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# House Tax Package Slashes Needed Tax Relief to Small Businesses

## *Executive Summary*

- The onset of the 110th Congress, with Democrats newly in control, promised House and Senate consideration of a minimum wage bill. Faced with an increase in the minimum wage, the Senate Finance Committee constructed a bipartisan tax relief package to offset the impact to small businesses. The total package, fully offset, provided over $8 billion in needed relief to small businesses. The combined package, H.R. 2, passed the Senate on February 1, 2007 by a vote of 94 - 3.

- Originally, the House passed a stand-alone minimum wage bill on January 10, 2007, by a vote of 315 - 116. Only after the Senate passed its combined package did the House pass its own small business package, H.R. 976, on February 16, 2007, by a vote of 360 - 45.
  - Unfortunately, however, H.R. 976 provides only $1.3 billion in relief, hardly the help small businesses need and deserve to offset the additional costs of the mandatory wage increase.

- Economic growth can only be sustained if government-imposed costs are permitted to be offset. And that is what the Senate-passed bill does: it targets all of the tax relief to small businesses — the segment of our economy that will be most affected by the mandatory increased minimum wage.

- Targeted tax breaks will encourage <u>new</u> job growth, a practice that Congress must proactively support.

- Small businesses are the backbone of our economy and Congress must encourage their economic growth. Provisions *left out* of the House package, but essential to small businesses include:
  - Depreciation for Qualified Leasehold Improvements, Qualified Restaurant Improvements and New Restaurant Buildings;
  - Depreciation for Qualified Retail Improvement Property; and
  - Cash Accounting for Small Businesses.

- The Senate should insist on providing a robust relief package to affected businesses.

*If the Senate bill is peanuts, the House bill is a peanut shell. The House package is puny. I hope to see a final tax relief package that's much closer to the size of the Senate bill. We can reach some compromises, and we can get a minimum wage increase of $2.10. We can get a lot of tax loopholes filled. We can bring in more revenue, and we can help small businesses that sometimes are hurt by an increase in the minimum wage. So everybody win, win, wins.*

— Senator Charles Grassley, Ranking Member,
Senate Finance Committee, February 16, 2007

## Introduction

The onset of the 110th Congress, with Democrats newly in control, promised House and Senate consideration of a minimum wage bill. Faced with an increase in the minimum wage, the Senate Finance Committee constructed a bipartisan tax relief package to offset the impact to small businesses. The total package, fully offset, provided over $8 billion in needed relief to small businesses. The combined package, H.R. 2, passed the Senate on February 1, 2007 by a vote of 94 - 3.

Even though the Senate recognized the need for a strong small business tax package to accompany the minimum wage increase, the majority party in the House did not share the sentiment. Originally, the House passed a stand-alone minimum wage bill on January 10, 2007, by a vote of 315 - 116. Only after the Senate passed its combined package did the House pass its own small business package, H.R. 976, on February 16, 2007, by a vote of 360 - 45. Unfortunately, however, H.R. 976 provides only $1.3 billion in relief, hardly the help small businesses need and deserve to offset the additional costs of the mandatory wage increase.

Targeted tax breaks will encourage new job growth, a practice that Congress must proactively support. The economic course over the past three plus years has been strong, and Congress would do well not to disrupt it. The tax relief provided in the Senate-passed bill underscores Congress' support for job creation in that it provides small businesses with the tools and relief they need to not only absorb a minimum wage increase, but to also promote job creation.

Small businesses are relying on Congress' help and Congress should not let them down by passing an inadequate package. The Senate should insist on providing a robust relief package to affected businesses.

The following chart compares the provisions contained in both the House-passed and Senate-passed small business tax relief packages.

## Comparison of House and Senate Package

| Provision | Senate (H.R. 2) | House (H.R. 976) |
|---|---|---|
| Extension of Increased Expensing for Small Businesses | Provides a one-year extension of small business expensing. The $112,000 expense limit and the $450,000 phase-out threshold remain. | Provides a one-year extension of small business expensing with an increase from $112,000 to $125,000 (indexed for inflation). The phase-out threshold is increased from $450,000 to $500,000. |
| Fifteen-Year Straight-Line Cost Recovery for Qualified Leasehold Improvements | Included. | No provision. |
| Fifteen-Year Straight-Line Cost Recovery for Qualified Restaurant Improvements | Included. | No provision. |
| Fifteen-Year Straight-Line Cost Recovery for Qualified New Restaurant Buildings | Included. | No provision. |
| Fifteen-Year Straight-Line Cost Recovery for Qualified Retail Improvement Property | Included. | No provision. |
| Expansion of Eligibility for Cash Method Accounting | Included. | No provision. |
| Subchapter S Provisions to Modernize Rules and Eliminate Undue Restrictions on S Corporations | Included. | No provision. |
| Treatment of Professional Employer Organizations as Employers for Employment Tax Purposes | Included. | No provision. |
| Enhancement of the Tip Credit for Certain Small Businesses | No provision. | Included. |
| Family Business Tax Simplification | No provision. | Included. |

## Why Small Businesses Need a Robust Tax Package

Due to Republican pro-growth policies, the U.S. economy is on a course that Congress should seek to keep on track: 3.4 percent annualized real GDP growth so far this year, 14 straight quarters of positive capital investment, tax receipts up 11.8 percent in fiscal year 2006 (FY06), and labor productivity growth of more than 3 percent over the past five years.

