



# 2009 YEAR END TAX PLANNING FOR CONTRACTORS



Dawn M. Greenberg, CPA  
Tax Principal, Construction Services Group  
Cowan, Guteski & Co., P.A.

**L**owering your tax obligation starts with proper planning, and the sooner you begin, the better. Tax benefits can help you achieve a wide range of financial goals. In order to make the most of your money, you need to minimize your tax liabilities and take advantage of every available savings opportunity. As we approach year-end, you should consider implementing some of the following tax-planning strategies for your construction company.

## **Consider Section 179 “expensing” election**

One part of tax planning that contractors must assess is their future need for equipment. The acceleration of equipment purchases prior to year-end may allow you to take advantage of the increased \$250,000 business property expensing election under Tax Code Section 179. To be eligible, business property generally needs to be tangible personal property (i.e., machinery, equipment, furniture and fixtures) or off-the-shelf computer software. In addition, the expensing allowance is phased out dollar-for-dollar by the amount of eligible property that exceeds \$800,000. Up to \$25,000 may be written off for a sport utility vehicle (SUV) or truck that weighs between 6,000 and 14,000 pounds. If your company is hit by the alternative minimum tax (AMT), the expensing election is available for AMT purposes and could decrease your AMT tax liability.

If you plan to make the expensing election but find that your total asset purchases for 2009 are already close to the \$800,000 limit, you may want to postpone buying additional items until 2010. In 2010, your business again may be eligible to take advantage of this deduction. However, after 2009, the dollar amount of this election decreases to the limits in place prior to the American Recovery and Reinvestment Act of 2009 (ARRA).

## **Last call for bonus depreciation**

The Economic Stimulus Act of 2008 brought back the 50% bonus depreciation deduction, and ARRA extended it through the 2009 tax year. If you are planning on making a large equipment purchase this year, you may be able to maximize your current year deductions by taking advantage of the Section 179 deduction and bonus depreciation on the same property. Bonus depreciation is also allowed for AMT purposes.

## **Take into account other depreciation rules**

You generally will want to use the Modified Accelerated Cost Recovery System (MACRS), instead of the straight-line method of depreciation, to get a larger deduction in the early years of an asset's life. The IRS generally treats all newly-acquired tangible assets, other than real estate, as being placed in service at the mid-point of the first year, referred to as the half-year convention. But if you made more than 40% of the year's asset purchases in the fourth quarter, you must use the less favorable mid-quarter convention.

### **Cost segregation studies**

A cost segregation study can result in significant tax savings if your company built or acquired a building in the current or prior year. A cost segregation study identifies property components and their related costs that can be depreciated over five or seven years using 200% of the straight-line rate, or over fifteen years using 150% of the straight-line rate. This allows you to depreciate the property much faster and may dramatically increase your current deductions. By accelerating tax depreciation deductions, significant cash-flow savings can be achieved. With the final year of 50% bonus depreciation, a cost segregation study done in 2009 will yield an even higher benefit. The benefit of a cost segregation study may be limited in certain circumstances; for example, if the business is subject to AMT, has a net operating loss, or is located in a state that doesn't follow federal depreciation rules.

### **Claim all business losses**

A net operating loss (NOL) may normally be carried back two years to obtain a current tax refund, which can provide a cash infusion in times of a loss. Any loss not absorbed in the prior two-year period is then carried forward for up to 20 years. If you prefer, you may choose to waive the carry-back and carry the entire loss forward, which may be beneficial if your marginal tax rate in the carry-back years is unusually low. Other losses that may generate a deduction include casualty and theft losses (to the extent they are not covered by insurance) and losses from the sale or abandonment of business assets.

### **Consider employing your children**

In 2008, changes took effect that broadened the reach of the "kiddie tax." Employing a child age 18 (or a full-time student age 19-23) can save taxes on the child's unearned income. You can take a business expense as long as the child performs services for your business and the salary is reasonable. Therefore, you can shift your high tax bracket dollars to your child's lower tax bracket.

### **Manage work in progress**

A solid understanding of individual jobs can help forecast the operating results of the company for the year, and thus its tax liability. For a contractor using the completed contract method of accounting for long-term contracts for tax purposes, slowing the progress of an individual job late in the year can defer revenue into future years. Contractors not using the percentage of completion method of accounting for long-term contracts for tax purposes must also be cognizant of potential AMT implications, as AMT income for some taxpayers is required to be computed using the percentage of completion method.

### **Employee bonuses**

If you are an accrual-method taxpayer, you may be able to deduct employee bonuses, even if your corporation won't pay the bonuses until early 2010. Just make sure the corporation declares the bonuses before year-end and pays them within the first 2 ½ months of 2010. Bonuses generally cannot be accrued for employees who own a greater-than-50% interest in a C corporation or any interest in an S corporation.

### **Profit sharing contributions**

A profit-sharing plan contribution may be deductible in 2009, even if your business won't have the cash to contribute until after the end of the year. You have until the due date of your return, including extension, to contribute. Therefore, a calendar year corporation has until September 15, 2010, to make a deductible profit sharing contribution for 2009. Consider this approach even if you do have the funds

available at year-end so that your business can invest the cash or use it for business purposes until the contribution is due.

