

Sen. John Thune's Investment in New Ventures and Economic Success Today (INVEST) Act of 2017

Section by Section Summary

Title I – Start-up and Organizational Expenses

Section 101 – Expansion of the deduction for start-up and organizational expenses: The bill would consolidate the three separate provisions under current law relating to the deductibility of start-up and organizational expenses into a single unified section that applies to all business types. Start-up and organizational expenses include costs to investigate, create, or otherwise begin or acquire a business prior to the business actually commencing operation as well as costs such as legal or accounting expenses relating to the formation of a corporation, partnership or limited liability company (LLC). The bill would increase the amount of these expenses that can be deducted immediately from the current \$5,000 to \$50,000 and increase the phase-out from the current \$50,000 to \$100,000 for expenses in excess of the expensing limit. Expenses that are not immediately deductible would be recovered over a 10-year period, rather the 15-year period under current law. All dollar thresholds would be indexed for inflation.

Title II – Accounting Methods

Section 201 – Cash method of accounting for small corporations and certain partnerships: The bill would increase to \$15 million the threshold for small corporations and partnerships with a corporate partner to qualify for the cash method of accounting. The cash method generally allows a business to recognize income and deduct expenses when the cash is received or paid, rather than having to accrue income and expenses. Under current law, these types of businesses may only use the cash method if they have average gross receipts of \$5 million or less during the preceding three years. Businesses structured as sole proprietors, partnerships (with non-corporate partners), LLCs, and S corporations generally may use the cash method regardless of the amount of their gross receipts. Farm corporations and farm partnerships with a corporate partner may only use the cash method if their gross receipts do not exceed \$1 million in any year. An exception allows certain family farm corporations to qualify if their gross receipts do not exceed \$25 million. The bill would increase the general farm corporation limit to \$15 million, but not reduce the limit for family farm corporations.

Section 202 – Expensing of inventory by small and mid-sized businesses: The bill would permit businesses that sell materials or products to deduct the cost of such inventory immediately, rather than having to employ an inventory accounting method as required under current law (e.g., specific identification, first-in-first-out, or last-in-first-out method). Under current law, businesses that are required to use an inventory method also must use the accrual method of accounting for tax purposes (except for certain small businesses with average gross receipts of not more than \$1 million). This provision would interact with the changes to the cash-method rules to permit any business with average annual gross receipts of \$15 million or less to use the cash method even if business has inventories.

Section 203 – Exception for small and mid-sized businesses from capitalization of certain costs to inventory: The bill would provide a comprehensive exemption from the uniform capitalization rules (UNICAP) for businesses meeting the \$15 million threshold proposed for the cash method of accounting described above. The UNICAP rules generally require a business to capitalize the direct and indirect costs associated with inventory and recover such costs when the inventory is sold, rather than when the costs are incurred. The UNICAP rules are complex and can have a significant accounting burden on businesses, especially smaller businesses. Under current law, a business with average gross receipts of \$10 million or less in the preceding three years is not subject to the UNICAP rules for personal property acquired for resale. The exemption does not apply to real property (e.g., buildings) or personal property that is manufactured by the business. The bill would expand the exemption to apply to real or personal property acquired or manufactured by the business, provided it meets the \$15 million threshold.

Section 204 – Increased exception for completed contract method: The provision would increase the threshold to \$15 million for the completed-contract method, which is used primarily to account for small construction contracts. Under current law, construction companies with average annual gross receipts of \$10 million or less in the preceding three years are permitted to deduct costs associated with construction when they are paid and recognize income when the building is completed. Other businesses generally are required to account for longer-term contracts under the percentage-of-completion method, which allows for deductions and income recognition each year based on the percentage of the contract completed. The completed-contract method is a simpler accounting method and more closely aligns with the cash method of accounting.

Title III – Expensing and Cost Recovery

Section 301 – Section 179 expensing: The bill would expand the applicability of Section 179 by allowing smaller businesses to expense the cost of property and equipment as well as building improvements up to \$2 million per year with the benefit phased out dollar-for-dollar beginning at \$3 million (i.e., a business would no longer qualify for Section 179 expensing if it invested more than \$5 million in a year). Under current law, businesses may expense up to \$510,000 (for 2017) and the benefit is phased out when the business invests more than \$2.54 million (for 2017).

