Sage Fixed Assets
Depreciation Fundamentals

User guide

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Contents

Section IV: Chapter 6: Depreciation of Nonrecovery Property IV-115

Section IV: Chapter 7: Depreciation and the Alternative Minimum Tax (AMT) IV-127

Section IV: Chapter 8: Depreciation and Adjusted Current Earnings (ACE) IV-145

Section IV: Chapter 9: Depreciation and IRS Tax Form 4562 IV-161

Section V: Conclusion V-1

Section V: Depreciation Questions V-5

Section VI: Tables VI-1

Section VII: Quick Reference VII-1

Glossary

Index

Introduction: Features and More Features...

Welcome to **Sage Fixed Assets - Depreciation Fundamentals**! As you are about to see, this guide is the most thorough, practical, and easy to use depreciation reference and training resource ever developed. To assist you in obtaining the maximum benefit from its use you need to be aware of its many features:

- **"How To's"—**In this guide, we will discuss theory so you can understand why something needs to be done, but most important we will tell you how to do it! Look for How To's throughout the entire guide (they are listed in our Index under "How To" for easy reference).
- **Tips—**Watch for these and benefit from our experience. We can help save you tax dollars, save you valuable time, *and* help you make good decisions.
- **Notes—**Our Notes will:
  - Give you additional clarification of the text.
  - Give you additional information and a more in-depth explanation if you want it.
  - Ensure that you will have all the answers. For example, if we tell you something cannot be done, we will also tell you what *can* be done.
- **Timeline—**We have created a concise history of depreciation in an easy-to-read timeline. See "A History of Depreciation," page ix.
- **IRS Code Cites—**Whenever we are discussing a complicated issue we realize you may want to refer to the IRS Code section itself. Also, if something is beyond the scope of this guide (such as "tunnel bores"), we will give you the code cite so you can obtain the information you need.
- **"Depreciation Questions"—**This is an invaluable checklist to ensure that nothing is forgotten or overlooked when depreciating an asset. You'll find it on page V-5.
- **"Quick Reference"—**This is a useful listing of the IRS Code sections and regulations that relate to depreciation. The list is presented two ways: numerically and alphabetically. It starts on page VII-1.
- **Alphabetical Listing of Commonly Used Assets—**We have alphabetized the most commonly used assets: by property type, by manufacturing type, and by business type. This will enable you to quickly determine the depreciable life of any property and save you time, while avoiding all of the mistakes caused by the misclassification of assets. See page VI-4.
- **IRS Tables and How To Use Them—**All of the necessary tables are included in the back of this guide. In addition, we have given you simplified directions on locating the appropriate table quickly and easily:
  - How To Use the MACRS Percentage Tables—See page VI-14.
  - How To Use the ACRS Percentage Tables—See page VI-41.

- How To Use the Tables for Listed Property—See page VI-48.
- **IRS ADR Class Life Table**—See page VI-4.
- **Glossary**—All of the key depreciation terms are found in our Glossary.
- **Index**—Our very detailed Index will assist you in locating all pertinent information about any topic within seconds.

We know you will find this guide to be an invaluable part of your library, both as a reference book and as a useful training manual for your staff.

Preface: Historical Overview

The rules governing **depreciation** over the years have continuously evolved and become more complex. Most of the complexity is the result of legislation passed by Congress and official guidance issued from the Office of Chief Counsel at the Internal Revenue Service (IRS).

Prior to the enactment of the 1954 Internal Revenue Code, the **straight-line** method of depreciation was required to be used for tax purposes. However, much was changed in 1954 when accelerated methods of depreciation were finally sanctioned by the IRS. This also marked the beginning of the keeping of two sets of records for numerous businesses as they began to calculate depreciation by two different methods for the same fixed asset and, of course, needed to keep track of this. Many wished to continue the straight-line depreciation method for financial statement purposes, with the intent of fairly and realistically reflecting the continual deterioration of its fixed assets. At the same time they wanted to take advantage of the larger and quicker deductions for tax purposes by using the accelerated methods of depreciation.

In 1971, another major development occurred when the **Class Life Asset Depreciation Range System** (ADR) was created. Under this system, which lasted until 1981, property acquired in a given year was grouped by the primary activity for which it was used and assigned to a **vintage** account. A separate vintage account is established for each class of property, with a defined depreciation period. The asset classifications of ADR came to the forefront once again with property acquired after 1986.

The Economic Recovery Tax Act of 1981 revolutionized depreciation with the creation of the **Accelerated Cost Recovery System** (ACRS). This new system greatly simplified the depreciation rules with the goal of encouraging capital investment. A new phrase was coined with assets being referred to as "**recovery property**." The concept of useful lives was replaced with the newly created "**recovery periods**," and depreciation was now referred to as "**cost recovery**."

This was followed by the Tax Reform Act of 1986, which introduced a **Modified Accelerated Cost Recovery System** (MACRS). MACRS, along with an **Alternate MACRS Method** (ADS), has incorporated the ADR asset classifications. The recovery periods under both MACRS and ADS are based on the asset's midpoint life under ADR. The provisions of MACRS are not as generous as ACRS. MACRS attempted to more closely match class lives with assets' useful lives, as well as slowing the rate of their cost recovery.

Although there have not been any *major* changes affecting depreciation since the Tax Reform Act of 1986, there have been numerous tax acts passed by Congress that include depreciation-related provisions:

1. **The "Job Creation and Worker Assistance Act of 2002" (JCWAA)**

The JCWAA introduced a 30% first year depreciation deduction and special relief provisions for property in the lower Manhattan area impacted by the terrorist attacks of 9/11/2001.

2. **The "Jobs and Growth Tax Relief Reconciliation Act of 2003" (JGTRRA)**

   The JGTRRA increased the first year depreciation deduction from 30% to 50% and also included a provision to increase the Section 179 annual limit from $25,000 to $100,000, and to increase the Section 179 phase-out threshold from $200,000 to $400,000.

3. **The "Working Families Tax Relief Act of 2004"**

   The Working Families Tax Relief Act eliminated the phaseout limitations for qualified electric vehicles placed in service in 2004 and 2005, allowing taxpayers to claim 100% of the allowable credit, and also eliminated the phaseout for the deduction of qualified clean-fuel vehicle property placed in service in 2004 and 2005, allowing taxpayers to claim 100% of the allowable deduction.

   In addition, the expiration date of the accelerated recovery periods for MACRS Indian Reservation Property was extended through December 31, 2005, and the designation of the DC Enterprise Zone was also extended through December 31, 2005.

4. **The "American Jobs Creation Act of 2004"**

   The American Jobs Creation Act of 2004 extended the increased Section 179 annual limit, indexed for inflation, for an additional two years along with other expensing enhancements but did limit the amount of Section 179 to $25,000 for a Sport Utility Vehicle placed in service after the enactment date.

5. **The "Energy Tax Incentives Act of 2005"**

   The Energy Tax Incentives Act of 2005 extended and created tax credits for the following energy saving property: Solar Energy, Clean Coal Production, Fuel Cell and Microturbine Plants, and Other Energy Property.

   The 2005 Energy Bill also created new Section 179 deductions such as 179C for Qualified Refineries and 179D for Energy Efficient Commercial Buildings. The 2005 Energy bill sunsets Section 179A deductions for clean-fuel vehicles and clean-fuel vehicle refueling property placed in service after 12/31/ 2005, rather than 12/31/ 2006. For vehicles placed in service in 2005, the 2005 Energy Bill introduced new tax credits for the purchase of hybrid, fuel cell, advanced lean burn diesel and other alternative power vehicles.

6. **The "Gulf Opportunity Zone Act of 2005"**

   The Gulf Opportunity Zone Act of 2005 created special economic zones, the Katrina Gulf Opportunity (GO) Zone as well as Rita and Wilma GO Zones in response to widespread devastation due to Hurricanes Katrina, Rita and Wilma. The bill enacted many provisions related to hurricane relief including the following depreciation related legislation: bonus depreciation enacted for rebuilding in the GO Zone, increased Section 179 limits for GO Zone assets and increased Rehabilitation Credits for qualified GO Zone buildings.

7. **The "Tax Increase Prevention and Reconciliation Act of 2005"**

The Tax Increase Prevention and Reconciliation Act of 2005 extended the increased Section 179 expense deduction and phase-out threshold through 2009. Previously, the increased Section 179 expense deduction and phase-out threshold had been scheduled to decrease in tax years beginning in 2008. The bill also enacted a provision to allow taxpayers to elect to treat the sale or exchange of self-created musical compositions or copyrights as the sale or exchange of a capital asset. This bill also allows for expenses paid or incurred in creating or acquiring a musical composition or copyright to musical composition to now be amortized over five years. These provisions apply to property placed in service in tax years beginning after December 31, 2005 and before January 1, 2011. This bill also extended the amortization period of geological and geophysical expenditures to five years for major integrated oil companies. Although, the bill was passed in 2006, it carries a 2005 designation because it was a carryover from last year's budget.

8. The "Tax Relief and Health Care Act of 2006"

The Tax Relief and Health Care Act of 2006 extended the expiration date of the accelerated recovery periods for MACRS Indian Reservation Property. Previously, the accelerated recovery periods for Indian Reservation property had expired on December 31, 2005 but now it has been extended for property placed in service through December 31, 2007. The fifteen year recovery period for Leasehold Improvement and Restaurant Property also was extended to include property placed in service through December 31, 2007. As a result of this bill, certain property placed in service before January 1, 2011 in the GO Zone is now eligible for bonus depreciation. The Section 179D deduction has also been extended for one year for qualifying property placed in service through December 31, 2008. Section 179D property represents property purchased or costs incurred in making commercial building property more energy efficient. This bill also introduces deductions for two specialized types of property. A 50% bonus depreciation deduction for "Cellulosic Biomass Ethanol Plant Property" can be taken for property placed in service before January 1, 2013. And finally a new Section 179E 50% deduction can now be taken for Advanced Mine Safety Equipment placed in service after December 20, 2006 and through December 31, 2008.

9. The "Economic Stimulus Act of 2008"

The Economic Stimuls Act of 2008 nearly doubled the Section 179 expense for tax years beginning in 2008 from $128,000 to $250,000 and reinstituted the 50% bonus depreciation for all areas of this country for qualified property placed in service in 2008 and certain types of property placed in service in 2009.

10. The "Housing Assistance Act of 2008"

Under the Housing Assistance Act of 2008, businesses can elect, for the first tax year ending after March 31, 2008, to treat certain unused research and AMT credits as allowable and refundable in lieu of claiming bonus and accelerated depreciation for eligible qualified property.

11. The "Heartland, Habitat, Harvest, and Horticulture Act of 2008 - Title XV of the Food, Conservation, and Energy Act of 2008"

The Heartland, Habitat, Harvest, and Horticulture Act of 2008 - Title XV of the Food, Conservation, and Energy Act of 2008 (The 2008 Farm Act) classified all racehorses as three-year property for depreciation purposes regardless of their age, if placed in service after 2008 and before 2014. The 2008 Farm Act also provided 50% depreciation allowance for qualified Recovery Assistance property located in the Kansas disaster area, and increased the Section 179 expense and investment cost limits by $100,000 and $600,000 respectively for qualified Recovery Assistance property.

