

December 14, 2006

Dear Clients and Friends,

The recently passed 2006 Tax Relief and Health Care Act, a wide-ranging measure that preserves a variety of popular tax breaks for families and businesses, extends energy provisions encouraging alternative and renewable energy sources, and includes trade, oil drilling and Medicare provisions, and contains an array of tax provisions with immediate and long-term impact on businesses. Here is a look at the key tax provisions that directly affect business taxpayers.

**Extension and modification of certain tax relief provisions:**

The new law extends through 2007, and in certain circumstances modifies, provisions which under prior law either expired at the end of 2005 or would have expired at the end of 2006. These include:

- ◆ Research tax credit. The research and development (R&D) credit, which expired at the end of 2005 under prior law, is extended to qualified amounts paid or incurred during 2006 and 2007. In addition, for tax years ending after 2006, the new law enhances the credit by (i) increasing the rates of the alternative incremental credit and (ii) creating a new alternative simplified credit that does not use gross receipts as a factor (so that newer businesses can access the credit).
- ◆ Work opportunity and welfare-to-work tax credits. The work opportunity tax credit (WOTC), which is a credit for wages paid by employers who hire individuals from certain targeted groups, and the welfare-to-work tax credit (WWTC), which is a credit for wages paid by employers who hire long-term family assistance recipients, are extended in their current form for 2006 and combined in 2007. Modifications of the combined credit include expanded eligibility for the WOTC (raised age ceiling for food stamp recipients from 25 to 40), revised eligibility requirements for ex-felons, and extension of the paperwork filing deadline from 21 days to 28 days.
- ◆ New markets tax credit. The credit is extended for one year (through the end of 2008), permitting a \$3.5 billion maximum annual amount of qualified equity investments.
- ◆ Qualified zone academy bonds (QZABs). QZABs are tax credit bonds issued by States or localities principally for school renovation. Bond holders may claim a tax credit against federal income taxes in lieu of receiving interest. The new law extends QZABs for two years and authorizes states to issue up to \$400 million of QZABs for 2006 and 2007. The new law also adds special rules relating to expenditures and arbitrage and new information reporting rules.
- ◆ Brownfield remediation expensing. Expensing of costs associated with cleaning up hazardous (“brownfield”) sites is extended through 2007, and the definition of an eligible contaminated site is expanded to include sites contaminated by petroleum products.
- ◆ Tax incentives for investment in the District of Columbia. Three tax benefits available to businesses operating in designated D.C. enterprise zones are extended through 2007— 20% wage credit, \$35,000 of additional expensing under Sec. 179, tax-exempt bonds—and zero capital gains for property held five years is extended through 2012 (two year extension).
- ◆ Indian employment tax credit. The business tax credit available for employers of qualified employees that work and live on or near an Indian reservation is extended through 2007.

- ◆ Accelerated depreciation for business property on Indian reservations. A special depreciation recovery period for qualified Indian reservation property is extended to property placed in service through 2007.
- ◆ Leasehold and restaurant improvement recovery. The accelerated writeoff for certain leasehold improvements and restaurant property (depreciation over 15 years instead of 39 years) is extended through 2007.
- ◆ Enhanced deduction for corporate contributions of computer equipment for educational purposes. The rule that encourages businesses to contribute computer technology and equipment to schools by allowing an enhanced deduction for such contributions is extended through 2007.
- ◆ Suspension of 100 percent-of-net income limitation on percentage depletion for oil and gas from marginal wells. This tax break is extended through 2007.
- ◆ Economic development credit for American Samoa. A new temporary 2-year credit for possessions corporations operating in American Samoa is provided. The credit, which is generally based on the amount of wages paid in American Samoa and depreciation deductions with respect to property located in American Samoa, is effective for the first two years beginning after Dec. 31, 2005 and before Jan. 1, 2008.
- ◆ GO Zone bonus depreciation. The bonus 50% first-year depreciation break that was included in the Gulf Opportunity Zone Act of 2005 is modified by extending the placed-in-service deadline for certain property used in certain highly damaged areas within the Gulf Opportunity Zone.

**Extension of certain expiring energy provisions and other energy provisions:**

The new law provides an extension through 2008 of a number of energy provisions that would have expired at the end of 2007 under prior law. It also contains a package of other energy provisions. The changes include:

- ◆ Credit for electricity produced from certain renewable resources. The placed-in-service date for facilities qualifying for the renewable electricity production tax credit is extended for one year through Dec. 31, 2008 for certain facilities (e.g., those producing electricity from wind, closed-loop biomass, open-loop biomass, small irrigation, landfill gas, and trash combustion).
- ◆ Energy credit for certain business purchases. The 30% business tax credit for the purchase of fuel cell power plants and solar equipment is extended through Dec. 31, 2008.
- ◆ Credit to holders of clean renewable energy bonds. The clean renewable energy bond (CREB) program is extended through Dec. 31, 2008 and an additional \$400 million of CREB bonding authority is provided.
- ◆ Special depreciation allowance for cellulosic biomass ethanol plant property. The new law provides 50% bonus first-year depreciation for new qualified cellulosic ethanol plants placed in service after the date of enactment of the new law and before 2013.
- ◆ Credit for new energy efficient homes. The tax credit for builders of new energy efficient homes is extended for one year through Dec. 31, 2008. The credit applies to manufactured homes meeting a 30% energy reduction standard and other homes meeting a 50% standard.
- ◆ Deduction for energy efficient commercial buildings. The deduction for energy efficient commercial buildings meeting a 50% energy reduction standard is extended for one year, through Dec. 31, 2008.
- ◆ Clean coal gasification tax credit. The tax credits for subbituminous coal gasification projects are modified, effective for applications for certification submitted after Oct. 2, 2006, to ensure that more of these facilities are constructed.

**Other tax relief provisions:**

The new law also contains a package of other tax provisions designed to provide additional tax relief and certainty to taxpayers. These include:

- ◆ Manufacturing deduction for U.S. businesses with branches in Puerto Rico. The new law allows qualifying U.S. businesses operating as branches in Puerto Rico to claim the Sec. 199 domestic manufacturing deduction, effective for the first two years of the taxpayer beginning after 2005 and before 2008.
- ◆ Mine safety provisions. The new law provides 50% expensing for certain equipment expenditures related to safety equipment for underground mines located in the United States and provides tax credits for certain mine rescue team training programs, effective for three years through 2008.

**Certain provisions made permanent:**

A number of provisions that were enacted on a temporary basis by the Tax Increase Prevention and Reconciliation Act of 2005 are made permanent, including:

- ◆ The provision treating environmental cleanup settlement funds as governmentally-owned (i.e., not subject to tax) if certain standards and requirements are met
- ◆ The provision simplifying the application of the active trade or business test to certain corporate distributions by applying this test on an affiliated group basis
- ◆ The provision providing capital gains treatment for self-created musical works when these works are sold by the artist.

Please keep in mind that this letter has only described the highlights of the new law. If you would like more details on any aspect of this legislation, please call your Keiter Stephens principal at your earliest convenience.

Sincerely,

Keiter, Stephens, Hurst, Gary & Shreaves, P.C.