

## What Contractors Need to Know About the New Tax Laws

1. Changes have been made to tax laws during 2004. Those that most affect contractors include the following:

### A. American Jobs Creation Act signed October 22, 2004

- 1) **Allows individuals to deduct the greater of sales tax expense or state income tax expense**
  - a. Begins in 2004
  - b. IRS to produce a table based on income
  - c. Tax on autos and boats is added to table amount
- 2) **Allows manufacturers a 3% deduction (increasing to 9% in 2010) against profit from domestic manufacturing activity**
  - a. Construction is included in definition of manufacturing activity (also engineering and architectural services)
  - b. Limited to 3% of the lesser of taxable income or production income
  - c. Deductible in years starting after 2004

Revenue (Construction and/or Plant)	\$10,000,000
Direct Cost	<u>9,000,000</u>
Gross Profit	1,000,000
General and Administrative Expenses	<u>500,000</u>
Taxable Income	<u>\$ 500,000</u>
Lesser of Gross Profit (\$1,000,000) or Taxable Income (\$500,000)	\$ 500,000
Deduction Percentage	<u>3%</u>
Deduction From Taxable Income	<u>\$ 15,000</u>

- 3) Limits expensing deduction for vehicles less than 14,000 pounds to \$25,000 in first year**
  - a. Bonus and regular depreciation can add to \$25,000 limit
  - b. Purchases after 10/22/04
  
- 4) Allows exemption for “mobile machinery” from federal highway taxes (12% excise tax and heavy vehicle use tax)**
  - a. Mobile machinery is designed for off-road use but reaches job sites over public roads under its own power
  - b. Includes mobile cranes, concrete pumpers, paving equipment
  
- 5) Increases first year depreciation expense deduction (Section 179) to \$102,000**
  - a. Total fixed asset purchases cannot exceed \$410,000 for the year
  
- 6) Reduces depreciable life for leasehold improvements**
  - a. Reduces depreciable life from 39 years to 15 years
  - b. Property placed in service after 10/22/04
  - c. Improvements must be made to buildings more than 3 years old

**B. New tax law did not extend 50% bonus depreciation on new equipment**

- 1) Expires 12/31/04
- 2) Allowed in 2005 for aircraft and long-lived assets (15 years) under contract in 2004

**C. Corporations with \$10 million in assets required to file form M-3 with 2004 tax return**

- 1) Reconciles financial statement income with tax return
- 2) Designed to smoke out large tax shelters but long-term contracts are included