12. The "Emergency Economic Stabilization Act of 2008"

The Emergency Economic Stabilization Act of 2008 (EESA) provided a compilation of tax incentives targeted to businesses, several of which revised as well as extended tax benefits. The EESA extended through 2016 the energy tax credit for solar energy, fuel cell, and microturbine property. New energy tax credits of 10% were added through 2016 for combined heat and power system property and geothermal heat pump systems; and 30% or up to $4,000 through 2016 for small wind energy property. The aggregate credits for qualifying advanced coal projects were expanded to $2,550,000,000, and up to 30% of the qualified investment is allowed for credits. Up to 30% of the qualified investment is also allowed for qualifying gasification project credits.

The EESA extended through 2013 the taxpayer election to expense costs of certain refinery property and the tax credit for energy efficient commercial buildings; through 2009 tax incentives for advanced mine safety equipment.

The EESA included cellulosic biofuel within the definition of biomass ethanol plant property for purposes of the 50% depreciation allowance. It also allowed a 50% depreciation allowance for reuse and recycling property used to collect, distribute, or recycle certain materials, including scrap, fibers, and metals.

The EESA allowed an accelerated 10-year recovery period for the depreciation of qualified smart electric meters and smart electric grid systems. It allowed accelerated depreciation (i.e., five-year recovery period) for certain farming business machinery or equipment placed in service before January 1, 2010. It extended through 2009 accelerated depreciation for qualified leasehold and restaurant improvements and for certain improvements to retail space; accelerated depreciation of business property on Indian reservations and of motorsports racing track facilities; the increased rehabilitation tax credit for property in the Gulf Opportunity (GO) Zone. Rehabilitation credit is allowed through 2011 for qualified property located in the Midwestern Disaster Area.

The EESA allowed 50% depreciation allowance and increased the Section 179 expensing allowance for qualified disaster assistance property. It defined "qualified disaster assistance property" to include nonresidential real or residential rental property in a federally declared disaster area. It also increased Section 179 expense and investment cost limits by $100,000 and $600,000 respectively for qualified disaster assistance property.

13. The "American Recovery and Reinvestment Act of 2009"

The tax provisions under the American Recovery and Reinvestment Act of 2009 include extended bonus depreciation and increased expensing for 2009, an increase in first-year depreciation for passenger cars in the amount of $8,000 through 12/31/2009, expansion of ITC to include a new advanced energy project credit of 30%, elimination of the $4,000 annual limitation on business energy tax credit for qualified small wind energy after 12/31/2008, and an option to either claim an energy tax credit or apply for a grant for specified energy property.

14. **The "Small Business Jobs Act of 2010"**

The Small Business Jobs Act of 2010 increased Section 179 expensing limit from $250,000 to $500,000, and investment limit from $800,000 to $2 million for 2010 and 2011 tax years. Up to $250,000 of Section 179 expense can be taken for qualified real property for 2010 and 2011 tax years. The new law continued to treat off-the-shelf computer software as qualified Section 179 property that is subject to full Section 179 expensing thru 2011 tax years. The new law extended 50% first-year bonus depreciation through December 31, 2010 for qualified property (December 31, 2011 for certain aircraft and property with longer production periods). The limitation under Code Section 280F on the amount of depreciation deductions allowed was increased in the first year by $8,000 for qualified automobiles placed in service in 2010. The new law removed cell phones and similar personal communication devices as listed property. The new law also raised the start-up expense deduction to $10,000 and increased the phaseout threshold to $60,000 for 2010.

15. **The "Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010"**

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (The Act) extends the bonus depreciation provision under Code Section 168(k) and temporarily increases the rate for qualified property acquired and placed in service as follows (note that the definition of qualified property remains the same):

- 1/1/2010 through 9/8/2010: 50%
- 9/9/2010 through 12/31/2010: 100%
- 1/1/2011 through 12/31/2011: 100%
- 1/1/2012 through 12/31/2012: 50%
- For long-production-period property and certain aircraft, the placed-in-service dates are extended one year.

The Act increases Section 179 expensing limit to $139,000, and investment limit to $560,000 for tax years beginning 1/1/2012 through 12/31/2012. Treatment for off-the-shelf computer software as qualified Section 179 property that is subject to full Section 179 expensing is extended through 2012 tax years.

15-year cost recovery period for qualified leasehold improvements, restaurant building and im-provements, and retail improvements is extended through 12/31/2011. Accelerated depreciation for business property on an Indian reservation is extended through 12/31/2011. Seven-year cost recovery period for motorsports entertainment complexes is extended through 12/31/2011.

Advanced mine safety equipment expensing is extended through 12/31/2011. Tax incentives for empowerment zones and investment in the District of Columbia are extended through 12/31/2011.The Act increases rehabilitation credit for historic structures in the Gulf Opportunity Zone (GO Zone) through 12/31/2011.

16. **The "American Taxpayer Relief Act of 2012"**

The American Taxpayer Relief Act of 2012 extends a number of provisions scheduled to expire after 2011:

15-year cost recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements is extended through 12/31/2013.

7-year cost recovery period for motorsports entertainment complexes is extended through 12/31/2013.

Accelerated depreciation for business property on an Indian reservation is extended through 12/31/2013.

Section 179 property expensing deduction of $500,000 is extended through 12/31/2013.

Section 179 investment threshold of $2,000,000 is extended through 12/31/2013.

Treatment for off-the-shelf computer software as qualified Section 179 property that is subject to full Section 179 expensing is extended through 12/31/2013.

Section 179 expensing deduction of $250,000 allowed for qualified real property is extended through 12/31/2013.

Section 179 increased expensing deduction of $35,000 for empowerment zones is extended through 12/31/2013.

Advanced mine safety equipment expensing is extended through 12/31/2013.

50% Bonus for qualified property is extended through 12/31/2013 (or 12/31/2014 for certain property with longer production periods).

50% Bonus for second generation biofuel, which includes cellulosic biofuel plant property is extended through 12/31/2013 (previously 12/31/2012).

17. The "Tax Increase Prevention Act of 2014"

The Tax Increase Prevention Act of 2014 passed by Congress and signed into law in December 2014 retroactively extends a number of provisions that had expired on 12/31/2013:

15-year cost recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements is extended through 12/31/2014.

7-year cost recovery period for motorsports entertainment complexes is extended through 12/31/2014.

Accelerated depreciation for business property on an Indian reservation is extended through 12/31/2014.

Section 179 property expensing deduction of $500,000 is extended through 12/31/2014.

Section 179 investment threshold of $2,000,000 is extended through 12/31/2014.

Treatment for off-the-shelf computer software as qualified Section 179 property that is subject to full Section 179 expensing is extended through 12/31/2014.

Section 179 expensing deduction of $250,000 allowed for qualified real property is extended through 12/31/2014.

Section 179 increased expensing deduction of $35,000 for empowerment zones is extended through 12/31/2014.

Advanced mine safety equipment expensing is extended through 12/31/2014.

50% Bonus for qualified property is extended through 12/31/2014 (or 12/31/2015 for certain property with longer production periods).

50% Bonus for second generation biofuel, which includes cellulosic biofuel plant property is extended through 12/31/2014 (previously 12/31/2013).

18. The “Protecting Americans from Tax Hikes Act of 2015 (PATH Act)”

The PATH Act makes permanent certain tax provisions and retroactively extends other provisions that were set to expire on 12/31/2014:

Section 179 expensing limit of $500,000 and investment threshold of $2,000,000 made permanent, with limits indexed for inflation beginning 2016

Section 179 expensing made permanent for qualified real property; $250,000 cap eliminated beginning 2016.

Section 179 expensing made permanent for off-the shelf computer software.

15-year cost recovery period for qualified leasehold improvements, restaurant buildings and improvements, and retail improvements permanently extended.

50% Bonus extended for qualified property placed in service in 2015-2017

40% Bonus allowed for qualified property placed in service in 2018

30% Bonus allowed for qualified property placed in service in 2019

Seven-year cost recovery period for motorsport entertainment complexes extended through 12/31/2016

Accelerated depreciation for Indian reservation property extended through 12/31/2016

Section 179 increased expensing for empowerment zones extended through 12/31/2016

Advanced mine safety equipment expensing extended through 12/31/2016

19. The "Tax Cuts and Jobs Act of 2017"

The "Tax Cuts and Jobs Act of 2017" introduces increased limits for first year expensing, broadens the definition of qualified improvement property, repeals Corporate AMT, limits like-kind exchange treatment to real property, and makes changes to many other depreciation related areas.

Section 168 Allowance increased to 100% expensing for qualifying property, starting 9/28/2017. In general, for qualified property acquired after 9/27/2017 and placed in service by 12/31/2022, the 50% bonus rate is increased to 100%, and then phased-out over the following years.

Section 179 expensing increased to $1,000,000 per year and the investment threshold increases to $2,500,000 starting in 2018. The 2017 expensing limit remains at $510,00 with the investment threshold at $2,030,000.

Changes definition of "qualified real property" for Section 179 expensing to:

any qualified improvement property described in section 168(e)(6) and any of the following improvements to non-residential real property:

- Roofs

- Heating, ventilation, and air-conditioning property
- Fire protection and alarm systems
- Security systems

The exclusion from expensing for property used in connecting with lodging facilities, such as residential rental property, is eliminated.

Yearly automobile depreciation caps almost tripled for vehicles placed in service after December 31, 2017:

Tax Year 1..............$10,000 ($18,000 if bonus depreciation claimed)

Tax Year 2..............$16,000

Tax Year 3..............$9,600

Tax Years 4 + ...$5,760

The first-year bonus increase is lower if 50%, 40% or 30% bonus is required. A lower rate is required if the vehicle is acquired pre-9/28/2017.

The caps will be indexed for inflation after 2018.

The Alternative Minimum Tax (AMT) was repealed by the Tax Cuts and Jobs Act of 2017 for corporations, effective for tax years beginning January 1, 2018 and later. AMT is still in effect for individuals.

Eliminated the 15-year qualified leasehold, retail, and restaurant improvement property classes.

Expanded the definition of qualified improvement property and assigned a 15-year recovery period (assuming a technical correction is made).

A decrease in the 7-year recovery period for new farming machinery and equipment to 5 years, and elimination of the rule requiring use of the 150-percent-declining balance method on property used in a farming business (thus 200% DB can be used).

Like-kind exchange treatment is no longer allowed for depreciable tangible personal property, and intangible and non-depreciable personal property Effective for disposals/exchanges after 2017 (with limited transition exceptions).

Like-kind exchanges are limited to real property. Thus, as under current law, no gain or loss is recognized on the exchange of real property held for productive use in a trade or business or for investment if that real property is exchanged solely for real property of like kind that will be held either for productive use in a trade or business or for investment.

This guide incorporates these tax legislations and all IRS official guidance issued related to these acts.

