

State and Local Tax Bulletin

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Alabama Edition



BRADLEY ARANT
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LLP

New Federal and State Legislation Provide Tax Incentives to Promote Job Creation

By Bruce P. Ely, James E. Long, Jr. and William T. Thistle

Upcoming Seminars Involving Members Of Our SALT Practice Group

May 3, 2010

Tax Executives Institute, Houston Chapter. Chris Grissom will be speaking on the State Taxation of Pass-Through Entities. For more information, please visit the TEI website: www.tei.org.

May 13-14, 2010

Alabama Society of CPAs Annual Business and Industry Conference, Hyundai Motor Manufacturing Plant, Montgomery, Alabama. Jimmy Long and Will Thistle will be speakers in a presentation on Recent Alabama Tax Developments. For more information, please visit the ASCPA website: www.ascpa.org.

May 13, 2010

Alabama State Bar, Section of Taxation Annual Meeting, Montgomery, Alabama. Bruce Ely will be speaking on the Alabama Tax Legislative Update: 2010 Regular Session, and Jimmy Long will be serving as a co-panelist regarding the Disharmony in Alabama's Conformity to Federal Tax Classification for Business Entities. For more information, please visit the Alabama State Bar's website, www.alabar.org.

This Spring, both Congress and the Alabama Legislature passed bills designed to promote job creation. Both the "Hiring Incentives to Restore Employment Act" (the "HIRE Act," Public Law 111-147) and the "Reemployment Act of 2010" (Alabama Act 2010-557) provide tax incentives for businesses that hire unemployed workers. On March 18, 2010, President Obama signed the HIRE Act into law. The HIRE Act encourages companies to hire unemployed workers by exempting certain wages from Social Security taxes (payroll tax exemption), and by providing employers with a business tax credit if they retain the new hires for at least 52 consecutive weeks. Similarly, the Reemployment Act of 2010, which Governor Riley signed last week, is designed to create jobs by providing an income tax deduction to businesses that hire certain unemployed persons. Each incentive is summarized below.

The Federal HIRE Act

The HIRE Act is estimated to create 250,000 jobs nationally and cost \$17.6 billion. The HIRE Act encourages employers to hire (and retain) unemployed workers by establishing two federal tax incentives and also aims to help small businesses by extending the maximum amount that they can deduct in the first year under I.R.C. section 179 for property placed in service in 2010.

The HIRE Act's first tax incentive targeted towards unemployment relief is the so-called "payroll tax holiday," which relieves qualified employers of their 6.2% share of Federal Insurance Contribution Act (FICA) taxes for certain qualified individuals. For 2010, this incentive could save employers up to \$6,621.60 per new employee. A "qualified individual" must: (1) begin employment **after February 3, 2010 and before January 1, 2011**; (2) certify by a signed affidavit that he or she has not been employed for more than 40 hours during the 60-day period before employment with the qualified employer; (3) not have been hired to replace another employee, unless that employee voluntarily quit or was terminated for cause; and (4) not be "related" to the qualified employer. A "qualified employer" is defined broadly to include all private sector employers, and only excludes government employers (except for public institutions of higher education). The IRS has released a revised 2010 Form W-2 to report wages and a new Form W-11, an affidavit for a new hire to certify his or her qualification under the HIRE Act.

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The HIRE Act's second incentive provides a new income tax credit up to \$1,000, applicable to any **tax year ending after March 18, 2010**, for any "qualified individuals" (as defined above) that were: (1) employed by the taxpayer at any time during the taxable year; (2) employed for a period of not less than 52 consecutive weeks; and (3) whose wages during the last 26 weeks of their employment equaled at least 80% of their wages during the first 26 weeks of their employment. A taxpayer will be entitled to a \$1,000 business tax credit under I.R.C. section 38(b) if they hire qualified individuals who satisfy these three conditions and earn annual wages in excess of \$16,129.03.

The HIRE Act also provides additional economic incentives for small businesses by extending maximum expensing amounts under I.R.C. section 179 for tangible personal property placed in service during 2010. Section 179 allows certain taxpayers to elect to immediately deduct the cost of qualifying property placed in service during the taxable year, rather than recovering the cost of such property through depreciation or amortization deductions over time. Qualifying property generally includes tangible personal property used in a trade or business (including canned software). The taxpayer's section 179 deduction may not exceed the taxable income derived from the applicable trade or business, but any excess section 179 deduction may be carried forward to subsequent tax years. With respect to taxable years beginning in 2008, the maximum amount that a taxpayer could expense under section 179 was increased to \$250,000. However, the maximum expense allowance was reduced by the amount by which the cost of qualifying property placed in service during the taxable year exceeded \$800,000. The HIRE Act extends both the temporary \$250,000 maximum and \$800,000 threshold for taxable years beginning after 2007 and before 2011.

