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President's Budget Seeks to Expand or Extend Several Business Tax Credits and Deductions

by Clare Stoudt

The Obama Administration's Fiscal 2011 budget proposal (the "Budget"), released to Congress on February 1st, would extend and/or expand the new market tax credits, advanced energy project credits, cash grant in lieu of low-income housing credits program, research and experimentation credits, business expense deductions, and bonus depreciation deductions and would create a new hiring tax credit.

New Market Tax Credits. The federal allocation of the New Markets Tax Credit (NMTC), a 39% credit for qualified equity investments made to acquire an interest in a qualified community development entity that is held for a period of seven years, expired in 2009. The Budget would extend the NMTC through 2011 and increase the allocation amount from $3.5 billion per year to $5 billion per year. The NMTC has become an important source of financing for a variety of development projects in qualified communities.

Qualified Advanced Energy Project Credits. The American Recovery and Reinvestment Act of 2009 (ARRA) established a new 30% credit under Section 48C for "clean energy technology manufacturing facilities," which was capped at $2.3 billion. Unlike other investment tax credits, the Section 48C credit was not self-executing; taxpayers were required to submit applications for certification by the Department of Energy and allocation of credits on a competitive basis. Projects submitted in the initial application process far exceeded the original $2.3 billion of credits. The Budget would allocate an additional $5 billion of the 30% credits. The additional $5 billion might not even cover the remaining eligible projects for which applications were previously submitted. Some industry participants have suggested that an alternative cash grant election might be helpful for start-up operations.

Low-Income Housing Credits. In response to the diminished market for low-income housing tax credits (LIHTC) which resulted from the recession, the ARRA included provisions that allowed state housing agencies to opt to receive a cash amount in lieu of a portion of the state's Section 42 LIHTC allocation in 2009. States were required to use these grants in lieu of credits to make awards to finance the construction or acquisition of qualified low-income housing projects generally subject to the same rental requirements and recapture rules as properties financed with LIHTC. This program has been critical in assisting states in replacing the capital from tax credit investors and continuing the construction of low-income housing projects in the pipeline. The Budget would modify and extend these provisions to allow states to elect to give cash assistance in lieu of up to 40% of their 2010 per capita LIHTC allocation.

Research and Experimentation Tax Credit. The Budget would make permanent the Section 41 research and experimentation (R&E) tax credit. This 20% credit for incremental R&E expenditures has long been in the Internal Revenue Code, subject to various sunset and termination rules, and most recently expired at the end of 2009.

Expensing of Assets. The Budget would continue for 2010 the more expansive Section 179 election limits on the expensing of expenditures by small businesses applicable for 2008 and 2009. For 2010, eligible taxpayers would be allowed a maximum deduction of $250,000 for the cost of qualifying property placed in service in 2010, with a phase-out beginning at $800,000 of qualifying investment.

Bonus Depreciation. The Budget would extend the Section 168(k) special bonus depreciation election, an additional first-year depreciation deduction of 50% of basis for certain qualified property, to property acquired after 2007 and before 2011, and placed into service during 2010 (through 2011 for certain longer-lived and transportation property).

Job Creation Credit. The Budget also has a line item for a $33 billion initiative under which businesses would be granted a $5,000 tax credit for each net new employee hired in 2010, although the proposal was not specifically described in the Budget.

In a February 4th news conference, Senate Majority Leader Harry Reid (D-Nev.) and other Senate Democrats introduced a jobs agenda that includes a number of tax incentives. The package includes a job creation tax credit, extensions of unemployment insurance and benefits, small business investment depreciation, extension of highway construction initiatives, and Build America Bonds. The hiring tax credit faces opposition in the House, however, with Ways and Means Committee members expressing their concern on the proposal to Treasury Secretary Geithner earlier in the week.

If you would like to learn how one or more of these provisions would specifically impact your organization, please contact one of the following members of Pillsbury's tax team:

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