

State and Federal Tax Issues in a New Market

In addition to the hands-on management issues that arise when a contractor expands into a new market, there are also significant tax questions that must be considered, especially if the expansion crosses state lines. Unfortunately, the tax implications of a move or expansion are easily overlooked until the bill comes due. By then, it's usually too late to factor tax expenses into bids that have already been submitted.

The most obvious tax issue is the variation in state and local income taxes from one jurisdiction to another. Contractors are often blindsided by these, especially if their home market has relatively low corporate income tax rates, and they do not have regular month-to-month contact with their accountant. In addition, there is the question of how the company's net income should be properly apportioned among the various states in which it operates.

S corporations may face additional complications. Some states do not have a state income tax law equivalent to an S corporation, and other states may require a separate state-level S corp election. Failing to anticipate this can lead to sizable unexpected tax obligations.

The last few years have seen continuing changes in federal income tax law, including increases in the amount of capital expense that may be deducted from current year income under IRS Code Section 179, rather than depreciated over time. Moreover, an additional "bonus depreciation" deduction may also be allowed on qualifying property in the year it is placed in service.

Some states match the federal depreciation rules, but others have chosen to "decouple" their tax law from the federal standards because they cannot afford the lost tax revenue. This decoupling can result in a higher than expected state income tax obligation in a new jurisdiction.

If tax issues such as these are not anticipated, they can turn an otherwise promising expansion opportunity into a net loser for the company. Always consult your accountant before taking on any work in a new taxing jurisdiction.

The Construction Advisor is produced quarterly by Bober Markey Fedorovich. For more information about our services, please call or email our team leader Dale A. Ruther, CPA, CIT, partner, at (330) 762-9785 or druther@bobermarkey.com.

Unless expressly stated otherwise, any U.S. tax advice contained in this communication (including attachments) is not intended or written to be used, and cannot be used, by the recipient for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code.

©2010 Bober, Markey, Fedorovich & Company