addition some or all of each grant is subject to recapture if the grant eligible property is disposed of by the grant recipient within five years of being placed in service."

The Act denies taxpayers receiving Department of Energy grants for purchase of property qualifying for Energy Credits the benefit of those Credits. If Energy Credits were claimed for progress expenditures for construction of such property before receipt of the grant, those tax credits are recaptured.

- **Code Secs. Affected—**Code Sec. 48(d) added.

Act Sec. 1121–Extension and Modification of Credit for Nonbusiness Energy Property

Code Sec. 25C(c) allows individual taxpayers who make "qualified energy efficiency improvements" to their homes as defined in Code Sec. 25C(c) or expend amounts for "residential energy property" satisfying the definition of Code Sec. 25C(d) to claim a tax credit for the full amount of the residential energy property expenditures and 10 percent of the amount paid for qualified energy efficiency improvements.

The Act amends Code Sec. 25C(a) to increase the amount of the tax credit to 30 percent of the amounts a taxpayer pays for qualified energy efficiency improvements and expenditures for residential energy property qualifying under the statute. In addition the aggregate amount of tax credits, which may be claimed over the lifetime of a taxpayer, is increased from $500 to $1,500. The Act also amends the energy efficiency standards for electric heat pumps, central air conditioners, water heaters, wood stoves, natural gas, propane and oil furnaces and water heaters, exterior windows, doors and skylights, and installation materials. Finally, the sunset of the statute is extended by one year.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 25C(a) and (b) replaced; Code Sec. 25C(c)(2) amended; Code Sec. 25C(d) amended; Code Sec. 25C(g)(2) amended.

Act Sec. 1122–Modification of Credit for Residential Energy Efficient Property

Existing law provides individual taxpayers with a tax credit under Code Sec. 25D equal to 30 percent of qualified solar electric property, qualified solar water heating property and qualified fuel cell property expenditures made by a taxpayer during the year. The tax credit under Code Sec. 25D for qualified solar electric property and qualified solar water heating property expenditures was capped at $2,000. The Act eliminates these caps entirely and similarly eliminates caps on the maximum expenditures eligible for credit in the case of dwellings occupied by more than one individual.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Code Secs. Affected—**Code Sec. 25D(b)(1) amended; Code Sec. 25D(e)(4) amended.

Act Sec. 1123–Temporary Increase in Credit for Alternative Fuel Vehicle Refueling Property

Code Sec. 30C allows a 30-percent tax credit for the cost of "qualified alternative fuel vehicle refueling property" that satisfies the definition of Code Sec. 30C(c) and that is used in a trade or business of a taxpayer or installed in the taxpayer's principal residence.

In the case of property not relating to hydrogen, the Act increases the amount of the tax credit from 30 to 50 percent and allows the credit to be taken with respect to as much as $50,000 of depreciable property and $2,000 of nondepreciable assets. In the case of property relating to hydrogen, the credit remains at 30 percent but the amount of eligible property in any tax year is increased from $30,000 to $200,000.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years ending after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 30C(e)(6) added.

Act Sec. 1141–Credit for New Qualified Plug-in Electric Drive Motor Vehicles

The Act amends Code Sec. 30D, which provided a tax credit for "qualified plug-in electric drive motor vehicles" described in Code Sec. 30D(d) by limiting the maximum credit to $7,500 regardless of vehicle weight. Prior law limited the number of vehicles qualifying for the tax credit to 250,000 for all manufacturers. The Act increases the vehicle limitation to 200,000 per manufacturer for vehicles sold after December 31, 2009.

- **Effective Date—**Effective for vehicles acquired after December 31, 2009.
- **Code Secs. Affected—**Code Sec. 38D amended; Code Sec. 30B(d)(3)(D) amended; Code Sec. 38(b)(35) amended; Code Sec. 1016(a)(25) amended; Code Sec. 6501(m) amended.

Act Sec. 1142–Credit for Certain Plug-in Electric Vehicles

The Act creates a new 10-percent tax credit for low speed vehicles, motorcycles and three-wheeled vehicles. Under prior law these types of vehicles would not satisfy the criteria of "qualified plug-in electric drive motor vehicles." The Act allows these types of vehicles to qualify for a 10-percent tax credit capped at $2,500.