A History of Depreciation

Year	Depreciation-Related Events
Pre-1954	Straight-Line depreciation.
1954	Enactment of **1954 Internal Revenue Code** allows accelerated depreciation (such as 200% declining-balance and sum-of-the-years'-digits methods).
1962	The **1962 Revenue Act** changes the treatment of gain on the sale of depreciable personal property. It requires all such gain to be treated as ordinary income to the extent of depreciation taken.
1971	Creation of the **Class Life Asset Depreciation Range System** (ADR), which begins to standardize depreciable lives.
1981	> **ACRS, Accelerated Cost Recovery System**. > **Section 179 Expense Deduction** - $5,000 maximum. > **Economic Recovery Act of 1981**.
1984	> **Listed Property** is created. > **Luxury Automobiles** have depreciation "ceilings." > The recovery period of **ACRS real property** is lengthened. > **Tax Reform Act of 1984**.
1986	> **Investment Tax Credit** is repealed. > **Tax Reform of 1986**.
1987	> **MACRS, Modified Accelerated Cost Recovery System**. > **Section 179 Expense Deduction** increased to $10,000.
1989	> **Listed Property definition** extended to include cellular phones and similar telecommunications equipment. > **Revenue Reconciliation Act of 1989**.
1990	> **ACE Adjustment** is created.
1993	> **Section 179 Expense Deduction** increased to $17,500. > Recovery period for **nonresidential real property** increased to 39 years. > **Amortization of goodwill** allowed. > **Code Section 197 intangibles** and standardized amortization periods. > **ACE Depreciation Adjustment** eliminated for property placed in service after 12/31/1993. > Shorter depreciation lives for **Indian Reservation Property**. > **Revenue Reconciliation Act of 1993.** > **Omnibus Budget Reconciliation Act of 1993**.
1996	> **Section 179 Expense Deduction** begins a phased-in increases to $25,000 ($18,000 allowed in 1997). > **Small Business Job Protection Act of 1996**.
1997	> **Small business corporations** are exempt from AMT beginning after 12/31/1997. > **Taxpayer Relief Act of 1997**.
2002	> **30% Depreciation Allowance**. > **Job Creation and Worker Assistance Act of 2002**.

Year	Depreciation-Related Events
2003	> **50% Depreciation Allowance**. > Section 179 Expense Deduction increased to $100,000. > Section 179 Phase-out Threshold increased to $400,000. > **Jobs and Growth Tax Relief Reconciliation Act of 2003**.
2004	> Shorter depreciation lives for **Indian Reservation Property** is extended. > **Working Families Tax Relief Act of 2004**. > Section 179 Expense Increased Deduction extended through 2007. > Sport Utility Vehicles limited to $25,000 of Section 179 Expense after 10/22/2004. > **American Jobs Creation Act of 2004**.
2005	> Existing energy credits extended and new energy credits created. > Additional Section 179 deductions for energy saving property and processes. > **Energy Tax Incentives Act of 2005**. > Bonus depreciation enacted for rebuilding in the GO Zone. > Existing Section 179 increased by the lesser of $100,000 or the cost of qualified Go Zone property. > Rehabilitation Credit increased from 20% to 26% for a certified historic structure and from 10% to 13% for a pre-1936 building. > **Gulf Opportunity Zone Act of 2005**.
2006	> Increased Section 179 expense deduction and phase-out threshold extended through 2009. > **Tax Increase Prevention and Reconciliation Act of 2005**. > Shorter depreciation lives for **Indian Reservation Property** is extended through 2007. > Fifteen year recovery period for **Leasehold Improvement and Restaurant Property** is extended through 2007. > 50% Bonus Depreciation allowed for **certain GO Zone Property** through 2010. > Section 179D expense deduction extended through 2008. > 50% Bonus Depreciation allowed for **Cellulosic Biomass Ethanol Plant Property** through 2012. > New Section 179E expense deduction allowed for **Advanced Mine Safety Equipment** placed in service after the date of enactment of the bill and through 2008. > **Tax Relief and Health Care Act of 2006**.

Year	Depreciation-Related Events
2008	> **Economic Stimulus Act of 2008**. > Section 179 Expense Deduction increased to $250,000 for 2008 tax years. > Section 179 Phase-out Threshold increased to $800,000. > Return of 50% bonus depreciation for qualified property placed in service in 2008 and certain property placed in service through 2009. > **Housing Assistance Act of 2008**. > Election to treat research & AMT credits as allowable and refundable instead of claiming the 50% depreciation allowance. > **The 2008 Farm Act.** > Three-year property for all racehorses PIS after 2008 and before 2014. > 50% depreciation allowance for Kansas Disaster Zone. > Section 179 expense and cost limits increased for Kansas Disaster Zone. > **Emergency Economic Stabilization Act of 200**8. > 50% depreciation allowance for Qualified Disaster Zone. > Section 179 expense and cost limits increased for Qualified Disaster Zone. > Various energy tax credits extended. > Section 179C, 179D, & 179E extended. > Indian Reservation termination date extended through 12/31/2009. > Accelerated depreciation for qualified leasehold, restaurant, & retail space improvements extended through 12/31/2009. > 10-year recovery period for smart electric meters and smart electric grid systems. > Five-year recovery period for certain farming business machinery or equipment.
2009	> **American Recovery and Reinvestment Act of 2009**. > 50% Depreciation allowance and Section 179 increased expensing. > New advanced energy project credit. > Removal of $4,000 annual credit limit for qualified small wind energy. > Grants in lieu of energy credits or electricity production credits.
2010	> **Small Business Jobs Act of 2010.** > 50% depreciation allowance and Section 179 increased expensing limit. > New Section 179 expensing limit for qualified real property. > Off-the-shelf computer software considered qualified Section 179 property. > $8,000 increase in depreciation deduction in first year for qualified autos. > **Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.** > 100% depreciation allowance. > 15-year cost recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements. > Indian Reservation extended. > Seven-year cost recovery period for motorsport entertainment complexes. > Advanced mine safety equipment expensing. > Section 179 increased expensing for empowerment zones extended. > Rehabilitation credit extended.

Year	Depreciation-Related Events
2011	> **Small Business Jobs Act of 2010.** > Section 179 increased expensing limit. > New Section 179 expensing limit for qualified real property. > Off-the-shelf computer software considered qualified Section 179 property. > **Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.** > 100% depreciation allowance. > 15-year cost recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements. > Indian Reservation extended. > Seven-year cost recovery period for motorsport entertainment complexes. > Advanced mine safety equipment expensing. > Section 179 increased expensing for empowerment zones extended. > Rehabilitation credit extended.
2012	> **Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.** > 50% depreciation allowance. > Section 179 increased expensing. > Off-the-shelf computer software considered qualified Section 179 property.
2013	> **American Taxpayer Relief Act of 2012.** > 15-year cost recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements extended. > Seven- year cost recovery period for motorsport entertainment complexes extended. > Accelerated depreciation for Indian reservation property extended. > Section 179 increased expensing limit of $500,000 extended. > Section 179 expensing deduction for real property extended. > Off-the-shelf computer software considered qualified Section 179 property. > Section 179 increased expensing for empowerment zones extended. > Advanced mine safety equipment expensing extended. > 50% Depreciation allowance extended.
2014	> **Tax Increase Prevention Act of 2014.** > 15-year cost recovery period for qualified leasehold improvements, restaurant building and improvements, and retail improvements extended. > Seven- year cost recovery period for motorsport entertainment complexes extended. > Accelerated depreciation for Indian reservation property extended. > Section 179 increased expensing limit of $500,000 extended. > Section 179 expensing deduction for real property extended. > Off-the-shelf computer software considered qualified Section 179 property. > Section 179 increased expensing for empowerment zones extended. > Advanced mine safety equipment expensing extended. > 50% Depreciation allowance extended. > $8,000 increase in depreciation deduction in first year for qualified autos and trucks extended.

Year	Depreciation-Related Events
2015	> **Protecting Americans from Tax Hikes Act of 2015** > Section 179 expensing limit of $500,000 permanently extended, with limit indexed for inflation. > Section 179 expensing of qualified real property and off-the-shelf computer software permanently extended. > 15-year cost recovery period for qualified leasehold improvements, restaurant property, and retail improvements permanently extended. > 50% Depreciation allowance extended for 2015-2017; allowance phases down to 40% in 2018; and 30% in 2019. >$8,000 increase in depreciation deduction in first year for qualified autos and trucks extended for 2015-2017, $6,400 increase in 2018, $4,800 increase in 2019. > Seven-year cost recovery period for motorsport entertainment complexes extended > Accelerated depreciation for Indian reservation property extended. > Section 179 increased expensing for empowerment zones extended. > Advanced mine safety equipment expensing extended.
2017	> **Tax Cuts and Jobs Act of 2017** > Section 179 limit increased to $1,000,000 in 2018. > Section 179 phase-out increases to $2,500,000 in 2018. > Section 179 limits and phase-out will be indexed for inflation after 2018. > Section 168 Allowance 100% reinstated after 9/27/2017 and before 12/31/2022. The allowance of 100% is then phased-out over the following years. > Yearly automobile depreciation caps almost tripled for vehicles placed in service after December 31, 2017. > Corporate AMT is eliminated after effective for tax years beginning January 1, 2018 and later. AMT is still in effect for individuals. > 15-year qualified leasehold, retail, and restaurant improvement property classes are eliminated after December 31, 2017. > The definition of qualified improvement property is expanded and assigned a 15-year recovery period (assuming a technical correction is made). > Like-kind exchange treatment is no longer allowed for depreciable tangible personal property after 12/31 2017 with some exceptions. > 7-year recovery period for new farming machinery and equipment decreased to 5 years after 12/31/2017. > Rule requiring use of the 150-percent-declining balance method on property used in a farming business has been eliminated as of 12/31/2017.

Section I: Fundamentals of Depreciation

In his section:

"Wear and tear from use . . . deterioration and decay . . . allowance for obsolescence . . . gradual decline in value . . ."

Depreciation has many different meanings, depending on the user. For tax and accounting purposes, depreciation is a process of allocation. It is necessary to match deductions with income. When a business acquires equipment or machinery, it does so with the purpose of producing income. Because most of a business's fixed assets will last longer than a year, it would be misleading to expense their entire cost in the first year they are acquired. To do so would distort income.

What Are Fixed Assets?

Fixed assets have three main characteristics:

- They are durable in nature and have physical substance.
- They are acquired by a business for use in its operations and are *not for resale*.
- They yield service over a number of years and *usually* may be depreciated.

Some examples of fixed assets are: equipment, furniture, buildings, and land. While land is a fixed asset, it is never depreciated. That is why we say fixed assets are "usually," but not always, depreciated.

Raw material, on the other hand, is not a fixed asset. Although it is durable and used by a business, it is not a fixed asset because it becomes part of a product that is held for resale.

Who May Claim Depreciation?

Normally the owner of the depreciable property is the person entitled to claim the depreciation expense. However, there are a few situations that need further clarification.

Depreciation may only be claimed by the taxpayer who retains the benefits and burdens of ownership. Generally, this is the same taxpayer who has legal title to the property, but this is not always the case.

A lessor is usually entitled to depreciate property that he leases to others. However, if the lessee is required by the lease terms to return the property to the lessor in the same condition as when he first leased it, the lessor suffers no economic loss, has none of the burdens of ownership, and, therefore, may not depreciate it. The lessee, in this instance, may claim the depreciation.