### **Consider distribution decisions and accumulated earnings penalty**

If your business is organized as a C corporation, you should keep taxes in mind when making decisions about distributing corporate earnings. Dividends are taxable to you and the other shareholders who receive them and are not deductible by the corporation. But, the cost of taking dividends has decreased – your tax rate on such income would be capped at a 15% long term capital gain rate. Compensation, while deductible by the corporation, is taxable to you at your regular tax rate, which may be as high as 35%. In addition, compensation is subject to payroll taxes. Compensation must be “reasonable” for it to be deductible.

The IRS can assess a corporate accumulated earnings tax penalty on companies that accumulate excessive amounts of income in order to avoid paying taxable dividends. This penalty is 15% for 2009. Generally, a corporation can accumulate up to \$250,000 without penalty. If your corporation has a reasonable business purpose for accumulating greater earnings – the anticipated purchase of new equipment or bonding requirements, for instance – document why the additional money is needed in the corporate minutes.

### **Evaluate the deduction for domestic production activities**

The American Jobs Creation Act of 2004 (AJA) created a new deduction for manufacturers. The definition of “manufacturer” under the new law is broader than its traditional meaning. The deduction is available to businesses engaged in activities such as construction, engineering, and architectural services. It applies to sales of tangible property produced primarily in the United States. The deduction phased in, and in 2005 and 2006, businesses were allowed to deduct 3% of the lesser of their income from qualified production activities or their taxable income. The allowed deduction increased to 6% for 2007 through 2009, and will be 9% in 2010. The deduction is further limited to 50% of wages paid during the calendar year and can be used against both regular tax and AMT. Plan now to maximize your benefit from this deduction. Determine whether your business qualifies, if there are ways to increase your deduction, and how to capture the necessary information in your accounting system.

### **Energy credits**

A taxpayer may deduct the cost of certain energy-efficient improvements installed on or in a depreciable building located in the U.S., effective for improvements placed in service after December 31, 2005, and prior to December 31, 2013. The deduction applies to “energy-efficient commercial building property,” which is defined as depreciable property that is installed as part of a building’s: 1) interior lighting systems; 2) heating, cooling, ventilation and hot water systems; or 3) envelope, and is part of a certified plan to reduce the total annual energy and power costs of these systems by at least 50% in comparison to a reference building that meets specified minimum standards.

Additionally, the energy credit under Internal Revenue Code Section 48 (a component of the investment tax credit) is 30% in 2009 for: 1) qualified fuel cell property; 2) equipment that uses solar energy to generate electricity to heat or cool a structure (including to provide hot water) or provide solar process heat; and 3) equipment that illuminates the inside of a structure using fiber-optic distributed sunlight. For stationary micro-turbine property and other energy property, the credit remains at 10%. ARRA also reduced some limitations and expanded the availability of this credit. Originally set to expire on December 31, 2008, the 2008 Energy Act extended it through December 31, 2016.



**COWAN, GUNTESKI & Co., P.A.**

Certified Public Accountants and Consultants

SERVING THE TRI-STATE AREA

877-349-6880

[www.CowanGunteski.com](http://www.CowanGunteski.com)

## Tax credit for “energy-efficient” homes

The Energy Tax Incentives Act of 2005 (Energy Act) provides home builders an incentive to build energy-efficient homes. Under a provision in the Energy Act, eligible contractors can qualify for a new tax credit when they construct qualified new energy-efficient homes. Tax credits are more valuable to taxpayers than deductions because they are subtracted dollar-for-dollar off the tax liability. The credit is either \$2,000 or \$1,000 per qualifying home, and construction of the new energy-efficient home must have been substantially completed after August 8, 2005. The qualifying home must be certified to have an annual heating and cooling energy consumption that is 50% below that of a comparable dwelling unit constructed in accordance with certain specified standards. Building envelope component improvements (includes materials or systems specifically and primarily designed to reduce heat loss or gain, exterior windows including skylights, doors, and any duct sealing and infiltration reduction measures) must account for at least 10% of the reduction. The new energy efficient home must be sold by the contractor to a person for use as a residence during the year, and the new home must be acquired prior to January 1, 2010, in order for the contractor or producer to get the credit.

Through careful management of work-in-progress, proper timing of expenses and utilization of tax credits, contractors can accurately assess their tax exposure for the current year. Proper planning can reduce this exposure and alleviate tax filing surprises by allowing the taxpayer time to prepare for tax payments.

*The technical information in this article is necessarily brief. No final conclusion on these topics should be drawn without further review and consultation. Please be advised that, based on current IRS rules and standards, the advice contained herein is not intended to be used, nor can it be used, for the avoidance of any tax penalty assessed by the IRS.*

### ***About Cowan, Guteski & Company, P.A.***

As one of the leading accounting and consulting firms for the construction industry and a Master Sponsor of the New Jersey Builders Association, Cowan, Guteski & Co. provides clients with advice and counsel on how federal and state tax laws could impact their businesses. Our goal is to position your construction company to take advantage of all legitimate strategies to minimize your tax obligation. Contact Dawn Greenberg, CPA and Tax Principal with the Construction Services Group at 732-349-6880 ext. 7718 or [dgreenberg@cowanguteski.com](mailto:dgreenberg@cowanguteski.com) to discuss your particular situation.

As a diversified certified public accounting firm, Cowan, Guteski & Co., is committed to being an active partner in its clients’ growth by delivering value beyond accounting, innovative solutions and consistent exceptional service. Visit [www.CowanGuteski.com](http://www.CowanGuteski.com) for more information on the services available to meet the unique needs of the construction industry.