- **Effective Date—**Effective for vehicles purchased after the date of the enactment of the Act.
- **Code Secs. Affected—**Code Sec. 30 amended; Code Sec. 24(b)(3)(B) amended; Code Sec. 25(e)(1)(C)(ii) amended; Code Sec. 25B(g)(2) amended; Code Sec. 26(a)(1) amended; Code Sec. 904(i) amended; Code Sec. 1400C amended.

Act Sec. 1143–Conversion Kits

The Act also creates a new 10-percent tax credit of up to $4,000 for the cost of converting any motor vehicle into a "qualified plug-in electric motor vehicle" satisfying certain battery capacity requirements. The tax credit is taken as part of the Alternative Vehicle Motor Credit (described below) and is allowed in addition to other credits that may have already been taken for the vehicle. If the conversion triggers recapture of Alternative Vehicle Motor Credits previously taken, recapture is waived by the Act.

- **Effective Date—**Effective for property placed into service after the date of the enactment of the Act.
- **Sunset—**Ineffective for property placed into service after December 31, 2011.
- **Code Secs. Affected—**Sections 30B(h) and (i) redesignated as Code Sec. 30B(i) and (j); Code Sec. 30B(h) added.

Act Sec. 1144–Treatment of Alternative Motor Vehicle Credit As a Personal Credit Allowed Against AMT

Code Sec. 30B allows taxpayers a tax credit for "qualified fuel cell motor vehicles" described in Code Sec. 30B(b)(3), "advanced lean burn technology vehicles" described in Code Sec. 30B(c)(3), "qualified hybrid motor vehicles" described in Code Sec. 30B(d)(3) and "qualified alternative fuel motor vehicles" described in Code Sec. 30B(e)(4) (collectively referred to as the "Alternative Motor Vehicle Credit"). Generally, the Credit ranges from $8,000 to $40,000 depending on the weight of the vehicle.

The Act provides that the Alternative Motor Vehicle Credit of Code Sec. 30B is a personal credit allowed for both alternative minimum tax as well as regular tax purposes. This treatment removes the prior reduction in the Credit for AMT purposes.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Code Secs. Affected—**Code Sec. 30B(g)(2) amended; Code Sec. 24(b)(3)(B) amended; Code

Sec. 25(e)(1)(C)(ii) amended; Code Sec. 25B(g)(2) amended; Code Sec. 26(a)(1) amended; Code Sec. 904(i) amended; Code Sec. 1400C(d)(2) amended; Code Sec. 30C(d)(2)(A) amended Code Sec. 55(c)(3) amended.

Act Sec. 1151–Increased Exclusion Amount for Commuter Transit Benefits and Transit Passes

ARRTA increases the exclusion amount for commuter transit benefits and transit passes to an amount equal to the exclusion amount for qualified parking.

- **Effective Date—**Effective for months beginning on or after the date of enactment of the Act.
- **Sunset—**Ineffective for months beginning on or after January 1, 2011.
- **Code Secs. Affected—**Code Sec. 132(f)(2) amended.

Business Tax Incentives

Act Sec. 1201(a)–Special Depreciation Allowance for Certain Property Acquired During 2009

Existing law allows an additional first-year depreciation deduction equal to 50 percent of the adjusted basis of qualified property placed in service during 2008 for both regular tax and alternative minimum tax purposes (commonly referred to as "Bonus Depreciation"). The term "qualified property" refers to MACRS property with an applicable recovery period of 20 years or less, certain computer software, certain leasehold improvements and certain other property qualifying under Code Sec. 168(k)(2).

ARRTA Section 1201(a) extends the additional first-year depreciation deduction so that it applies to property purchased and placed in service during the 2009 calendar year. All of the prior law's requirements with respect to this deduction have been retained.

For certain types of long-lived property described in Code Sec. 168(k)(2)(B) and (C), the time limits for the Bonus Depreciation are extended through 2010.

- **Effective Date—**The amendments apply to property placed in service after December 31, 2008, in tax years ending after that date, except for the amendments to Code Sec. 168(k)(4)(D) (relating to the definition of "eligible qualified property"), which apply to tax years ending after March 31, 2008.
- **Code Secs. Affected—**Code Sec. 168(k) amended, Code Sec. 168(l)(5) amended; Code Sec. 1400N(d)(3) amended.