Such growth can only be sustained if government-imposed costs are permitted to be offset. And that is what the Senate-passed bill does: it targets all of the tax relief to small businesses — the segment of our economy that will be most negatively affected by the mandatory increased wage. In order to compensate for this accommodation to employees, small businesses must be able to offset their increased costs with targeted tax benefits.

Targeted tax breaks will encourage new job growth, a practice that Congress must proactively support. The economic course over the past three plus years has been strong, and Congress would do well not to disrupt it. Since August 2003, more than 7.4 million jobs have been created, more jobs than the European Union and Japan *combined*. In the past three months, there have been 513,000 net new jobs, which is on top of 41 straight months of job growth. In addition, employment has increased in 49 states within the past year.[1]

Small businesses are the backbone of our economy and Congress must encourage their economic growth:

- small firms represent 99.7 percent of all employer firms
- small firms employ half of all private sector employees
- small firms have generated 60 to 80 percent of net new jobs annually over the last decade
- small firms create more than 50 percent of non-farm private gross domestic product (GDP)
- small firms employ 41 percent of all high tech workers (such as scientists, engineers, and computer workers).[2]

## Congress Must Provide Robust Relief to Small Businesses

In an attempt to help small businesses to stay competitive and keep our economy growing, the final small business tax package Congress passes must be sufficient to mitigate the burden imposed on small businesses by the mandatory wage increase. Businesses can only create jobs when they are growing, and one of the most effective ways to encourage business growth is to reduce the cost of new business investment by allowing businesses to write off the investments immediately or to depreciate investment costs more rapidly. Below are provisions *left out* of the House package, but essential to small businesses:

- **Depreciation for Qualified Leasehold Improvements, Qualified Restaurant Improvements and New Restaurant Buildings:** Allow 15-year recovery period for

[1] http://www.whitehouse.gov/infocus/economy/.
[2] http://www.sba.gov/advo/stats/sbfaq.pdf.

qualified leasehold improvement property, qualified restaurant improvements, and new restaurant buildings.

- The restaurant industry is the largest U.S. employer, after the government; nearly one-third of Americans get their first job in a restaurant.[3] While such entry-level job opportunities could be reduced if the minimum wage is increased, Congress can encourage the creation of new restaurant jobs by making it more cost-effective to operate a restaurant.
- The present-law 39-year recovery period is an unfair penalty. Taxpayers should not be required to recover the costs of certain improvements beyond the useful life of the investment.
- Restaurants experience considerably more traffic and remain open longer than most commercial buildings, and such daily use causes rapid deterioration and forces restaurateurs to constantly repair and upgrade their facilities. Thus, restaurants have a shorter lifespan than other commercial establishments.[4]
- The accelerated depreciation will encourage more new restaurants to be built, which will increase restaurant employment opportunities.

- **Depreciation for Qualified Retail Improvement Property:** Allow 15-year recovery period for qualified retail improvements.
  - The present-law 39-year recovery period is an unfair penalty. Taxpayers should not be required to recover the costs of certain improvements beyond the useful life of the investment.
  - It is unfair to treat retailers differently based on whether the building in which they operate is owned or leased. Many small businesses own the building in which they operate their business, so the provision provides similar treatment between leasehold and retail improvements.[5]

- **Cash Accounting for Small Businesses:** Allow the cash-basis accounting method to be an option for small businesses with gross revenues up to $10 million, regardless of inventories.
  - Allowing cash-basis accounting will reduce administrative costs for small businesses and increase simplicity.

## Conclusion

Senate Republicans must hold steadfast in their commitment to helping small businesses cope with a minimum wage increase. Only a comprehensive relief package will give the small businesses the help they need to counter any adverse effects of a minimum wage increase. The Senate should not falter in their commitment to providing a robust relief package and should work for a compromise that reflects such commitment.

[3] "Restaurant Industry Facts," available at www.restaurant.org/research/ind_glance.cfm.
[4] Senate Finance Committee Report, found at http://www.senate.gov/~finance/press/Bpress/2007press/prb012207leg.pdf.
[5] *Id.*