“Small Business and Work Opportunity Tax Act of 2007: Follow the money!”

One way to judge which are the most significant provisions in the Small Business and Work Opportunity Tax Act of 2007 – signed by President Bush on May 25, 2007, as part of a larger bill focused on war funding – is to look at which provisions are projected to cost the most or to raise the most revenue.

The tax breaks included in this legislation are fully paid for with revenue increases. The main premise behind the legislation is that small business should receive some tax breaks to help offset the cost of being required to pay workers more due to the minimum wage increase. It would be a rare small business that finds that the cost of increasing the minimum wage for its workers is fully offset by the tax breaks included in the legislation.

Still, a little help is better than none, and besides, it’s the thought that counts at least Congress may hope it counts come election time.

Another interesting result of a look at the numbers is that, in some cases, today’s tax break is tomorrow’s tax increase, or vice-versa. With Congress, it is all about getting the right numbers in the right years. So sometimes what appears to be a significant tax item over a five-year period does not look so significant 10 or more years out.

THE BIG TAX BREAKS

The winning tax break is the extension and modification of the Work Opportunity Tax Credit. The credit has been extended to Aug. 31, 2011. The veterans category has been expanded to include veterans with service-connected disabilities who have been unemployed for six months or more during a one-year period ending on the hire date. The qualified wage threshold for this group has also been increased. The high-risk youth category has been expanded to include rural counties with declining populations. This change comes in with a projected 10-year cost to the government of $2.572 billion, with most of that coming in getting help to small businesses likely to be hiring minimum wage workers.

The third most significant tax break (being discussed ahead of the second most significant because the two are related) in terms of revenue cost is the $457 million 10-year cost of permitting the tax credit for Social Security taxes paid with respect to cash tips to continue to be calculated at the old minimum wage rate of $5.15. This tax break also appears to be well-focused on helping the businesses that are most affected by the minimum wage increase.

The second most significant tax break is allowing both of the two preceding tax breaks for alternative minimum tax purposes. Allowing the WOTC for AMT purposes comes with a projected 10-year cost of $65 million, and allowing the FICA tip credit for AMT purposes comes with a 10-year cost of $552 million, more than the projected cost of the underlying tax break.

The package of S corporation relief provisions together are projected to have a 10-year cost of $892 million. Of these, the most significant would be the exclusion of capital gains from passive investment income, at a cost of $361 million; the treatment of qualifying director shares, at a cost of $201 million; and the recapture of bad debt reserves, at a cost of $199 million.

The tax breaks focused on the Gulf Opportunity Zone together come with a 10-year cost of $239 million, with almost all of that associated with a two-year extension and modification of a provision with respect to use of the Low-Income Housing Credit with respect to areas damaged by Hurricane Katrina, Rita and Wilma.

Last on the list, although getting a lot of attention, is the increase and extension of the Code Sec. 179 expensing election through Dec. 31, 2010. Although this would move to the top of the list if looking at the five-year cost projection ($3.503 billion), by the 10-year point the cost is only $68 million. The projection experts are predicting logically that this provision will primarily just accelerate into earlier years depreciation that would have been claimed anyway later in the 10-year period.

THE REVENUE RAISERS

Tops on the list here is a modification of the suspension-of-interest rules where the Internal Revenue Service fails to give timely notice. The rules will now come into effect only after 36 months, rather than after 18 months. Apparently the 18-mont deadline was too tough for the IRS to work with. This change is projected to raise $2.43 billion over 10 years.

Next on the list, and the provision getting the most attention from individual taxpayers, it the provision raising the age of the "Kiddie Tax" in 2008 to children under the age of 19 and full-time students under the age of 24. This provision comes just in time to frustrate planning for the capital gain tax rate falling to zero for taxpayers in the lowest two tax brackets in 2008 through 2010. This provision is projected to raise $1.432 billion over the nest 10 years.

Third on the list is the cutback in the entitlement to collection due process procedures for employment tax liabilities. This restriction is projected to raise $288 million over 10 years.

Although not listed as a revenue raiser, the increase in the minimum wage itself is projected to raise $457 million in revenue over 10 years. This revenue estimate only reflects the reduction in the amount of credits that taxpayers may claim under the FICA tip tax credit as a result of increasing the minimum wage.

A good example of a provision solely inserted for budget manipulation is the increase in corporate estimated tax payments due in July through September of 2012. This projection, over a five-year period, would top the list of revenue raisers at roughly $5 billion. This is fully offset, however, in 2013, leaving a 10-year projected cost of $0.

SUMMARY

With tax breaks totaling $4.844 billion over 10 years, the Small Business and Work Opportunity Tax Act of 2007 is, in the grand scheme of things, not a very significant piece of tax legislation. Still, it does seem to accomplish its stated purpose – to give small business a little something on the tax side to help offset the minimum wage increase included in the legislation.

Although the tax breaks are totally offset with revenue raisers, the revenue raisers are not primarily directed at small business. Individuals and corporations, and anyone with a late IRS notice, will pay for the tax breaks focused at small business. And although small business will be the beneficiary of most of the larger tax breaks, when you add in the minimum wage increase, small business does not come out ahead under this legislation either.