Act Sec. 1201(b)–Extension of Election to Accelerate the AMT and Research Credits in Lieu of Bonus Depreciation

Prior law allowed a taxpayer otherwise eligible for the Bonus Depreciation to elect to claim additional research or alternative minimum tax credits in lieu of the Bonus Depreciation. The election applied to "eligible qualified property" placed in service after March 31, 2008, and before January 1, 2009.

Taxpayers making the election to forego Bonus Depreciation will claim a refundable credit. The credit is limited to the lesser of (1) 20 percent of the foregone Bonus Depreciation, (2) six percent of the taxpayer's AMT and R & D credit carryfowards arising from tax years beginning before 2006, or (3) $30 million. The taxpayer must depreciate the remaining adjusted basis of the "eligible qualified property" using the straight-line method.

The Act permits taxpayers making the election to forego Bonus Depreciation under Code Sec. 168(k)(4) to do so for certain property placed in service in calendar year 2009. AARTA adds Code Sec. 168(k)(4)(H), which introduces the concept of "extension property," and defines it as property which is "eligible qualified property" (as defined in amended Code Sec. 168(k)(4)(D)) solely because of the extension of Bonus Depreciation by AARTA Section 1201(a).

Those taxpayers who had already made the election under Code Sec. 168(k)(4) to increase the research or minimum tax credits for its first tax year ending after March 31, 2008, are given the opportunity to choose not to make the election for "extension property" placed into service for the first tax year ending after December 31, 2008, and each subsequent year (the "Extension Period"). Those taxpayers who have not made an election under Code Sec. 168(k)(4) for the first tax year ending after March 31, 2008, may make the election for property placed into service during the Extension Period.

- **Effective Date—**The amendments apply to property placed in service after December 31, 2008, in tax years ending after that date.

Act Sec. 1202–Temporary Increase in Limitations on Expensing of Certain Depreciable Business Assets

Prior law provided that a taxpayer may elect to expense under Code Sec. 179 the costs of acquiring qualifying property placed in service in a tax year up to a maximum amount of $250,000. Further, prior law reduced the $250,000 maximum Code Sec. 179 expense deduction (but not below zero) by the amount by which the total cost of qualifying property placed in service during a tax year exceeded $800,000.

Prior law reduced the $250,000 and $800,000 thresholds to $125,000 and $500,000, respectively, (with those amounts indexed for inflation beginning in 2009) for calendar years 2009 and 2010. Other rules applied to calendar years beginning after 2010.

AARTA Section 1202 extends the $250,000 and $800,000 thresholds to tax years beginning in 2009 only.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2009.
- **Code Secs. Affected—**Code Sec. 179(b)(7) amended.

Act Sec. 1211–Five-Year Carryback of Operating Losses

Generally, present law allows net operating losses to be carried back two years and forward 20 years. Certain exceptions apply to net operating losses arising under various circumstances, and those losses may be eligible for carryback periods longer than two years. However, net operating losses cannot reduce the taxpayer's alternative minimum taxable income by more than 90 percent.

ARRTA allows an "eligible small business" incurring a net operating loss in its tax year ending in 2008 to elect to increase its carryback period for those losses from two years to either three, four or five years, in the taxpayer's discretion. Further, a taxpayer may elect to apply these provisions to tax years beginning in 2008, rather than the one ending in 2008.

The election to lengthen the carryback period must be made by the due date (including extensions) of the taxpayer's return for the tax year in which the net operating loss arises, using procedures established by the IRS. An election once made is irrevocable and may be made only with respect to one tax year.

The term "eligible small business" means a taxpayer whose average gross receipts for tax years ending in 2005, 2006 and 2007 do not exceed the sum of $15 million.

The IRS is instructed to prescribe certain anti-abuse rules including anti-stuffing rules, anti-churning rules (including rules relating to sale-leasebacks) and rules relating to losses from wash sales which are similar to the rules under Code Sec. 1091.

