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Stimulus Bill Provides Acquisition Tax Opportunities

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On February 17, 2009, President Barack Obama signed the stimulus bill, known as the American Recovery and Reinvestment Act of 2009 (the Act), providing $288 billion in tax relief to individuals and companies. Below is a summary of several important federal tax provisions that may apply to the structuring of acquisitions.

Shortened Holding Period for S Corporation Built-In Gains

Conversion of a C corporation to an S corporation is generally not a taxable event. However, the S corporation must hold its assets for 10 years following the conversion (the Recognition Period) to avoid being taxed at the highest taxable corporate rate (currently 35%) on all gains that were built-in at the time of the election. The Act reduces the holding period for assets from ten to seven years for a Recognition Period ending in the 2009 or 2010 tax years. For property acquired from a C corporation in a carryover basis transaction, the recognition period is reduced to seven years from the date the property was acquired. Consequently, an S corporation shareholder may be able to sell the business three years earlier under the new provision and possibly receive preferential tax treatment.

Extension of Bonus Depreciation

Last year, Congress temporarily allowed businesses to immediately deduct 50% of the cost of qualifying purchases, as compared to depreciating them over time. The Act extends this benefit for qualified property purchased and placed in service in 2009. Qualified assets can range from computers to manufacturing equipment but do not include real estate. A business that purchased or plans to purchase qualified tangible assets must place the property in service by January 1, 2010, to take advantage of this provision.

Extension of Enhanced Business Expensing

To increase additional investment and help businesses recover capital expenditures, businesses may immediately expense certain depreciable business assets such as equipment or machinery. Before the Act, the maximum deduction was scheduled to decrease to $133,000. However, the Act increased the maximum deduction to $250,000, with a dollar-for-dollar phaseout to the extent the taxpayer's purchase of qualifying assets exceeds $800,000.

Expanded Carryback of Net Operating Losses for Small Businesses
Before the Act, a net operating loss (NOL) could only be carried back two years before the year in which gross income exceeds business deductions. For 2008 (not 2009), the Act extends the maximum NOL carryback period to five years for small businesses with gross receipts of $15 million or less.

Revocation of Guidance Exempting Banks from Loss Limitation Rules
In late September 2008, the Internal Revenue Service issued Notice 2008-83 to encourage acquisitions of troubled financial institutions. Notice 2008-83 provided that any deduction properly allowed after an ownership change to a bank for losses on loans or bad debts would not be treated as a built-in loss or a deduction attributable to periods before the change date. Banks were permitted to rely on this rule until further guidance was provided. The Act provides that the Internal Revenue Service is not authorized to provide exemptions or special rules that are restricted to particular industries or classes of taxpayers, thus repealing Notice 2008-83. For taxpayers who have already relied upon Notice 2008-83, it is effective only for ownership changes occurring on or before January 16, 2009, except that the guidance is effective for ownership changes occurring after January 16, 2009, that were made under:

a written binding contract entered into on or before January 16, 2009, or

a written agreement entered into on or before January 16, 2009, if the agreement was described on or before that date in a public announcement or in a filing with the SEC required by reason of the ownership change.

What This Means To You
The Act may have created opportunities for additional tax savings when setting the timing and structure of acquisitions. However, many provisions are available for a short amount of time, so immediate consideration should be given to these provisions as they apply to your business.

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