Whoever makes the investment and incurs the expense is entitled to the depreciation. It is therefore possible to have the lessor depreciate the property while the lessee is depreciating the improvements he made to the property.

S corporations claim depreciation the same as C corporations. The only difference is when an S corporation elects to expense an asset by claiming **Section 179 expense**. The Section 179 expense is a "pass through" item to the shareholders, meaning that no expense is taken at the corporate level, but rather at the individual level. We will discuss the Section 179 expense in depth in Section IV: "Chapter 1: First-Year Expensing." Also discussed in Section IV, Chapter 1 are other Section 179 deductions: Section 179B, Section 179C, Section 179D, and Section 179E.

What Property May Be Depreciated?

To qualify for depreciation, property must meet the following qualifications:

- It must be used in a trade or business or held for production of income.
- It must have a **useful life** of more than one year.
- It must wear out or lose value over time.
- It must be fully installed and ready for use.

First you need to determine if an asset is used in a "trade or business." A trade or business is an activity entered into with the reasonable expectation of earning a profit. It cannot be a hobby! This is an important distinction, which has been clarified by the IRS because of past abuses by taxpayers.

In addition to ascertaining that a profit motive exists, the asset to be depreciated also must be used, and not just owned, by the business. For example, if a corporation owns a motor home that is used only for the recreational enjoyment of its employees, such an asset may not be depreciated.

Furthermore, if property is used partly for business and partly for personal use, only the business portion may be depreciated. For more information, see Section IV: "Chapter 4:

Passenger Automobiles and Other Listed Property."

Some types of property, although used in a taxpayer's business or held for production of income, may not be depreciated. Examples of such property are:

- Inventory
- Property for which you pay rent
- Videotapes (for important information, see Section IV: "Chapter 7: Depreciation and the Alternative Minimum Tax (AMT).")
- Land

Costs involved with land improvements warrant further explanation, as the rules are somewhat complex. The costs of clearing, grading, and filling in land generally are not depreciable, but instead are added to the **basis** of the land. There is an exception to this rule, however, when these costs are associated with a depreciable asset such as a parking lot. In such a case, the land preparation costs will increase the depreciable basis of the parking lot, and will thereby be depreciated along with the lot. The costs of demolishing any structure, however, are *always* added to the basis of the land and may *never* be depreciated.

Note: Landscaping may sometimes be depreciated, but only if it is planted close enough to a building that it would be destroyed if the building was replaced. Also, exhaustible natural deposits, such as oil or gas, are said to be "depleted" rather than depreciated. (IRS Code Sec. **611**)

Once it is determined that the property qualifies as being used in a trade or business or is held for production of income, there are still three more qualifications it must have in order to be depreciated:

- The property must have a life that is longer than one year. If the property will last less than one year, it usually may be expensed in the year acquired. An example of this is the expensing of supplies.
- The property to be depreciated must be subject to either wear and tear or obsolescence over time. It must actually be used in a business, not merely displayed.
- The property must be installed and capable of being used. This is not necessarily the date on which it is acquired. We will discuss this further in "Elements of Depreciation," page I-7.

Note: If an item has a low unit cost, then even if it meets all of the above requirements for depreciation, it still may be expensed in the current year, due to the concept of materiality. For example, a small tool costing $25 may be expensed in the year purchased, even though it may have a service life of several years.

Additional Expenditures

If you have determined that an asset is depreciable, there may be an additional decision to make if you later incur an expense relating to that asset.

Additional expenditures invariably occur in relation to your fixed assets after they are initially acquired and placed in service. Such expenditures occur in the normal course of business in order to maintain a fixed asset or because of a change in its use. Depending on the nature of the expenditure, it may either be claimed as an expense or capitalized. If it is capitalized and the original asset is depreciable, then it can also be depreciated. The rules covering these additional expenditures are different for financial versus tax reporting purposes.

Financial Reporting

For financial reporting, such expenditures (either accrued or paid) may be divided into two broad categories, based on how they are handled on the financial statements:

- Revenue Expenditures
- Capital Expenditures

Revenue expenditures are current-period expenses and appear on the income statement. Capital expenditures increase the asset account and appear on the balance sheet. In other words, revenue expenditures only benefit the current period, whereas capital expenditures benefit both the current and future periods.

Think "future benefit!" To qualify as a capital expenditure, one of the following three conditions must apply:

- The useful life of the asset is lengthened.
- The value of the asset is increased (i.e., either the quantity of services produced by the asset is increased or the quality of what is produced is enhanced).
- The asset is adapted to a different use.

An expenditure that relates to a depreciable asset and that does not fit one of the above conditions is considered to produce no significant future benefit and, therefore, should be expensed.

What happens if an item is misclassified? If, for example, a capital expenditure is mistakenly recorded as a revenue item and expensed, what is the effect on the financial statements? Three things will happen:

1. The balance sheet will be understated (because the new asset was not included in the Property, Plant, and Equipment account).
2. The income statement will be understated in the year of purchase (because an expense was taken on the full amount of the asset's acquisition cost).
3. The income statement will be overstated in future periods (because the depreciation expense that should be claimed for the asset will not be deducted).

Within these classifications of revenue and capital expenditures, there are certain types of expenditures that are made to fixed assets during their depreciable lives. We can categorize them as follows:

- **Maintenance and repairs**
- **Improvements and replacements**
- **Additions**

Maintenance and Repairs

Maintenance and *ordinary* repairs are revenue expenditures and are expensed in the current period.

An allowance account may be used as a way of allocating this type of expense throughout the year. An allowance account is often used when:

- Monthly or quarterly financial statements are prepared *and*
- Routine maintenance and repairs are largely done only once or twice during the year.

An annual maintenance and repair program benefits a company throughout the year. It would, for example, be misleading to show 80% of the annual maintenance cost all in one month.

Example: Sage Smart, Inc. brings in an outside contractor several times each year to perform routine maintenance and repair its manufacturing equipment. The majority of the work is scheduled during May, which is its slowest month. Obviously, the benefits of this are seen throughout the year. Sage Smart sets up an Allowance for Repairs account, estimates that its cost will be $80,000 for the year, and makes the following entries:

Result: (Only shown for the first two quarters of the year)

End of first quarter (No maintenance has been done yet):

Repair expense	20,000	
Allowance for repairs (1/4 x $80,000)		20,000

End of second quarter ($60,000 repair costs incurred):

Allowance for repairs	60,000	
Cash or Notes Payable		60,000
Repair expense	20,000	
Allowance for repairs		20,000

Note: An *extraordinary* repair (such as an engine overhaul) should be accounted for as an improvement, a replacement, or an addition.

Improvements and Replacements

An improvement may entail a substitution or it may result from a major repair. If it involves a substitution and it results in a better asset than the one currently used, it is referred to as an improvement. If it involves a substitution of a current asset with a similar asset, it is referred to as a replacement.

An improvement or a replacement that benefits future periods is a capital expenditure. If, however, a replacement or an improvement is fairly minor (such as changing a light bulb), it is included as an ordinary repair and expensed.

When a substitution occurs, the old asset is removed and replaced with the cost of the new asset. Otherwise, as long as it benefits future periods, it is set up as a new asset (capitalized) and depreciated.

Additions

An addition should always be capitalized. It increases the size of an existing asset and creates a new asset. However, often an addition to an asset results in extra expenses due to the requirement of some change to the existing asset. An example of this is the cost of removing a wall to add a room to a building. In most cases the removal costs are expensed. Such costs would only increase the basis of the new asset (the addition) if the company had anticipated originally that the addition would be added.

Elements of Depreciation

Tax Reporting

Before 2014, the tax rules for additional expenditures made to fixed assets were not all that different from those for financial reporting purposes. However, effective for tax years beginning on or after January 1, 2014, the IRS issued new final regulations governing expenditures made on tangible property. Referred to as the tangible property regulations, the principal expenses covered by these regulations are for costs to acquire, produce, and improve tangible property.

The final regulations contain guidance for handling the following types of additional expenditures made to fixed assets:

- Materials and supplies
- Repairs and maintenance
- Improvements

There is also a definition of a "unit of property" included in the regulations.

Materials and Supplies

Materials and supplies are tangible property(but not inventory) that is used or consumed in the taxpayer's operations. Materials and supplies include components for the maintenance, repair, or improvement of a unit of tangible property. Materials and supplies also include rotable, temporary, and emergency spare parts.

Note: A "rotable spare part" is a material and supply part acquired for installation on property but which is removable. At some point, a rotable spare part may be removed from the property and repaired or improved. It is then reinstalled on the same property, installed on another property, or kept for a later time when it may be needed. A "temporary spare part" is a material and supply used temporarily until a new or repaired part is installed in its place. An "emergency spare part" is a material and supply acquired for a specific machine but is set aside to be used if needed to avoid down time.

The repair regulations allow $200 of materials and supplies to be expensed. Materials and supplies are deductible when purchased if they are incidental and deductible when used or consumed if they are non-incidental.

Note: Incidental materials and supplies are kept on had but no record of their consumption is maintained. Non-incidental materials and supplies are items that are usually more costly and less numerous and which the taxpayer tracks.

By being included as materials and supplies, rotable, temporary, and standby emergency spare parts may be expensed as they are used or consumed, or the taxpayer may elect to capitalize (and depreciate) them.

There is also an optional method that may be elected for either rotary or temporary spare parts whereby:

1. The cost of the part is expensed when initially installed.
2. The part's fair market value is recognized as income when later removed from the property and is also included in the basis of the rotable part, along with the cost of removing it.
3. The costs of any repairs, maintenance, or improvements are added to the part's basis in the year paid.
4. In the year the part is reinstalled, the cost of reinstalling it is deducted, as well as the amounts previously included in the rotable part's basis.
5. Any remaining basis of the part in the year in which it is disposed is also deducted.

Note: Standby emergency spare parts do not qualify for the optional method.

For example, A rotable part costs $100. Expense the $100 cost. Later the company removes the part from the property to make repairs/improvements to it and at that time its FMV is $80 and the cost to remove it is $2. Recognize $80 in income and record $82 in basis of the rotable part (i.e., capitalize it). Repairs/improvements cost $30 which is capitalized. In the year in which the part is reinstalled, it costs $10 to re-install so deduct the $10 and the $30 of repairs.

Repairs and Maintenance

Expenditures for routine maintenance may be expensed. To qualify as "routine," the maintenance must be made to keep the asset in efficient operating condition and must be expected to be performed more than once during the asset's class life. This includes any routine maintenance on a building and its structural components but with one difference: it applies to the real property only if the business reasonably anticipates performing the maintenance more than once in a 10-year period.

In addition, there is an annual election available whereby a taxpayer may instead choose to capitalize maintenance and repair costs that are capitalized on a taxpayer's books and records. Once made, this election is irrevocable.

Any repairs made to an asset before it is placed in service must be capitalized.