- **Effective Date—**Except as otherwise noted, tax years ending after December 31, 2007.
- **Transitional Rules—**ARRTA allows taxpayers who have already filed income tax returns which recognized a net operating loss for a tax year either ending in the calendar year 2008 or beginning in the calendar year 2008 (*see* Code Sec. 172(b)(1)(H) as amended by the Act as discussed above) transition rules which permit return positions previously taken with respect to those net operating losses to be amended. Such taxpayers must make an affirmative election to use these transition rules within sixty calendar days after the date of enactment. Taxpayers who previously elected to forego the net operating loss carryback period under Code Sec. 172(b)(3) may elect to change that decision, thereby allowing the extended carryback provisions of the Act to apply. Those taxpayers may then make a second election to increase their carryback period. Finally taxpayers may file an application for a quick adjustment and refund of the tax benefit arising from the 2008 calendar year net operating loss under Code Sec. 6411(a).
- **Code Secs. Affected—**Code Sec. 172(b)(1)(H) is amended; Code Sec. 172(k) is deleted; and Code Sec. 172(l) is redesignated as Code Sec. 172(k).

Act Sec. 1212–Decreased Required Estimated Tax Payments in 2009 for Certain Small Businesses

Code Sec. 6654 requires taxpayers to make estimated tax payments. These provisions apply to individuals, nonresident aliens, decedent's estates and trusts. Under prior law, the required annual estimated tax payment was the lower of (1) 90 percent of the tax shown on the return for the current year or (2) 100 percent of the tax shown on the return for the preceding tax year (increased to 110 percent if the taxpayer's adjusted gross income exceeded $150,000 in the preceding tax year).

ARRTA Section 1212 revises the foregoing requirement for calendar year 2009 for eligible individual taxpayers who earn at least 50 percent of their adjusted gross income from a small business to reduce their estimated tax requirements to 90 percent of the tax liability for 2008. Individual taxpayers are eligible for this relaxed estimated tax payment rule if their 2008 adjusted gross income was less than $500,000. For a married person filing separately, the threshold is $250,000. For a decedent's estate or a trust, adjusted gross income is determined under the rules of Code Sec. 67(e).

- **Effective Date—**Effective for tax years beginning after December 31, 2008.
- **Sunset—**Ineffective for tax years beginning after December 31, 2009.
- **Code Secs. Affected—**Code Sec. 6654(d)(1)(D) added.

Act Sec. 1221–Incentives to Hire Unemployed Veterans and Disconnected Youth

Under prior law the Work Opportunity Tax Credit (WOTC) is available to employers on an elective basis who hire employees from one or more of nine targeted groups.

ARRTA creates two additional classes of individuals who, if hired by an employer, make that employer eligible for WOTC. Those classes are described as "unemployed veterans" and "disconnected youth."

The Act defines the term "veteran" as "having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, or having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability." To be classified as an "unemployed veteran," the veteran must be certified as "having been discharged or released from active duty in the Armed Forces at any time during the five-year period ending on the hiring date" and "being a recipient of unemployment compensation under State or Federal law for not less than 4 weeks during the 1-year period ending on the hiring date."

Disconnected youths must be certified as (1) "having attained age 16 but not age 25 on the hiring date," (2) "not regularly attending any secondary, technical, or post-secondary school during the 6-month period preceding the hiring date," (3) "not regularly employed during such 6-month period," and (4) "not readily employable by reason of lacking a sufficient number of basic skills." The Conference Committee Report explains "it is intended that a low-level of formal education may satisfy the requirement that an individual is not readily employable by lacking a sufficient number of skills."

- **Effective Date—**Applicable for individuals who begin work for the employer after December 31, 2008.
- **Sunset—**Inapplicable for individuals who begin work for the employer after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 51(d)(14) added.

Act Sec. 1231–Deferral and Ratable Inclusion of Income Arising from Business Indebtedness Discharged by the Reacquisition of a Debt Instrument

Existing law generally requires cancellation of indebtedness income to be included in a debtor's gross income unless certain exceptions set forth in Code Sec. 108 or 102 are satisfied.

ARRTA introduces Code Sec. 108(i), which allows certain taxpayers to defer the recognition of a certain type of cancellation of indebtedness income for a certain number of years, then recognize that income ratably over the subsequent five years, subject to a number of restrictions.

