




THE UNITED STATES CONFERENCE OF MAYORS

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TO: All Mayors

FROM: Tom Cochran 
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SUBJECT: Key Tax Provisions in the American Recovery Conference Agreement: Report # 2

Today President Barack Obama signed into law the American Recovery and Reinvestment Act of 2009 (ARRA). The new law, which includes \$301 billion in tax cuts, will provide tax relief to individuals and businesses; and help make credit more accessible to local governments.

The following is a summary of some of the key tax provisions of interest to Mayors:

RECOVERY FOR STATE AND LOCAL GOVERNMENTS

- **Deductions for Financial Institution Investments in Municipal Bonds:** Under current law, financial institutions are not able to deduct the carrying costs associated with purchasing municipal bonds. To make municipal bonds more attractive to financial institutions in 2009 and 2010, the new law will allow financial institutions to deduct 80 percent of the carrying costs associated with purchasing municipal bonds up to two percent of the institutions total assets. (Estimated Cost: see next item).
- **Small Issuer Exception:** Since 1986 banks have been able to deduct the carrying costs of bonds purchased from small issuers who do not expect to issue more than \$10 million in bonds annually. ARRA will increase the dollar threshold from \$10 million to \$30 million in 2009 and 2010. (Estimated Cost: \$3.234 billion for both items above over 10 years).
- **Exclusion of Tax-Exempt Bonds From the Alternative Minimum Tax:** Will exclude tax-exempt private activity bonds from the Alternative Minimum Tax in 2009 and 2010. Again, this will make these bonds more attractive to investors. (Estimated Cost: \$555 million over 10 years).
- **New School Construction Bonds:** Will create a new category of bonds to assist state and local governments with the construction and rehabilitation of schools or the acquisition of land to build public schools. (Estimated Cost: \$9.877 billion over 10 years).

- **Tax Credit Bond Option:** Will provide state and local governments the option of issuing a tax credit bond instead of a tax-exempt governmental bond in 2009 and 2010. Both tax credit bonds and tax-exempt bonds provide a subsidy to municipalities by reducing the cash interest payments a local government must pay on its debt. Tax credit bonds differ in two ways: the interest paid is taxable and a portion of the interest paid on tax credit bonds takes the form of a federal tax credit. (Estimated Cost: \$4.348 billion over 10 years).
- **Three Percent Withholding Requirement:** Will delay for one year (until January 1, 2012) the application of a federal mandate requiring state and local governments to withhold three percent of most payments made to contractors providing property and services. This applies to governments that spend more than \$100 million annually. (Estimated Cost: \$291 million over 10 years).
- **Qualified Zone Academy Bonds (QZAB):** Will allow an additional \$1.4 billion of QZAB issuing authority to state and local governments in 2009 and 2010 qualified. Bonds could be used to finance renovations, equipment purchases, development of course material, and training teachers and personnel at qualified schools. (Estimated Cost: \$1.045 billion over 10 years).

RECOVERY FOR INDIVIDUALS

- **Making Work Pay Tax Credit:** Will provide a refundable tax credit up to \$400 for individuals with an adjusted gross annual income of \$75,000, and up to \$800 for couples with an adjusted gross annual income of \$150,000. (Estimated Cost: \$116.199 billion over 10 years).
- **Earned Income Tax Credit:** Will increase the earned income tax credit from 40 percent of an eligible family's first \$12,570 in annual earnings to 45 percent of an eligible family's first \$12,570 in annual earnings. (Estimated Cost: \$4.663 billion over 10 years).
- **Child Tax Credit:** Will increase eligibility for the refundable Child Tax Credit in 2009 and 2010. For 2008 the Child Tax Credit is refundable to the extent of 15 percent of the taxpayer's earned income in excess of \$8,500. The new law will reduce the floor in 2009 and 2010 to \$3,000. (Estimated Cost: \$14.830 billion over 10 years).
- **Education Tax Credit:** For 2009 and 2010 the new law will provide taxpayers a new "American Opportunity" tax credit up to \$2,500 for the cost of tuition and related expenses at a college or university. (Estimated Cost: \$13.907 billion over 10 years).
- **First-Time Home Buyer Tax Credit:** Last year Congress provided a refundable tax credit up to \$7,500 for first-time home buyers. Taxpayers receiving this credit are required to pay back any amount received under this provision over 15 years. The new law eliminates the repayment obligation for taxpayers purchasing homes after January 1, 2009 and increases the maximum credit to \$8,000. (Estimated Cost: \$6.638 billion over 10 years).
- **Sale Tax Deductions for Vehicle Purchase:** Will provide taxpayers a deduction for state and local sales taxes paid on the purchase of new cars, light trucks, recreational vehicles, and motorcycles through 2009. (Estimated Cost: \$1.684 billion over 10 years).