The provision would also streamline the Section 179 rules that apply to expensing of costs relating to buildings. First, it would consolidate the current rules for leasehold improvements, retail improvements, and restaurant property into a general “improvement property” concept, which was adopted for the bonus-depreciation rules under the PATH Act. This concept generally would allow costs associated with improving a building (e.g., refurbishing restrooms, remodeling restaurant seating areas, modernizing grocery store display aisles and refrigerated cases) to be expensed within the Section 179 limits regardless of whether the property is leased or owned and without regard to the particular industry of the business. Second, the bill would allow businesses to expense other costs associated with a building, including roofs, heating, ventilation and air-conditioning systems, fire protection and alarm systems, and security systems. Under current law, these costs of improving a building must be capitalized and depreciated over the 39-year depreciation life of the building. The bill would also permit the cost of property used in rental real estate (e.g., appliances, furnishings) to be expensed within the Section 179 limits.

Section 311 – 50-percent general cost recovery: The bill would make permanent the current temporary rule that allows businesses to elect to expense 50-percent of the cost of certain property and recover the remaining cost under the current depreciation rules. This change would allow a business of any size to recover half of the cost of new investments in qualifying property in the year that the property is placed in service, with the resulting tax savings available to reinvest in the business. Permanent 50-percent expensing is also important for smaller businesses that qualify for Section 179 because a business may only expense costs under Section 179 to

the extent of its income for the year. Thus, 50-percent expensing under the depreciation rules provides additional flexibility and improved cost recovery for smaller businesses as well as larger ones.

Section 312 – Depreciation of farm machinery and equipment: The bill would restore a provision, which expired at the end of 2009, that permitted farmers and ranchers to depreciate most farm machinery and equipment over five years rather than seven years. The bill also would repeal the rule under current law that requires property used in a farm business to be depreciated more slowly than in other industries. These changes would better align the depreciation rules with the economic useful life of farm machinery and equipment and provide consistent treatment for agricultural businesses under the tax code.

Section 313 – Updated schedule of depreciable property: Under current law, businesses have had to use a 1987 schedule of property class lives (Revenue Procedure 87-56) to determine the recovery periods that apply. Not surprisingly, there is now a whole range of technology and other types of property that did not exist in 1987 that do not fit squarely within the schedule. The bill would authorize the Treasury Department to work in conjunction with the Commerce Department’s Bureau of Economic Analysis to update the schedule of class lives. Under the bill, the Treasury Department would issue a report to Congress every five years updating the schedule. For the first report, which would be due by the end of 2020, the new recovery periods would become effective in 2022. The bill also would amend the Congressional Review Act to treat the schedule as a major rule, which would give Congress more flexibility to overrule any schedule if necessary.

Section 314 – Depreciation of business vehicles: The bill would modernize the current and outdated depreciation rules for business vehicles to allow a business to recover more of the cost of cars, light trucks, and vans, up to \$50,000 over six years. The bill would also allow a business to take full advantage of 50-percent expensing in the first year that the vehicle is placed in service, up to \$25,000. Under current law, a company that purchases a passenger automobile for business use may only deduct up to \$16,935 of the cost over six years (\$24,935 with temporary 50-percent expensing). Slightly higher limits apply to light trucks and vans. The current limitation does not apply to industrial vehicles (i.e., weighing more than 6,000 pounds), vehicles used for transporting people or products for hire, any ambulance or hearse, or other trucks or vans designated under IRS regulations.

Section 315 – Amortization of costs of acquired intangibles: The bill would reduce the recovery period for intangible property that is acquired by a business. Intangible property includes patents, copyrights, trade names, franchise rights, customer lists, and the goodwill or going-concern value inherent in a business. Currently, the cost of such intangibles must be amortized over 15 years, which the bill would reduce to 10 years.