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TAX CHANGES FOR BUSINESSES AND CORPORATIONS IN THE JOBS AND GROWTH TAX RELIEF RECONCILIATION ACT OF 2003

As you probably know, Congress recently passed the Jobs and Growth Tax Relief Reconciliation Act of 2003. The Act contains important changes for businesses and corporations, including two temporary tax breaks designed to encourage immediate investments. Under the first of these breaks, small companies can expense up to $100,000 in new equipment investments through 2005. Under a second provision, businesses can depreciate more of their assets sooner through 2004. Another change for corporations affects the estimated tax payment rules for 2003. Small business owners will also benefit from accelerated rate reductions. The purpose of this letter is to provide you with a brief overview of these provisions.

VASTLY LIBERALIZED EXPENSING ELECTION

The expensing election permits small businesses to expense (i.e., to deduct immediately rather than depreciate over several years) a certain amount of the cost of tangible depreciable personal property purchased and placed in service in an active trade or business during the tax year. Tax compliance by small businesses will be simplified because they will be able to avoid the complexities of the depreciation rules. Under the 2003 Jobs and Growth Act, all of the following expensing changes are effective for tax years beginning after 2002 and before 2006:

- The maximum annual expensing amount is $100,000 (it was $25,000 before).
- The maximum annual expensing amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the tax year exceeds a specified dollar level. This dollar level is increased to $400,000 (from $200,000).
- The above increased dollar amounts will be inflation-indexed for tax years beginning after 2003.
- Off-the-shelf computer software is made eligible for expensing.
- Taxpayer revocation of expensing elections will no longer require IRS consent.

INCREASE AND EXTENSION OF BONUS FIRST-YEAR DEPRECIATION

In general, under pre-2003 Jobs and Growth Act law, a 30% additional first-year depreciation allowance applied to the non-expensed portion of qualified property (which included most new MACRS property) if: (1) its original use commenced with the taxpayer after September 10, 2001; (2) the asset was acquired by the taxpayer after September 10, 2001 and before September 11, 2004; and (3) it was placed in service by the taxpayer before 2005 (before 2006 for certain property with longer production periods).

The Act makes the following changes:

< For 30% bonus first-year depreciation purposes, property can be acquired before 2005.

< 50% bonus first-year depreciation applies to qualified property if (1) its original use commences with the taxpayer after May 5, 2003; (2) the asset is acquired by the taxpayer after May 5, 2003, and before 2005 (there can't be a written binding contract for acquisition in effect before May 6, 2003); and (3) it is placed in service by the taxpayer before 2005 (before 2006 for certain property with longer production periods).

< Taxpayers can elect on a class-by-class basis to claim 30% instead of 50% bonus first-year depreciation for qualifying property, or elect not to claim bonus first-year depreciation at all. Two situations in which a taxpayer would likely consider making an election to claim smaller bonus first-year depreciation (or to elect out of it entirely) are where the taxpayer (1) has about-to-expire net operating losses, or (2) anticipates being in a higher tax bracket in future years.

Note, under the 2003 Jobs and Growth Act, as under pre-2003 Jobs and Growth Act law, there is no alternative minimum tax (AMT) depreciation adjustment for the entire recovery period of qualified property recovered under the bonus first-year depreciation rules (50% or 30%).

 # LIBERALIZED CORPORATE ESTIMATED TAX FOR 2003

Despite the general rule that estimated tax payment installments must be made no later than April 15, June 15, September 15 and December 15, 25% of the amount of any required installment of corporate estimated tax which is otherwise due on September 15, 2003, will not be due until October 1, 2003. The change in installment due date to October 1, 2003 for 25% of the amount of the installment that otherwise would have been due in September affects corporations using (1) the calendar year (third installment of estimated tax would have been due on September 15, 2003); (2) a fiscal year ending March 31, 2004 (second installment would have been due on September 15, 2003); (3) a fiscal year ending May 31, 2004 (first installment would have been due on September 15, 2003); and (4) a fiscal year ending September 30, 2003 (last installment would have been due September 15, 2003). The due dates for all other estimated tax payments aren't changed by the 2003 Jobs and Growth Act provision.

 # ACCELERATION OF REDUCTION IN INDIVIDUAL INCOME TAX RATES

The 2003 Jobs and Growth Act also includes individual tax rate changes that will help small businesses, including an immediate reduction of the marginal tax brackets paid by all but the lowest earners. Under the change, the tax rates for 2003 and thereafter above 15% are 25%, 28%, 33%, and 35% (previously rates for 2003 above 15% were 27%, 30%, 35%, and 38.6%). These rate reductions had been scheduled for 2006.

After 2010, rates above 15% are scheduled to revert to the pre-Economic Growth and Tax Relief

Reconciliation Act of 2001 levels (i.e., 15%, 28%, 31%, 36%, and 39.6%). Sole proprietors and owners of pass-through entities such as partnerships should particularly benefit from the acceleration in the reduction in the top tax brackets.