REINVESTMENT IN RENEWABLE ENERGY

- **Clean Renewable Energy Bonds:** Will authorize an additional \$1.6 billion of clean renewable energy bonds to finance facilities that generate electricity from wind, closed-loop biomass, open loop biomass, geothermal, small irrigation hydropower, landfill gas, marine renewable and trash combustion facilities. Bond authorization will be subdivided: 1/3 to qualifying states and local governments; 1/3 to qualifying projects of public power providers; and 1/3 to qualifying projects of electric cooperatives. (Estimated Cost: \$578 million over 10 years).
- **Conservation Bonds:** Will authorize an additional \$2.4 billion of qualified energy conservation bonds to finance state, municipal and tribal government programs and initiatives designed to reduce greenhouse gas emissions. (Estimated Cost: \$803 million over 10 years).
- **Long-Term Extension and Modification of Renewable Energy Tax Credit:** Will extend the placed-in-service date for wind facilities for three years (through December 31, 2012). Will also extend the placed-in-service date for three years (through December 31, 2013) for certain other qualifying facilities including: hydropower, landfill gas, and waste to energy. (Estimated Cost: \$13.143 billion over 10 years).

ECONOMIC RECOVERY TOOLS

- **Recovery Zone Bonds:** Will create a new category of tax credit bonds for investment in economic recovery zones. Will authorize \$10 billion in recovery zone economic development bonds and \$15 billion recovery zone facility bonds which could be issued in 2009 and 2010. Each state will receive a minimum (1% of total) amount of bonds and a share of the national allocation based on its relative share of job losses in 2008. These allocations will be sub-allocated to municipalities that will be permitted to use the bonds to invest in infrastructure, job training, education and economic development in areas of significant poverty, unemployment or home foreclosures. (Estimated Cost: \$5.371 billion over 10 years).
- **New Markets Tax Credit:** Under current law, there are \$ 3.5 billion of New Markets Tax Credits (NMTC) available for each of 2008 and 2009. The new law increases the available credits for 2008 to \$5 billion and the available credits for 2009 to \$5 billion. (Estimated Cost: \$815 million over 10 years).

TAX INCENTIVES FOR SMALL BUSINESSES

- **Extension of Enhanced Small Business Expensing:** To help small businesses recover the cost of certain capital expenses, small businesses will be allowed to write-off the cost of these expenses in the year they are purchased instead of recovering the costs through depreciation over time. Until the end of 2010, small business tax payers will be allowed to write-off up to \$125,000 (indexed for inflation) of capital expenditures, which will be subject to a phase-out once capital expenditures exceed \$500,000 (indexed for inflation). In 2008, the write-off amount was increased to \$250,000 subject to phase-out starting at \$800,000. The new law extends the temporary increases for capital expenditures incurred in 2009. (Estimated Cost: \$41 million over 10 years).

- **Five-year Carryback of Net Operating Losses for Small Businesses:** Under current law, net operating losses (“NOLs”) may be carried back to the two taxable years before the year that the loss arises (the “NOL carryback period”) and carried forward to each of the succeeding twenty taxable years after the year that the loss arises. For 2008, the bill extends the maximum NOL carryback period from two years to five years for small businesses with gross receipts of \$15 million or less. (Estimated Cost: \$947 million over 10 years).
- **Small Business Capital Gains:** The new law allows a 75 percent exclusion for individuals on the gain from the sale of certain small business stock held for more than five years. This change is for stock issued after the date of enactment and before January 1, 2011. (Estimated Cost: \$829 million over 10 years).