Improvements

Taxpayers are required to capitalize amounts paid for non-routine repairs which are made to improve tangible property. There are three types of expenditures for improvements:

- Restoring a unit of property
- Adapting a unit of property to a new or different use
- Adding a "betterment" to a unit of property

A restoration returns a property to its former state and intended use. Some examples:

- Rebuilding an asset after the end of its class life
- Replacing a major component or structural part

A betterment, unlike repairs, makes a material change to the property. Some examples:

- A fix to correct a defect or condition that was known at the time of acquisition or developed during its production
- A material addition to the unit of property including a physical enlargement, expansion, extension, or increase in capacity
- An expenditure expected to materially increase the productivity, efficiency, strength, quality, or output of the property

There is a special safe harbor rule for small taxpayers who own or lease buildings valued at $1 million or less. Taxpayers, who have average annual gross receipts of $10 million or less during the three preceding tax years, may elect not to capitalize (and, therefore, deduct) the cost of improvements if their total expense for maintenance, repairs, and improvements is the lesser of $10,000 or two per cent of the building's unadjusted basis. This allowable expensing of improvements is calculated on a per-building basis and if taken, must be elected annually for each building.

Unit of Property

When the IRS issued its final repair regulations, much of the language concerns a "unit of property" that is being placed in service, repaired, or improved. The definition of a "unit of property" is a single unit of property, other than a building, that consists of components that are functionally interdependent. All the components of a unit of property must be of the same class of property and be properly depreciated using the same recovery method for tax reporting.

The rules for what comprises a unit of property for the capitalization rules do not affect how an asset is treated for depreciation. The reverse is not true, however, as how the taxpayer treats an asset for depreciation purposes, may affect how it is treated for capitalization purposes.

For real property, a building is considered a unit of property and includes its structural components. However, the major systems of a building are treated as separate units of property.

The nine components of a building (each of which is considered a building system and separate from the building) are:

Heating, ventilation and air conditioning systems (HVAC),

1. Plumbing systems,
2. Electrical systems,
3. All escalators,
4. All elevators,

5. Fire protection and alarm systems,
6. Security systems,
7. Gas distribution systems, and
8. Any other systems defined in published guidance

After you have determined that a particular fixed asset is depreciable, you need to know four things:

- The type of property.
- The date the asset was **placed in service**.
- The asset's **estimated useful life**.
- The asset's **depreciable basis**.

Note: Whether you are using a monthly or a 52/53-week accounting cycle will have no effect on the amount of depreciation claimed or how it is calculated.

Type of Property

Probably one of the most important things you need to know is the type of property. There are various rules concerning allowable methods of depreciation, as well as certain limitations to the amount of depreciation that may be claimed, all according to property type.

There are two major types of property:

- **Tangible**
- **Intangible**

Tangible property includes two kinds:

- **Personal**
- **Real**

Furthermore, within these classifications, there are other special types of property:

- **Amortizable property**
- **Listed property**

Tangible property is anything that can be seen or touched, whereas intangible property lacks physical substance. Generally, qualifying tangible property is depreciated and qualifying intangible property is amortized. Machinery, for example, is tangible and, therefore, depreciable, while a copyright is intangible and amortizable. **Amortization** is very similar to depreciation except that it always uses the straight-line method.

Note: For tax purposes, unlike accounting rules, both tangible and intangible property are sometimes said to be depreciated. (For a discussion of amortization, see Section II: "Amortization.")

Tangible property can be personal or real. Personal property, sometimes referred to as IRS Code **Section 1245 property**, includes cars, equipment, machinery, furniture, and anything that is tangible except for most real property. There are a few assets that are both Section 1245 property and real property. (A single purpose agricultural structure is one such example.) Generally real, property, sometimes referred to as IRS Code **Section 1250 property**, is buildings and land, and anything that is growing on or attached to the land.

Listed property is a special classification used for tax reporting purposes, not for financial reporting. The reason it is important for tax reporting is that the IRS has imposed both record keeping requirements and depreciation limitations on listed property. Listed property includes both personal and real property. It includes forms of transportation that can be used for personal as well as business purposes, such as cars, trucks, and boats. It also includes computers, cellular phones, and certain recreational, entertainment, and amusement properties. (For more information on listed property, see Section IV: "Chapter 4: Passenger Automobiles and Other Listed Property.")

The Date Placed in Service

Once you have determined the property type, the next step is to find out the date on which the asset was placed in service. For tax reporting purposes, the date placed in service, like the property type, can affect the allowable depreciation method. Also, for both financial and tax reporting purposes, the date placed in service affects the amount of depreciation taken for the first year it is used.

Depreciation begins on an asset on the date it is placed in service, which is not necessarily the same date on which it is acquired. Probably the best way to explain when an asset is placed in service is by use of the following examples:

- Machinery must be fully installed and operational.
- A truck purchased for heavy lifting must be ready and available to perform the function for which it was purchased. If it needs to be modified before it can perform, then depreciation cannot begin until it is capable of performing the desired function.
- Rental property can be depreciated as soon as it is ready and available to be rented. The fact that no one has yet rented it will not prevent it from being depreciated.
- A special rule exists for when depreciation begins on construction equipment used by a business to construct its own capital improvements. Here you must **capitalize** the cost of the construction equipment used and depreciate it over the life of the facilities being built. Depreciation of the equipment begins, therefore, when the facilities are placed in service.

Note: Depreciation ends when the asset's basis is fully recovered, or when it is disposed of or sold. If an asset becomes temporarily idle, depreciation continues to be claimed.

Estimated Useful Life

Another needed fact, the asset's estimated useful life, is determined very differently for financial reporting purposes and for tax reporting purposes. Whereas for financial purposes it is a realistically chosen life, for tax purposes it is a statutory number of years based on the type of property and year in which it was acquired.

Depreciable Basis

What you need to know to determine an asset's depreciable basis is discussed in the following segment.

Basis Used for Depreciation

The depreciable basis of an asset is the amount that may be claimed as a deduction over the asset's life or recovery period.

How To:

An asset's depreciable basis equals the following:

	Asset's **Acquired Value**
plus	Freight and installation costs
plus	Cost of repairs adding value or lengthening life
minus	**Section 179A expense** (clean fuel deduction) *
minus	**Electric Vehicle Credit** reduction amount
times	**Business-use percentage**
minus	**Section 179 expense** (including Sections **179B**, **179C**, **179D**, and **179E**)
minus	**Investment Tax Credit** reduction amount
minus	**First-year deduction (30%, 40%, 50%, or 100%** bonus depreciation**)** **
minus	**Salvage value**—if straight-line or sum-of-the-years'-digits method used
equals	Depreciable Basis

* The 2005 Energy Bill sunsets Section 179A deductions for clean-fuel vehicles and clean-fuel vehicle refueling property placed in service after 12/31/05, rather than 12/31/06. For vehicles placed in service after 2005, the 2005 Energy Bill introduced new tax credits for the purchase of hybrid, fuel cell, advanced lean burn diesel, and other alternative power vehicles.

** - 30% depreciation allowance under Section 168(k) is allowed for qualified property, including property with longer production periods from 9/11/01 to 5/5/03 and from 1/1/2019 to 12/31/2020.
- 30% depreciation allowance is allowed for qualified New York Liberty Zone from 9/11/01 to 12/31/06 (12/31/09 for real property).
- 50% depreciation allowance under Section 168(k) is allowed for qualified property from 5/6/03 to 12/31/04 (12/31/06 for property with longer production periods).
- 50% depreciation allowance under Section 168(k) is allowed for qualified property from 1/1/08 to 12/31/17 (12/31/18 for property with longer production periods).
- 50% depreciation allowance is allowed for qualified Gulf Opportunity Zone from 8/28/05 to 12/31/07 (12/31/08 for certain counties and parishes and 12/31/10 for real property).
- 50% depreciation allowance is allowed for qualified Kansas Disaster property from 5/5/07 to 12/31/08 (12/31/09 for real property).
- 50% depreciation allowance is allowed for qualified Disaster Zone property from 1/1/08 to 12/31/12 (12/31/13 for real property).
- 50% depreciation allowance is allowed for cellulosic biofuel property from 12/21/06 to 1/2/13.
- 50% depreciation allowance is allowed for second generation biofuel property from 1/3/2013-12/31/2016.
- 50% depreciation allowance is allowed for qualified reuse and recycling property starting 9/1/08.
- 100% depreciation allowance under Section 168(k) is allowed for qualified property from 9/9/10 to 12/31/11 (12/31/12 for property with longer production periods).
- 100% depreciation allowance under Section 168(k) is allowed for qualified property from 9/28/17 to 12/31/22 (12/31/23 for property with longer production periods). Different percentages apply for property acquired before 9/28/17 and placed in service after 9/28/17 and future years.

Note: The above computation is for the initial calculation of depreciable basis when the asset is first acquired. In following years, depending on the depreciation method being used, it may be necessary to also subtract out the accumulated depreciation already claimed on the asset before making subsequent calculations.

Notice that the starting point of the above formula is the asset's "acquired value." When an asset is purchased, the acquired value is simply its cost. However, there are many different ways to acquire assets, and each one has its own method for determining its acquired value:

Acquired by:	Basis is:
Inheritance*	**Fair market value**
Gift*	Carryover basis (i.e., basis in the hands of the donor)
Conversion from personal use	Lesser of: • **adjusted basis** (usually cost plus any improvements) or • Fair market value on date of conversion

* See IRS Code Sections **1011, 1014, and 1015** for further detail.

You will notice in the formula given at the start of this segment that several things increase basis:

Any freight and installation costs required to get the asset ready for its intended use will increase the asset's depreciable basis. Also, for tax purposes, the cost to investigate and facilitate the acquisition of an asset is capitalized. (For a detailed explanation of how repairs are handled, see "Additional Expenditures," page I-4.)

You will also notice in the formula for depreciable basis computation that several things decrease basis:

Salvage value sometimes reduces an asset's basis for depreciation, depending on the depreciation method being used. Salvage value is the estimated amount for which an asset could be sold at the end of its useful life. Straight-line and **sum-of-the-years'-digits** are depreciation methods that require that the salvage value be subtracted from the asset's acquired value to determine its depreciable basis. Under the **declining-balance methods**, however, while the salvage value is not subtracted from basis, the asset cannot be depreciated below its salvage value. Both ACRS and MACRS ignore salvage value entirely.

The 30%, 40%, 50%, and 100% first-year deduction (bonus depreciation) and the Section 179 expense (see Section IV: "Chapter 1: First-Year Expensing.") must be subtracted from an asset's acquired value to determine depreciable basis. When claiming both on the same asset, the Section 179 amount is deducted first.

You also need to watch for a possible basis reduction due to past Investment Tax Credit taken. For qualifying property placed in service after 1982 and before 1986, the taxpayer had a choice between reducing the asset's basis by one-half of the Investment Tax Credit taken or reducing the amount of the Investment Tax Credit itself. Be sure to make the appropriate reductions to the basis if necessary, when claiming the Investment Tax Credit.

Trade-ins and Basis

In the previous section, we explained that the computation for depreciable basis starts with the property's acquired value. When an asset is purchased, the acquired value is simply its cost. However, when an asset is received in a trade-in, the acquired value is not always as apparent. In addition, the value assigned to such an asset may be different for financial reporting than for tax reporting purposes.

Financial Reporting

For financial reporting purposes, nonmonetary exchanges are generally recorded at fair market value (FMV). The newly acquired asset is recorded at its fair market value or the fair market value of the asset relinquished, whichever is more evident. However, this is not always the case. Determining the value of a newly acquired asset can be somewhat complex when a trade-in is involved.

