



# *SBLC WEEKLY*

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## ***ADDING INSULT TO INJURY***

The small business lending assistance and tax relief bill, which the Senate passed last week, the House will pass this week, and the President will sign, contains several items on our “wish list.” Unfortunately, the Senate chose not to address the Form 1099 issue.

Lost in the discussion of the good news and bad news is one revenue offset to which we objected vehemently. The bill, which will soon become law, increases the penalties for failing to file information reporting forms in a timely and correct manner. Yes, those very same Form 1099s that are scheduled to multiple faster than the speed of light.

Here are the current penalties if the business taxpayer fails to file the information return:

- \$15 per information return if you correctly file within 30 days (by March 30 if the due date is February 28); maximum penalty is \$75,000 per year (\$25,000 for small businesses, defined below)
- \$30 per information return if you correctly file more than

30 days after the due date but by August 1; maximum penalty is \$150,000 per year (\$50,000 for small businesses)

- \$50 per information return if you file after August 1 or you do not file required information returns; maximum penalty is \$250,000 per year (\$100,000 for small businesses)

The definition of small business for this purpose is average annual gross receipts of \$5 million or less for the three most recent tax years (or for the period a business has been in existence, if shorter) ending before the calendar year in which the information returns were due.

The new penalties will be:

- \$30 per information return if you correctly file within 30 days (by March 30 if the due date is February 28); maximum penalty is \$250,000 per year (\$75,000 for small businesses)
- \$60 per information return if you correctly file more than 30 days after the due date but by August 1; maximum penalty is \$500,000 per year (\$200,000 for small businesses)

- \$100 per information return if you file after August 1 or you do not file required information returns; maximum penalty is \$1,500,000 per year (\$500,000 for small businesses)

Basically, the single report “inadvertent” penalties doubles and the aggregate amounts increases significantly. The new penalties are effective January 1, 2011.

## ***FORM 1099***

By now, every business owner on the planet knows about the newly expanded requirement to issue information reporting forms, Forms 1099, to vendors of good or services for which the business owner paid the vendor more than \$600 over the course of the year.

During the Senate’s debate on the small business lending assistance and tax relief bill, the Senate had the option to choose from dueling amendments. The Republicans offered an amendment to repeal the expansion. The Democrats offered an amendment to “mitigate” the burden on small business. Both failed. No surprise. The problem with the Republican amendment

was that it used some changes to other parts of the new health care law as the revenue offset, including elimination of a new preventative health care fund. There was no way nineteen Democrats were going to vote for it and a cloture vote failed to get the sixty votes. The good news is the Democratic "mitigating" amendment failed on a cloture vote as well. The mitigation provisions would have made Rube Goldberg proud. The vote tells the proponents a "fix" will not fly.

The momentum for repeal remains. The question is how to maneuver it through the legislative process. In the House, Representative Dan Lungren (R-CA) has filed a discharge petition to require the scheduling of his repeal bill, H.R. 5141 for a vote by the full House. "Discharge" means that the bill is released from the control of the committee with jurisdiction over the bill. Two hundred eighteen Representatives must sign the petition. Needless to say, it does not happen very often but it can be useful to apply pressure and sustain momentum.

There are still other tax bills that will be considered and inclusion of a repeal provision in such a legislative vehicle is the more likely course of action. Senator Mike Johanns (R-NE) picked up some Democratic support for his repeal effort and we will be working with him to build on that effort.

### ***LENDING ASSISTANCE AND TAX RELIEF***

The Senate passed H.R. 5297, the Small Business Jobs Act. The House is expected to pass it this week and the President will sign it into law soon thereafter. The highlights include:

### ***Increase of Section 179 Expensing and Expansion to Certain Real Property***

Under current law, taxpayers may elect to write off the costs of certain tangible personal property that is purchased for use in the active conduct of a trade or business in the year of acquisition, in lieu of recovering these costs over time through depreciation. For the taxable year beginning in 2010, taxpayers may write off up to \$250,000 of these capital expenditures subject to a phase-out once these capital expenditures exceed \$800,000. This bill would increase the thresholds to \$500,000 and \$2,000,000 for the taxable years beginning in 2010 and 2011. At the end of 2011, the amounts would revert to \$25,000 and \$200,000, respectively.