Specifically, the Act allows cancellation of indebtedness income arising from the "reacquisition" of "an applicable debt instrument" to be deferred until either (1) the fifth tax year following the tax year in which the reacquisition occurs if the reacquisition occurs in 2009, or (2) the fourth tax year following the tax year in which the reacquisition occurs if the reacquisition occurs in 2010.

Once the deferral period is over, the deferred income is recognized ratably over a five-year period. Only taxpayers reacquiring debt instruments between December 31, 2008, and January 1, 2011, may make the election.

An "applicable debt instrument" must be originally issued by a C corporation or "any other person in connection with the conduct of a trade or business by such person," and includes any instrument or contractual arrangement constituting indebtedness.

A "reacquisition" occurs when an "applicable debt instrument" is acquired by (1) the debtor that issued the particular debt instrument, or (2) any person related to the debtor as set forth in Code Sec. 108(e)(4). Additional rules apply to debt-for-debt exchanges in which the newly issued debt instrument has original discount.

The recognition of the deferred income will be accelerated if the electing taxpayer dies, liquidates, sells substantially all of the taxpayer's assets (including in bankruptcy), ceases doing business "or … similar circumstances" arise.

The IRS is instructed to issue regulations implementing this provision, including instructions regarding how the appropriate elections are to be made and the deferred income reported.

- **Effective Date—**Applicable for tax years ending after December 31, 2008.
- **Code Secs. Affected—**Code Sec. 108(i) added.

Act Sec. 1241–Special Rules Applicable to Qualified Small Business Stock for 2009 and 2010

Code Sec. 1202(a)(1) excludes 50 percent of any gain from the sale or exchange of qualified small business stock held for more than five years from the gross income of a taxpayer other than a corporation.

ARRTA adds Code Sec. 1202(a)(3), which increases the percentage set forth in Code Sec. 1202(a)(1) to 75 percent from 50 percent for qualified small business stock purchased in the calendar years 2009 and 2010 and held for more than five years.

- **Effective Date—**Effective for qualified small business stock acquired after the date of the enactment of the Act.
- **Sunset—**Ineffective for stock acquired after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 1202(1)(3) added.

Act Sec. 1251–Temporary Reduction in Recognition Period for Built-in Gains Tax

S corporations that were previously taxed as C corporations may have built-in gains attributable to the period during which they were a C corporation. If so, and if an asset with a built-in gain is sold by the S corporation during the 10-year period beginning with the date of the corporation's election to be taxed as an S corporation (the "Recognition Period"), then the S corporation pays tax at the highest marginal income tax rate which applies to C corporations in the year the built-in gain is recognized (currently 35 percent).

ARRTA creates new Code Sec. 1374(d)(7), which provides that, if an S corporation has completed its seventh tax year in the Recognition Period, then that S corporation will not recognize any built-in gains, and therefore pay no built-in gains tax, for assets sold in any tax year beginning in 2009 or 2010.

Further, if the S corporation received assets from a C corporation in a carryover basis transaction, then no built in gains will be recognized and no built-in gains tax paid if the gain is recognized in a tax year beginning in 2009 or 2010 and is the eighth, ninth or 10th tax year since the S corporation acquired the asset from the C corporation.

- **Effective Date—**Tax years beginning after December 31, 2008.
- **Sunset—**Tax years beginning after December 31, 2010.
- **Code Secs. Affected—**Code Sec. 1374(d)(7) amended.

Act Sec. 1262–Treatment of Certain Ownership Changes for Purposes of Limitations on Net Operating Loss Carryforwards and Certain Built-in Losses

Code Sec. 382 limits the ability of an acquiring corporation to deduct the net operating losses of an acquired corporation against its future income. These limitations are commonly referred to as "Section 382 limitations."

The Act provides that the Code Sec. 382 limitations will not apply to an ownership change (1) which "is required under a loan agreement or a commitment for a line of credit entered into with the Department of the Treasury under the Emergency Economic Stabilization Act of 2008" and (2) which "is intended to result in a rationalization of the costs, capitalization, and capacity with respect to the manufacturing workforce of, and suppliers to, the taxpayer and its subsidiaries." The relief provided by the Act is not extended to corporations in which a stockholder owns 50 percent or more of the stock of the corporation (by vote or value) immediately after such ownership change. For purposes of this 50-percent test, related parties under Code Secs. 267(b) or 707(b) are aggregated with the stockholder.