First we need to distinguish between trading *similar* assets and trading *dissimilar* assets. Similar assets are of the same general type, used for approximately the same purpose and in the same line of business. They do not need to be identical. If the trade-in does not involve a similar asset, the asset is treated as "dissimilar." This is an important distinction, as the treatment of the trade-in depends on the type of asset being traded.

When dissimilar assets are traded, such as land for a building, the asset received is recorded at the fair market value of the asset relinquished in the trade (unless the fair market value of the asset received is more apparent). You must also consider whether "boot" is involved. Boot is the cash or note payable given or received in addition to the asset traded. When a dissimilar asset is acquired, it is recorded at the FMV of the asset relinquished, plus the amount of any boot paid, less any boot received. Any gain or loss is recognized.

Example: Sage Trade, Inc. trades a machine with a fair market value of $25,000 for some land. The machine cost $30,000 and had $9,000 of depreciation expense claimed on it.

Result: The land received is recorded at $25,000, the fair market value of the machine given in trade. There is a $4,000 gain on the exchange. This is the difference between the machine's FMV ($25,000) and its net book value ($21,000). The following entry is made:

Land	25,000	
Accumulated depreciation	9,000	
Machine		30,000
Gain on exchange		4,000

When similar assets are traded, different situations require different handling:

- *If it's a loss situation*:* The asset received is recorded at the book value of the asset relinquished, less the amount of the loss (which is recognized), increased by any boot that is paid.
- *If it's a gain situation, and no boot is received:* The asset received is recorded at the book value of the asset relinquished, increased by any boot that is paid. (No gain is recognized.)
- *If it's a gain situation, and boot is received:* The asset received is recorded at the book value of the asset relinquished, less boot received, plus the gain recognized. (Only the portion of the gain relating to the boot is recognized.)

Note: *A gain or loss situation is determined by comparing the net book value of the relinquished asset with its fair market value (FMV). If the asset's FMV is more than its net book value, there is a gain.

Example: Sage Trade, Inc. trades a machine with a fair market value (FMV) of $15,000 (cost of $20,000 and with $8,000 of accumulated depreciation) for a similar machine.

Result: Since the traded machine's fair market value of $15,000 is more than its net book value of $12,000 ($20,000 cost less $8,000 depreciation), it is a gain situation. Since no boot is received, no gain is recognized. The new machine is recorded at $12,000, the book value of the asset relinquished:

Machine (new)	12,000	
Accumulated depreciation	8,000	
Machine (old)		20,000

Example: Assume the same facts as above except that Sage Trade, Inc. receives both a similar machine and $5,000 cash. The fair market value of the machine received is $10,000. (If the FMV of the asset received is not known, it may be calculated by subtracting the boot received from the FMV of the asset relinquished.)

Result: Since this is a gain situation (i.e., the FMV of the asset relinquished ($15,000) is more than its net book value ($12,000)) and boot ($5,000) is received, a portion of the gain relating to the boot is recognized. The formula for determining the amount of the gain to recognize is:

$$\frac{\textit{Boot received}}{\textit{Boot received} + \textit{FMV of Asset Received}} \times \textit{Total Gain*} = \textit{Gain Recognized}$$

* The *Total Gain* is the excess of the FMV of the assets received (including any boot received) over the net book value of the assets given up.

Therefore:

$$\frac{\$5{,}000}{\$5{,}000 + \$10{,}000} \times \$3{,}000 \;\; (\$10{,}000 + \$5{,}000 - \$12{,}000) = \$1{,}000$$

The new machine is now recorded at $8,000:

	Net book value of old machine given up	$12,000
less		
	Boot received	(5,000)
plus		
	Portion of gain recognized	1,000
	Basis of newly acquired machine	**$ 8,000**

Sage Trade, Inc. makes the following entry:

Cash	5,000	
Machine (new)	8,000	
Accumulated Depreciation	8,000	
Machine (old)		20,000
Gain on Exchange		1,000

Tax Reporting

For tax reporting purposes, an asset's value may be different from its value according to Generally Accepted Accounting Principles (GAAP). When an asset is acquired by use of a trade-in, the basis of the new asset is the adjusted tax basis of the asset relinquished plus any boot paid.

Example: Sage Trade, Inc. trades in an old machine for one worth $12,000. The old machine cost $10,000 two years ago and $5,200 of depreciation has been claimed. Sage Trade, Inc. also pays $7,000 cash.

Result: The basis of the new machine is:

Cash paid		$ 7,000
Basis of old machine:		
Cost	$10,000	
Accumulated depreciation	(5,200)	
Basis of old machine		4,800
Basis of new machine		$11,800

Sage Trade, Inc. makes the following entry:

Machine (new)	11,800	
Accumulated Depreciation	5,200	
Machine (old)		10,000
Cash		7,000

One of the provisions of the Tax Cuts and Jobs Act is that like-kind exchange treatment is no longer allowed for depreciable tangible personal property, and intangible and non-depreciable personal property. Effective for disposals/exchanges after 2017 (with limited transition exceptions).

The tax rules for how you depreciate the asset received in a like-kind exchange (or in an involuntary conversion) changed after January 2, 2000 (IRS Notice 2000-4). You now depreciate the new asset over the remaining recovery period of the old asset, rather than having to start with a new placed-in-service date. This accelerates the new asset's depreciation.

There are two requirements for applying these new rules:

- The transaction must qualify either as a §1031 like-kind exchange or as a §1033 involuntary conversion.
- The property given up *and* the property received must both be MACRS property.

The new rule only applies to the amount of the new asset's basis that does not exceed the taxpayer's basis in the old asset. If no additional money is paid, the new asset literally "steps into the shoes" of the old asset and continues with the old asset's depreciation method, its averaging convention, and, most importantly, its recovery period.

Should the basis of the new asset *exceed* the basis of the asset given up, the asset must then be depreciated as if it were two separate assets:

- Asset #1, which will have a basis equal to the old asset, is depreciated exactly as if it were the old asset, had it not been disposed.
- Asset #2, which represents the excess of the new asset's basis over the old asset's basis, is depreciated as a newly purchased asset. This asset should be assigned an appropriate depreciation method, with a new recovery period starting with its new placed-in-service date.

Example: Assume the same facts as above.

Result, prior law: The new machine is recorded at $11,800, with a new 5-year recovery period, and it receives $2,360 of depreciation for the first year.

Result, new law: The new machine is recorded as the following two assets:

Asset #1, cost of $10,000, with accumulated depreciation of $5,200, receives $1,920 ($10,000 x 19.2%, i.e., the third year percentages from the IRS table) of depreciation in the first year.
Asset #2, cost of $7,000 receives $1,400 ($7,000 x 20%) of depreciation in the first year.

Under the new rules, Sage Trade, Inc. deducts $3,320, or $960 more depreciation expense than under the prior law.

TIP
For tax purposes, it may not be advisable to trade in an asset if its market value is below its adjusted basis. In such a case, it may be better to sell the asset at a loss, claiming an immediate deduction. If the asset is traded, its undepreciated basis is added to the new asset and is deducted over a much longer period of time (the new asset's life). In making this decision you need to estimate your future income and tax rates.

Miscellaneous Basis Issues

There are a few more unusual situations where the property's basis needs to be determined under very specialized rules. These, along with appropriate references, are as follows:

- Personal Property reacquired by foreclosure (IRS Reg. **1.166-6(c)**)
- Real property reacquired by foreclosure (IRS Sec. **1038 (c)**)

In addition to the above, there is also the issue of when property, usually real estate, is acquired with a nonrecourse note. In such a case, if the fair market value of the property is less than the nonrecourse note, the asset's basis will be limited to its true value. This prevents the taxpayer from inflating the value of the property in order to claim large depreciation deductions. (See **Mayerson v. Commissioner, 47 TC 340 (1966)**.)

Note: A nonrecourse note only gives the seller rights against the property and not the buyer, if payment of the note is not made. In other words, if the buyer defaults on the note, the seller, or holder of the note, may repossess the property but cannot come after the buyer's personal assets to try to collect.

TIP
When acquiring property subject to a nonrecourse note, it is advisable to obtain an outside appraisal of the property to ascertain its value. This is especially important if the property is acquired from a related party.

Multiple Depreciation Calculations: An Overview

Now that you have an understanding of the types of property that may be depreciated, the elements of depreciation, and who can claim depreciation, you are ready to understand how depreciation is calculated. There are many different methods of depreciation. Different depreciation methods are used for different types of reporting:

- Financial reporting purposes—i.e., for the preparation of financial statements for presentation to company shareholders or to a lending authority such as a bank, or
- Tax reporting purposes—i.e., for the preparation of income tax returns.

Depreciation methods used for financial reporting are fairly straightforward. We will explain these in Section III: "Depreciation for Financial Reporting."

Depreciation methods for tax reporting purposes, however, are somewhat more complicated. Although these methods are based on some of the same methods as used for financial reporting, the IRS kept changing the rules over the past several years. Therefore, it is always necessary to first know the date on which an asset was placed in service and then to check which rules governed on that date.

Furthermore, for tax reporting purposes, even when you know the date placed in service, there are several different methods that may be required by the IRS to be used to depreciate the same asset, depending on which tax form you are completing:

- Federal income tax depreciation.
  - General depreciation—IRS Form 4562.
  - Alternative Minimum Tax depreciation—IRS Form 4626 (C corporations) or IRS Form 6251 (individuals).
  - Adjusted Current Earnings depreciation—IRS Form 4626 (C corporations).
- State income tax depreciation. These may or may not be the same depreciation methods as used for federal reporting purposes.

None of the above is complicated if taken one step at a time. In the following pages of this guide we will lead you through it.

Section II: Amortization

In this section:

As previously stated, qualifying intangible property may be amortized, rather than depreciated. Although for tax purposes the distinction is not always made between amortization and depreciation, amortization remains a viable concept in financial accounting and we will treat it separately here.

Amortization is computed using the straight-line method. (For an in-depth explanation of how to make the calculation, see Section III: "Depreciation for Financial Reporting.") The life of the property is determined by different factors depending on the type of property and whether it is being amortized for financial or tax reporting purposes.

For financial reporting, in most cases, the asset's useful life is the deciding factor. Generally, the rules that govern the amortizable life are less restrictive for financial reporting purposes than for tax reporting purposes.

The amortization rules for tax reporting purposes were greatly changed by the Revenue Reconciliation Act of 1993. One of the provisions of this Act was the adoption of a standardized 15-year period for recovering the cost of most intangibles acquired by a business, including **goodwill**. While the 1993 tax law was advantageous for some intangibles, it did require a longer—and thus slower—recovery period for others. Such property is now referred to as "**Section 197 intangibles**."

Since the amortization rules for intangible property are very different for financial versus tax reporting purposes, we will cover them separately in this chapter.

Amortization of Property for Financial Reporting Purposes

For financial reporting purposes, an intangible asset usually cannot be expensed. Rather, it is either amortized over its useful life or, if the asset's life is considered to be indefinite, it is capitalized and tested for impairment (usually annually). The amortizable life of an intangible asset is the period over which it gives economic benefit. There are several factors that should be considered when deciding on a useful life:

- Legal or contractual limitations.
- Renewal provisions.
- Effects of obsolescence, demand, and competition.
- Service life expectations of the people who use it.