Within the temporary higher thresholds, the bill would allow taxpayers to expense up to \$250,000 of the cost of qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property.

### ***Extension of Bonus Depreciation***

Businesses are allowed to recover the cost of capital expenditures over time according to a depreciation schedule. Congress temporarily allowed businesses to recover the costs of certain capital expenditures made in 2008 and 2009 more quickly than under ordinary depreciation schedules by permitting those businesses to immediately write off 50 percent of the cost of depreciable property placed in service in those years. This bill extends the additional, first-year 50 percent depreciation for qualifying property purchased and placed in service in 2010.

### ***Deductibility of Health Insurance for the Purposes of Calculating Self-Employment Tax***

Under current law, business owners are not permitted to deduct the cost of health insurance for themselves and their family members for purposes of calculating self-employment tax. This provision would allow business owners to deduct the cost of health insurance incurred in 2010 for themselves and their family members in the calculation of their 2010 self-employment tax.

### ***Modification of the Section 6707A Penalty***

The bill revises section 6707A of the Internal Revenue Code to make the penalty for failing to disclose a reportable transaction proportionate to the underlying tax savings. The penalty for failure to disclose reportable transactions to the IRS would be set at 75 percent of the tax benefit received. Reportable transactions are defined as investments in transactions that the IRS has identified as listed tax shelters or that have characteristics of tax shelters, including large losses or confidentiality agreements. The minimum penalty under this bill is \$10,000 for corporations and \$5,000 for individuals, and the maximum penalty is \$200,000 for corporations and \$100,000 for individuals. (A tip of the hat to SBLC Chair Paula Calimafde who brought this to the attention of SBLC long before anybody else had heard of this problem.)

### Increased Deduction for Start-up Expenditures

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 or creating an active trade or business, which would be deductible if paid or incurred in connection with the operation of an existing trade or business. For the taxable year beginning in 2010, the bill would temporarily increase the amount of start-up expenditures that may be deducted to \$10,000, subject to a \$60,000 phase-out threshold.

### Cellular Phone Deductibility

The bill would remove cell phones and similar devices from the list of items that require taxpayer business purpose substantiation so their cost can be deducted or depreciated like other business property, without onerous recordkeeping requirements.

### Small Business Lending Fund

The bill authorizes the creation of the Small Business Lending Fund to provide Treasury with the ability to purchase preferred stock and other debt instruments from eligible financial institutions with less than \$10 billion in total assets. Eligible institutions include insured depositories, bank and savings and loan holding companies, and certain community development loan funds. Eligible institutions with less than \$1 billion in total assets can apply to receive investments of up to 5 percent of their risk-weighted assets. Eligible institutions between

\$1 billion and \$10 billion in total assets can receive investments of up to 3 percent of risk-weighted assets. Participating institutions will pay a 5 percent dividend rate on the preferred stock, but this rate can be reduced to as low as 1 percent if a bank demonstrates a 10 percent increase in small business lending relative to a baseline set using the four quarters prior to enactment. The dividend rate is increased to 7 percent after two years, if the bank does not increase its small business lending. To encourage timely repayment, the rate increases to 9 percent after four and a half years.

### Requirement for Federal Agencies to Expand Their Assessments of Economic Effects on Small Businesses

The bill strengthens the Regulatory Flexibility Act by requiring agencies to respond to the SBA Chief Counsel of Advocacy's comments in the final rule. It also seeks more independence for the Office of Advocacy by mandating a separate line item in the SBA's annual budget.

## **INDEPENDENT CONTRACTORS**

Representative Jim McDermott (D-WA) and Senator John Kerry (D-MA) have introduced new versions of their bills to curtail the use of independent contractors. The identical bills, H.R. 6128 and S. 3786, the Fair Playing Field Act, still permit the Internal Revenue Service (IRS) to write classification standards and do away with a safe harbor for engaging independent contractors based on long standing industry practice. It is frequently referred to as "Section 530 relief" referring to the section of the Public Law that created it. (With respect to giving the IRS the right to write the rules, the small business community has worked since the late 1970s to prevent the IRS from writing the rules and a legislative moratorium has been in place since then. The theory being if Congress cannot set objective standards, how would the IRS?)

The principal change in the bill is to "soften" the transition for reclassification of individuals that are no longer protected by the Section 530 safe harbor.