



SBLC WEEKLY

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SMALL BUSINESS TAX AND LENDING RELIEF

The Senate is scheduled to take up H.R. 5297, the Small Business Jobs and Credit Act of 2010 that provides lending relief and tax relief. The bill is actually the combination of two bills recently passed by the House.

H.R. 5297 would establish a \$30 billion fund to boost lending to small businesses. Under the proposal, the SBLF would support lending among community and smaller banks with assets under \$10 billion. The bill would allow eligible institutions with assets of \$1 billion or less to apply for a capital investment from the Fund of up to 5 percent of risk-weighted assets. It would allow eligible institutions with assets of between \$1 billion and \$10 billion to apply for a capital investment from the Fund of up to 3 percent of risk-weighted assets. The new program would provide an incentive for smaller banks to increase small business lending – as their lending increases, the dividend rate or interest rate payable to Treasury gets reduced, to as low as 1 percent for banks that increase lending by 10 percent from a 2009 baseline.

The bill would create a Small Business Borrower Assistance Program (SBBAP). Under the SBBAP, small businesses that obtain a SBA 7(a) loan (except revolving credit line loans) in the amount of \$300,000 or less will receive a reserve equal to 6 percent of their small business loan principal “to help them make payments through the ups and downs of a cash flow cycle.” according to Representative Schrader, author of the SBBAP idea. Small businesses will automatically be enrolled in the SBBAP if eligible, unless the business specifically requests otherwise. In order to qualify, borrowers must obtain a qualifying loan within one year after the SBA issues final regulations for the program.

The borrower would request payments to be made as needed and the payments made by the SBA under the program shall only be made to the lender or servicer of a qualifying small business loan to be applied against outstanding principal or interest, and may not be made to the borrower.

The bill would exclude from gross income any amounts that are received under the SBBAP.

The bill provides some additional tax reductions for owners of a special type of small business stock. Under current law, Internal Revenue Code (IRC) Section 1202 provides a 50 percent exclusion for gain from the sale of “certain” small business stock that is held for more than five years. The amount of gain eligible for the Section 1202 exclusion is limited to the greater of 10 times the taxpayer’s basis in the stock, or \$10 million gain from stock in that small business corporation. The non-excluded portion of section 1202 gain is taxed at the lesser of ordinary income rates or 28 percent, instead of the lower capital gains rates for individuals. The term “certain” is based on the fact there are several specific conditions related to the nature of the stock that severely limit eligibility.

The American Reinvestment and Recovery Act temporarily increased the Section 1202 exclusion to 75 percent for qualifying stock acquired in 2009 and 2010.

The bill would temporarily increase the amount of the exclusion to 100 percent for qualifying stock acquired after March 15, 2010 and before January 1, 2012.

Under current law, IRC Section 6707A imposes a penalty on the failure to disclose a “reportable transaction” on any tax return or information statement. There are six categories of reportable transactions, one of which is a “listed transaction.” A “listed transaction” is a type of transaction identified by the IRS through guidance as a tax avoidance transaction. The penalty for failure to disclose a reportable transaction (other than a listed transaction) on a return is \$10,000 in the case of individuals and \$50,000 in any other case. For listed transactions, the penalty is \$100,000 in the case of individuals and \$200,000 in any other case. The Internal Revenue Service has taken the position it has no latitude to mitigate penalties and must assess the full penalty for inadvertent violations.

The bill would make the penalty for failing to disclose reportable transactions (including listed transactions) proportionate to the underlying tax savings.

Under current law, business expenditures are deductible against related business income even if they are financed with non-recourse debt. However, in order to prevent taxpayers from engaging in certain types of tax shelters, Congress enacted the “at-risk” rules to prevent taxpayers from using expenses financed with non-recourse debt to shelter unrelated income. There are exceptions to the at-risk rules in situations where Congress believed that, even though a project was financed with non-recourse debt, that it is likely that the financing will be repaid and that the purchaser will have real equity in property financed with the non-recourse debt (e.g., real estate).

The bill would provide an exception to the “at-risk” rules for non-recourse loans that are guaranteed by the Small Business Administration (SBA). The passive activity loss rules would still apply to these expenses to prevent taxpayers from engaging in tax shelter transactions.

Under current law, taxpayers may deduct up to \$5,000 in trade or business start-up expenditures. The amount that a business may deduct is reduced by the amount by which start-up expenditures exceed \$50,000. Start-up expenditures are defined as expenses paid or incurred in connection with investigating the creation of a business, and do not include expenses that would otherwise be allowed to be expensed (i.e., capital or equipment investments).

For taxable years beginning in 2010 or 2011, the bill would increase the limit on the tax deduction for trade or business start-up expenditures from \$5,000 to \$20,000, and increase threshold amount for reducing such limit to \$75,000.

In one respect, it would be nice if the Senate just took up the House bill and passed it. But, this being the Senate, no way that is going to happen. We know that there will be a manager’s amendment at a minimum including a bonus depreciation revival.

Senate Finance Committee Chairman Max Baucus (D-MT) and Ranking Member Charles Grassley (R-IA) introduced S. 3513, The Bonus Depreciation Extension to Create Jobs Act. The bill would extend the 50 percent bonus depreciation through 2010. The most recent version of bonus depreciation was enacted as part of the 2008 economic stimulus efforts.

The American Reinvestment and Recovery Act extended bonus depreciation, but the provision expired at the end of 2009.

The word is it will be in the manager’s amendment.

TAKING SMALL BUSINESS OUT OF THE EQUATION

A frequently-expressed observation by SBLC is we do not understand why Members of Congress do not take an extra few minutes and figure if there is some way to avoid dragging small business into the debate if they are proposing something the business community does not like. While we do not like ANY tax increases, if you set the threshold high enough, it is difficult for us to make a credible argument that it will hurt us.

In the estate tax relief debate, we have said for years now, that it is unfortunate that the super-wealthy and small business have been tied together.

Gives us a simple big exemption (we started advocating for a \$10 million exemption six years ago, and for a \$5 million exemption for the last few) and we are out of the game. It has been a source of frustration for us that the super-wealthy have always dragged us into the rate debate. Hello. A one percent cut off the top rate means a whole lot more to the super wealthy with a \$500 million potential estate than a \$10 million exemption off the bottom. It is easy arithmetic to see why.

Senator Bernie Sanders (I-VT) has introduced legislation, S.3533, the Responsible Estate Tax Act, to reinstate the estate tax.

Depending on the nature of your half glass, it is either permanent reinstatement or permanent relief.

He would reinstate the minimum exemption at the 2009 level of \$3.5 million for an individual. The top rate would be 45 percent for the excess, until you get to \$10 million and the top rate goes up to 50 percent on the excess. When you hit \$50 million the top rate goes up to 55 percent on the excess (which it will be on estates over \$1 million starting in 2011, if nothing is done!)

He adds another 10 percent surtax on estates over \$500 million.

He also provides some additional relief for farmers, allowing them to reduce the value of their farmland by \$3 million.

There are a couple of technical changes that may have some potential negative impact on some small businesses but in the scope of things not of major magnitude.

If he had started at \$5 million and included an adjustment for inflation, that would have been terrific. As it is, I am not sure how we can ignore this.

FOURTH OF JULY

As is our custom, no Weekly when Congress is not in session so no Weekly next week. Happy Fourth of July!