Note: The costs of most intangible assets with finite lives are required to be amortized whether the assets are purchased or developed internally.

There are a number of different types of amortizable intangible property. We will give a brief description of some of the more common ones, listed alphabetically, along with the life to be generally used in amortization.

The Statement of Financial Accounting Standards No. 142 (now FASB ASC 350), dated June 2001, superseded Accounting Principles Board Opinion No. 17, which had previously imposed a maximum life of 40 years on intangibles. FASB ASC 350 states that goodwill and other intangible assets that have indefinite useful lives will no longer be amortized. Instead, they should be assessed (at least annually) for impairment. An impairment loss occurs when an asset's carrying amount exceed its recoverable amount. If assets are impaired, their carrying amount is reduced and an impairment loss is recognized.

Computer Software

The costs of computer software, either purchased or developed internally, may be research and development (R & D) costs. If they are considered to be part of R & D, then they must be expensed. Computer software costs are not research and development costs, however, if the software is used in selling or administrative activities.

Sometimes, software is purchased and its cost is included with the price of the hardware instead of being itemized separately. When this happens, the software is treated as part of the basis of the hardware and is depreciated at the same rate and over the same life as the hardware.

If amortized, computer software is generally given a 60-month life. It may be amortized over a shorter period, however, if it can be clearly established that it will be obsolete or no longer used in a shorter period of time.

Copyrights

A copyright gives an exclusive right to reproduce, publish, and sell a literary product or artistic creation. The copyright's amortizable basis is the amount paid for it, if purchased, or if developed internally, the costs of securing it, as well as the costs of producing the work such as wages and materials. Any costs incurred to establish the copyright are also included as part of its basis.

Prior to 1978, a copyright was granted for 28 years, with the right to renew for another 28 years. Today a copyright is granted to a corporation for 120 years after creation or 95 years after publication, whichever expires first, and to an individual for the life of the author plus 70 years. However, the estimated useful life of a copyright is usually much less than its legal life, and it is generally written off over a fairly short period.

Covenants-Not-To-Compete

When purchasing a business, the contract will often contain an agreement that the seller will not engage in a competing business in a certain area for a specified period of time. A **covenant-not-to-compete** protects the buyer from immediate competition from the seller so that the buyer will have the opportunity to establish himself in the business.

The cost of the covenant-not-to-compete should be amortized over the period covered by the covenant, unless its estimated economic life is expected to be less.

Customer Lists

Customer lists represent groups of clientele with whom a business has established relationships. Their value is based on the assumption that the customers will continue business with the company and thus reduce marketing costs. Examples include patient record cards, subscriber lists, and service accounts. They are frequently sold for a specified price when a business or division is sold.

The value of a customer list diminishes over time as customers are lost. There are two different approaches for writing off a customer list. One method is to determine the life of such a list, based on historical data from similar types of businesses located in the same geographical area. If this information is available, then an estimated life can be determined and used to amortize the list.

Another method is to assign a value to each customer on the list, based on historical data. For example, if over a given year you could assess the total dollars earned by the company from each customer, you could then determine a percentage for each customer's business as compared to total earnings from all customers and, finally, multiply that percentage times the cost of the customer list. Then as a customer was lost, you would expense the dollar amount assigned to that particular customer.

Easements

Easement costs, which grant a right-of-way, frequently given to public utility companies for example, may be amortized if there is a limited and specified life.

Franchises

The cost of a franchise includes the fee paid to the franchisor, as well as any legal costs or expenses paid for acquiring it. Annual payments made under a franchise agreement, however, are expensed when incurred.

A franchise that is granted for a limited period should be amortized over its life. If the franchise has an indefinite life, it should be assessed, at least annually, for an impairment loss.

Goodwill

When a business is purchased and the buyer pays more than fair market value for its identifiable assets, net any liabilities assumed, this difference is called goodwill. Goodwill is measured by unrecorded assets such as loyal customers, a favorable location, a favorable line of credit, or superior management. These unrecorded assets may result from a variety of factors, including advertising or a business's reputation for quality control.

In December, 2000, the Financial Accounting Standards Board decided that goodwill that is recorded due to an acquisition can no longer be amortized. Under the new guidelines, goodwill should be reviewed for impairment and expensed against earnings only in the periods in which the recorded value of goodwill is more than its fair market value.

Note: Goodwill that is generated internally has no assigned value and is not recorded on the books.

Leasehold Improvements

Leasehold improvements are permanent betterments made to leased property, which is owned by someone else and which will usually revert to the owner at the end of the lease period. For example, a tenant may build shelves or install fixtures on the walls of a store he is renting. Although for income tax purposes leasehold improvements are depreciated, for financial reporting they are amortized.

Leasehold improvements are amortized over the remaining term of the lease or their expected useful life, whichever is shorter. If amortizing the improvements over the remaining term of the lease, renewal options in the lease agreement are generally ignored due to the uncertainty of whether or not the renewal will actually occur.

Organization Costs

Organization costs are the various costs incurred when forming a corporation or a partnership. For a corporation, these include attorneys' fees, accounting services, costs of issuing stock, and incorporation fees. For a partnership, these include attorneys' fees, fees incurred in the preparation of the partnership agreement, accounting fees, and filing fees. According to FASB ASC 720-15, organization costs are expensed as incurred.

Patents

A patent gives the owner the exclusive right to use a product or process for a period of 20 years. The patent may be developed internally, or it may be an existing patent that is purchased from someone else.

If developed internally, the patent's amortizable basis includes legal fees for patent applications, patent fees, litigation costs, and filing fees. Research and experimental expenses are discussed below, but are not included as part of the patent.

If the patent is purchased, the amortizable basis is the purchase price plus any costs, such as attorney fees, of successful legal actions to protect the patent.

Note: If a legal suit to protect a patent is unsuccessful, then the costs incurred, including all costs associated with the patent, may be written off immediately, since the patent would have then lost its value.

Normally a patent is amortized over its legal life of 20 years or its remaining life, if purchased from someone else. However, the actual life of a patent may be shortened if, for example, another process is developed that makes the original patent obsolete. The cost of the patent should be amortized over its legal life or over its economic life, whichever is shorter.

Research and Development Costs

Research and development costs must be expensed in the year paid or incurred (dependent on the business's accounting method). However, if there are intangibles purchased for use in research and development that have an alternative future use, they should be capitalized and amortized if they have a useful life or, if they have an indefinite life, they are subject to impairment testing.

Trademarks and Trade Names

Since trademarks and trade names may be renewed indefinitely, they have unlimited legal lives. If the trademark or trade name is developed internally, the cost to be amortized includes attorneys' fees, registration fees, design costs, and any other expenditures incurred in obtaining it. If it is purchased, the amortizable basis is the purchase price.

The cost of a trademark or trade name is subject to impairment testing if it is found to have an indefinite life (that is, if it is being continually renewed). Other times, the value of a trademark may have a very short life and should be amortized accordingly.

Amortization of Property for Tax Reporting Purposes

The Revenue Reconciliation Act of 1993 created a standardized 15-year period for amortizing most intangibles acquired by a business and, thereby, greatly changed the existing guidelines for amortization. There are, of course, many intangible assets still being amortized according to the pre–1993 Tax Act rules. This section will therefore be divided between pre–1993 Tax Act and post–1993 Tax Act rules.

Pre-1993 Tax Act Rules

Before the passage of the Revenue Reconciliation Act of 1993, the rules for amortization for tax reporting purposes were very similar to those for financial reporting purposes. Intangible assets that had a determinable life, such as a covenant-not-to-compete or a patent, used the asset's actual life for amortization purposes. Other intangible assets, such as computer software and organization costs, were usually amortized over a 5-year-period. However, some intangibles had special rules for tax reporting; we will summarize these below:

Goodwill

Goodwill could not be amortized.

Trademarks and Trade Names

Trademarks and trade names, prior to 1987, were amortized over 60 months. After 1986 and before the 1993 Act, they were capitalized and were not allowed to be written off.

Franchises

Franchises, generally, were amortized over the shorter of 10 years or the term of the agreement, including renewal periods if the prospect of the renewal was reasonably certain. However, if either the cost of the franchise was more than $100,000 or the franchise was being paid for over time, in installments, then special rules applied. (See IRS Code Sec. 1253 (d)(2) for further clarification.)

Customer Lists

Customer lists could be amortized only if they had a determinable life, based on facts and not just on unsupported opinion. However, if the amount paid for purchasing a customer list could not be separated from the amount paid for the purchase of goodwill, it could not be written off (since goodwill was not amortizable). If the latter occurred, the customer list could be expensed only on a final tax return if the entity went out of business.

Post–1993 Tax Act Rules

A standardized amortization period of 15 years, created by the Revenue Reconciliation Act of 1993, applies to qualifying property acquired after August 10, 1993, and may be elected for property acquired after July 25, 1991 (IRS Code Sec. 197, which is included in Section VII: "Quick Reference."). The 15-year period begins with the month of acquisition, and it applies *regardless* of the asset's actual useful life. These Section **197** intangibles, as they are now referred to, cover a large variety of intangible assets.

Being able to amortize goodwill was an important tax law change. Businesses with goodwill acquired after the above effective date can now take advantage of an extra deduction that previously was not allowed. Now a buyer can recover the cost of any goodwill, as well as a customer list, over the same 15-year recovery period.

While the 1993 tax act is advantageous for some intangibles, it requires a longer—and thus slower—recovery period for others. Covenants not to compete, for example, were amortized under prior law over the life of the covenant. A typical covenant-not-to-compete is in place for only 5 years. Now, all such covenants must be amortized over 15 years. Therefore, it takes much longer to fully recover their cost.

The intangibles that must now be amortized over 15 years include the following:

Covenants-Not-To-Compete

A covenant-not-to-compete is a promise by the seller of a business, made to the purchaser of that business, not to engage in a similar business within a specified area for a specified period of time. It gives the buyer an opportunity to secure a share of the market.

Customer-Based Intangibles

A customer-based intangible is the value of a market share, the composition of a market, or anything else resulting from the future provision of goods or services that arise from relationships with customers in the ordinary course of business. An example of a customer-based intangible is the portion of an acquired business that is attributable to the existence of a customer base, circulation base, undeveloped market, or market growth.

Franchises, Trademarks, and Trade Names

Franchises are contracts for the exclusive right to perform certain functions or to sell certain services or products. The franchisee may be allowed to use a certain trademark or trade name.

Goodwill and Going-Concern Value

Goodwill represents the benefit acquired in the purchase of a business, beyond the value of its assets. It includes loyal customers and a favorable location.

Going-concern value is the additional value that attaches to property because it is an integral part of an ongoing business. It includes the value assigned to the ability of a business to continue its operation without interruption in spite of an ownership change.

Information Bases

Information bases include customer lists, subscription lists, patient or client files, lists of advertisers, insurance expirations, training manuals, and any accounting or inventory control systems.