The Alabama Reemployment Act of 2010

Introduced by Gubernatorial candidate Robert Bentley (R-Tuscaloosa), the Reemployment Act of 2010 provides an income tax deduction for Alabama employers that create jobs for unemployed persons. Dr. Bentley has publicly stated that he anticipates this bill will create 4,000-5,000 jobs statewide. The income tax deduction is an amount *up to* 50% of the gross wages paid to each person hired. To qualify for the deduction, when the new employee is hired, he or she either must have been drawing state unemployment compensation benefits or his or her unemployment benefits must have expired. In addition, the employer must *retain* the new employee for at least one year to receive the income tax deduction.

Although it appears that the one year testing period **starts immediately**, the income tax deduction is only

effective for tax years 2011 and 2012 and is tied to wage rates paid to otherwise qualified employees. For instance, a deduction equal to 50% of gross wages is only permitted for wage rates of \$14 per hour and above; a 40% deduction is granted for wage rates between \$12 and \$14 per hour; and a 35% deduction is granted for wages rates between \$10 and \$12 per hour. No deduction is available if the job pays less than \$10 per hour or if the employee works less than 37.5 hours per week, regardless of the employee's wage rate, or (as mentioned above) if the employee does not remain on the payroll for at least one year.

For "qualified investing companies," which generally must invest \$2 million and create 20 new jobs in specified industries, this deduction may be in addition to Alabama's lucrative capital investment tax credit, otherwise known as the Capital Credit. Alabama's Capital Credit program provides a corporate or individual income tax credit equal to 5% per year of the total capital costs of certain qualifying projects, for up to 20 years. In effect, the qualifying project owner is entitled to receive an income tax credit for 100% of its capital costs, claimed over a 20 year period, but only if the project meets certain initial *and* continuing eligibility criteria.

The minimum wage requirements to be eligible for the Capital Credit were increased last year to the lesser of (a) \$15 per hour (indexed for inflation) or (b) the average hourly wage of the county where the project is located, both excluding benefits, for all projects that file their statements of intent with the Alabama Department of Revenue after May 21, 2009 (the effective date of Acts of Alabama 2009-722). However, the Alabama Legislature recently provided a six-month transition period to investing companies that filed their statements of intent with the ADOR on or before November 21, 2009. Such an investing company is only required to satisfy the base wage requirements that were in effect prior to May 21, 2009, *i.e.*, \$8 per hour (or \$10 per hour, including benefits). Thus, new investing companies making a substantial capital investment in-state and who hire unemployed workers at \$15 per hour (or just \$14 per hour in certain counties) could receive both a Capital Credit and an income tax deduction equal to 50% of the gross wages paid to those workers.

If you have any questions regarding how these new incentives may affect your company or clients, please contact Bruce Ely (205-521-8366), Chris Grissom (205-521-8514), Stuart Frentz (205-521-8216), Jimmy Long (205-521-8626) or Will Thistle (205-521-8985).

COST Southeast Regional Seminar

Please mark your calendars for the Council On State Taxation (COST) Southeast Regional Seminar, presenting an update on significant state tax issues for Alabama, Arkansas, Florida, Georgia, Mississippi, North Carolina, South Carolina and Tennessee. The seminar will be held in Birmingham (Energen Corporation, 1st Floor Auditorium), May 25 from 8:00 am to 1:45 pm, and is open to tax professionals from both COST member companies and non-COST member companies. The COST Southeast Regional Seminar includes the following topics:

- Recent Developments in the Southeastern States
- State Tax Policy Update: 2010 & Beyond - Including Certain Proposed Federal Legislation
- Discussion of Latest & Greatest State Tax Litigation
- States Under Fiscal Stress - Dealing with the State Tax Challenges from the Increased State Needs for More Revenues
- "Tell It To The Judge & Other Alabama Revenue-ers" - A Department of Revenue Update and Q&A with Chief Administrative Law Judge Bill Thompson and the Commissioner's Office

The registration fee is \$40 for COST members and \$75 for non-COST members. More information is available on COST's website, www.cost.org.

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