- **Effective Date—**Effective for ownership changes after the date of the enactment of the Act.
- **Code Secs. Affected—**Code Sec. 382(n) added.

Act Sec. 1403–Increase in New Markets Tax Credit

Code Sec. 45D provides a tax credit ("the New Markets Tax Credit") to investors owning qualified equity investments made to acquire stock in a corporation or a capital interest in a partnership organized to provide certain services to low-income communities or persons (generally referred to as a "qualified community development entity"). The maximum annual amount of qualified equity investments under prior law was limited to $3.5 billion.

ARRTA increases the maximum annual amount of qualified equity investments to $5.0 billion for the calendar years 2008 and 2009.

Section 1403(b) of the Act contains a transition rule, which provides that the 2008 increase in the maximum annual amount of qualified equity investments is to be allocated by the Secretary of the Treasury pursuant to the provisions of Code Sec. 45D(f)(2) to qualified community development entities that (1) submitted an application for calendar year 2008 and (2) either did not receive an allocation for that year or received a lower allocation than requested. The provisions of ARRTA Section 1403(b) are not included in the Internal Revenue Code.

- **Code Secs. Affected—**Code Sec. 45D(f)(1) amended.

Act Sec. 1511–Delay in Application of Withholding Tax on Government Contractors

Section 511(b) of the Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA) required the Federal government and the government of every state, political subdivision of a state, instrumentality of a state or state subdivision making certain payments to a government contractor to deduct and withhold three percent of the amount to be paid to that person. The withheld amounts were to be paid over to the IRS as an estimated tax payment. The withholding requirement was to apply to payments made after December 31, 2010.

ARRTA delays the application of the three-percent withholding tax regime from December 31, 2010, to December 31, 2011.

- **Effective Date—**Effective on the date the Act is enacted.

Act Sec. 1541–Regulated Investment Companies Allowed to Pass Through Tax Credit Bond Credits

Under prior law, shareholders of regulated investment companies (of which most mutual funds are an example) are allowed the benefit of the tax credits derived from qualified tax credit bonds held by the company. Generally these are qualified forestry conservation bonds under Code Sec. 54B, new clean renewable energy bonds under Code Sec. 54C, qualified energy conservation bonds under Code Sec. 54D and qualified zone academy bonds under Code Sec. 54E. Code Sec. 54A(h) provides that the Secretary of the Treasury is to issue regulations intended to govern allowance of the tax credits attributable to such bonds to the stockholders of the regulated investment companies holding the bonds. This guidance has not been forthcoming.

The Act allows regulated investment companies to elect to allocate the credits attributable to tax credit bonds to their shareholders. The Act defines "tax credit bonds" as either (1) "qualified tax credit bonds" as defined in Code Sec. 54A(d), (2) the Build America Bonds of new Code Sec. 54AA, or (3) any bond for which a credit is allowable under Subpart H of part IV of Subchapter A (generally, clean renewable energy bonds under Code Sec. 54 and the other types of tax credit bonds listed above).

The effect of the election is that the regulated investment company (1) is not allowed any of the tax credits passed through to its shareholders, (2) must include in its gross income the amount of the tax credits that would have applied without the election, and (3) must increase the amount of its dividends paid deduction by the amount of such income. Each shareholder is allowed a share of the credits, but must include in gross income an amount equal to the shareholder's proportionate share of the interest income attributable to the credits.

Prior to passthrough of the credit to the regulated investment company's shareholders, the company must mail a written notice to each shareholder not later than 60 days following the close of the regulated investment company's tax year. The notice must contain the shareholder's proportionate share of the passed-through credits and the amount of gross income the shareholder must recognize as a result of the credit.

- **Effective Date—**Tax years ending after the date of the enactment of the Act.
- **Code Secs. Affected—**Code Sec. 853A added; Code Sec. 54(l) amended; Code Sec. 54A(h) amended.