Licenses and Permits Granted by a Governmental Unit

This category includes liquor licenses, airport landing and takeoff rights, airline routes, and television and radio broadcasting licenses. Each renewal of these items is considered another acquisition. Also, although sometimes a license or permit is granted for an indefinite period of time, it still may be amortized over 15 years.

Patents, Copyrights, and Know-How

This category includes patents; copyrights; formulas; formats; package designs; and interests in films, sound recordings, videotapes, and books. It also includes computer software, but only if the software has been substantially modified, is under an exclusive license, or is not available to the general public.

Computer software that does *not* qualify for the 15-year standardized amortization period is depreciated on a straight-line basis over 3 years, beginning in the month placed in service, under IRS Code Section **167(f)(1)**. Generally, "off-the-shelf" software and software that is not acquired as part of an acquisition of a trade or business qualifies as Section 167(f) software, if acquired after August 10, 1993. The additional depreciation allowance applies to such software also.

Supplier-Based Intangibles

A supplier-based intangible is the value attached to the future acquisition of goods or services under relationships with suppliers of goods or services that are to be sold by the taxpayer. For example, the portion of a purchase price of an acquired business attributable to the existence of a favorable relationship with people who provide distribution services, such as favorable shelf or display space, is a supplier-based intangible. Another example of a supplier-based intangible is a favorable credit rating.

Workforce in Place

Workforce in place is the value of highly skilled, educated, and experienced employees of a business at the time it is purchased. It also includes the cost of acquiring any existing contracts or relationships with employees or consultants.

Miscellaneous Rules for Section 197 Intangibles

1. Generally, Section **197** intangibles cannot be created by the taxpayer. They must be acquired in a transaction involving the acquisition of assets constituting a trade or business or a substantial portion of one. However, the exclusion of Section **197** intangibles created by the taxpayer does *not* apply to trademarks, trade names, franchises, or licenses and permits granted by a governmental unit.
2. There are also special rules if Section **197** intangibles are disposed of at a loss. When this happens and the business still owns any other Section **197** property that was acquired in the same transaction as the intangible now being disposed, no loss can be claimed. The unrecognized loss must be added to the bases of the intangibles retained.
3. Finally, some intangible assets are not subject to IRS Code Section **197** and, therefore, are not assigned the 15-year standardized life:
   - **Organization Costs and Start-Up Costs.** Organization costs are incurred when forming a business entity such as a corporation or partnership. Start-up costs relate to beginning the operations of a new business. Generally, they are amortized over 60 months.

     Note: Syndication costs, which are expenses connected with issuing and marketing the interests in a partnership, may not be amortized or expensed.

- **Research and Development Costs.** Research and development costs either are expensed in the year paid or incurred or are amortized over a period of at least 60 months (IRS Code Sections **174**).
- **Section 167(f) software.** Section 167(f) software is depreciated on a straight-line basis over 3 years. Section 167(f) software that is also “off-the-shelf” software is eligible for Section 179 expensing if placed in service in a tax year beginning in 2003 or later.
- **Geological and Geophysical Expenditures.** The Tax Increase Prevention and Reconciliation Act of 2005 extended the amortization period of geological and geophysical expenditures (G & G costs) to five years for major integrated oil companies. G & G costs are the expenses incurred in gathering data in order to acquire mineral properties. Previously G & G costs were amortized over two years.
- **Musical Compositions or Copyrights.** The Tax Increase Prevention and Reconciliation Act of 2005 enacted a provision to allow taxpayers to elect to treat the sale or exchange of self-created musical compositions or copyrights as the sale or exchange of a capital asset. This bill also temporarily allowed for expenses paid or incurred in creating or acquiring composition or copyright to a musical composition to be amortized over five years, for years 2006 through 2010.

Miscellaneous Amortizable Property

There are also less common types of property that may be amortized. These, along with the appropriate IRS Code Sections, are as follows:

- Certain intangible drilling costs—Sec. **291(b), 263(c)**
- Circulation costs—Sec. **173**
- Mine development costs—Sec. **291(b), 616(a)**
- Pollution control facilities—Sec. **169**
- Reforestation expenditures—Sec. **194 ***
- Lease acquisition costs—Sec. **178**

* Under Code Section **194**, a tax payer is allowed to expense up to $10,000 of qualified timber property reforestation expenses within a taxable year in which the qualified expenses are paid or incurred.

Section III: Depreciation for Financial Reporting

In this section:

For financial reporting purposes, a business uses depreciation methods dictated by **Generally Accepted Accounting Principles** (GAAP). A number of depreciation methods have been developed, and while each different method will provide the same opportunity to deduct the asset's basis over its assigned life, the various methods do so at different speeds. Deciding which method to use is left completely to the discretion of the individual business, based on whichever method makes the most sense considering the facts and circumstances surrounding the particular asset.

Three decisions need to be made for each depreciable asset:

- Salvage Value
- Useful Life
- Depreciation Method

Salvage value is the dollar amount that can be received for an asset when it is retired from service at the end of its useful life, less all removal and selling costs. A building, therefore, normally does not have a salvage value, since it is assumed that the costs of demolition will approximate the sales value of any scrap materials recovered. Salvage value is sometimes referred to as the asset's residual value and is obviously an estimated amount, based on past experience.

In determining an asset's useful life, the objective for financial reporting is to select the life that will most accurately reflect the asset's true economic usefulness. Past experience again will serve as the best guideline, and it is a good idea to periodically review these lives and revise them as needed. (For a detailed explanation on how this is handled, see "Revising an Asset's Estimated Life," page III-7.) Some businesses prefer to use the same life for financial reporting as dictated by the IRS for income tax reporting, simplifying their record keeping.

The final decision for depreciation is to choose an appropriate depreciation method. Each method has a distinctive pattern of allocating the asset's cost to the specific years of its life. For some assets their useful lives will expire uniformly over the passage of time. Other assets will prove to be most useful or productive in their early years, with a decline in value later. Finally, certain assets' usefulness varies in direct proportion to their amount of use, which may be irregular.

Note: Although you can choose different depreciation methods for different assets, once chosen you must be consistent and use the same method of depreciation over the asset's entire life. If you decide you want to change a depreciation method then you need to do so in accordance with the Accounting Principles Board Opinion No. 20.

Depreciation Methods for Financial Reporting

Straight-Line Method

The simplest and most commonly used depreciation method for financial reporting is the straight-line method, which records depreciation uniformly over the asset's life. Under this method, which is also the method used for amortization, the same amount of depreciation is taken each year. It is most appropriately used when an asset's depreciation relates more to time than to frequency of use and its operating efficiency is relatively constant over its useful life.

How To:

The equation for calculating straight-line depreciation is:

$$\frac{\textit{Acquisition Cost} - \textit{Salvage Value}}{\textit{Life in Years}} = \textit{Annual Depreciation}$$

Example: Equipment costing $15,000, with a salvage value of $1,000, and with a useful life of 7 years will have an annual depreciation deduction of $2,000:

Result:

$$\frac{\$15{,}000 - \$1{,}000}{7 \textit{ Years}} = \$2{,}000$$

Accelerated Methods

Accelerated depreciation methods allocate a higher cost to the early life of an asset and a smaller cost in later years. These methods are generally used with those assets whose efficiency and productivity decline as the assets age. The two most commonly used accelerated methods are declining-balance and sum-of-the-years'-digits.

Declining-Balance Methods

Under these methods, the **net book value** (acquisition cost less accumulated depreciation) is multiplied by a fixed rate. Because the net book value will be smaller each year (due to the annual increase in accumulated depreciation), the amount of depreciation will also be less each year. Although the salvage value of the asset is not deducted from cost when using this method, the asset cannot be depreciated below its salvage value.

The two most popular declining-balance methods are double or 200% declining and 1.5 or 150% declining. Double declining is equal to twice the straight-line rate, and 1.5 declining is equal to 1.5 times the straight-line rate.

How To:

The equation for calculating double declining-balance depreciation is:

$$\frac{\textit{Acquisition Cost} - \textit{Accumulated Depreciation}}{\textit{Life in Years}} \times 2 = \textit{Annual Depreciation}$$

Example: Machinery costing $15,000, with a salvage value of $1,000, and with a useful life of 10 years will have the following calculation for the first year it is placed in service:

Result:

$$\frac{\$15{,}000}{10} \times 2 = \$3{,}000$$

For the second year, the following calculation is made:

$$\frac{\$15{,}000 - \$3{,}000}{10} \times 2 = \$2{,}400$$

How To:

The equation for calculating 1.5 declining-balance depreciation is:

$$\frac{\textit{Acquisition Cost} - \textit{Accumulated Depreciation}}{\textit{Life in Years}} \times 1.5 = \textit{Annual Depreciation}$$

Example: Using the same example as above, the calculation for the first year is:

Result:

$$\frac{\$15{,}000}{10} \times 1.5 = \$2{,}250$$

For the second year, the following calculation is made:

$$\frac{\$15{,}000 - \$2{,}250}{10} \times 1.5 = \$1{,}912$$

When using a declining-balance method, it is possible during an asset's life to change to the straight-line method. There are two reasons you may decide to do this:

- When using a declining-balance method, you will never completely depreciate the asset. If the asset does not have a salvage value, you may want to be able to completely write the asset off by depreciating it fully.
- Since the depreciation amounts calculated under declining-balance become progressively smaller near the end of the asset's life, you may feel at some point that this no longer accurately reflects the proper allocation of costs to income.

Note: At some point in the asset's life (generally around the midpoint), the amount of depreciation calculated according to straight-line will be greater than that calculated under the declining-balance method. If the change to straight-line depreciation is made, it will, therefore, result in a greater total depreciation deduction.

This switch to the straight-line method is sometimes referred to as the Remaining Value Over Remaining Life. Notice that here the asset's salvage value is deducted out, since you are using a form of straight-line depreciation.

How To:

The equation for switching to straight-line depreciation when either the double declining-balance or 1.5 declining-balance method is used is:

$$\frac{\textit{(Acquisition Cost – Accumulated Depreciation) – Salvage Value}}{\textit{Remaining Useful Life in Years}}$$

The usual time to make this switch to straight-line is when the calculated depreciation under the straight-line method will exceed the amount calculated under the declining-balance method. To give you an estimate of the time period when this occurs, depending on which method of declining-balance was used, see the chart below (salvage value is ignored here):

	Year to Switch to Straight-Line	
Original Useful Life	**1.5 Declining-Balance**	**Double Declining-Balance**
10 years	5	7
20 years	8	12
25 years	10	14
30 years	12	17
35 years	13	19

Example: Assume an asset costing $5,000, with no salvage value, and with a useful life of 5 years, is being depreciated under the double declining-balance method, but the owner wants to switch to the straight line method as soon as it will produce a greater amount:

Year	Cost	Less Accumulated Depreciation	Equals Net Book Value	Double Declining-Balance (DDB)	Switch to Straight-Line
1	5,000	N/A	5,000	2,000	Use DDB
2	5,000	2,000	3,000	1,200	Use DDB
3	5,000	3,200	1,800	720	Use DDB
4	5,000	3,920	1,080	432	540
5	5,000	4,352	648	259	540
			Total Depreciation =	$4,611	$5,000

Example: Assume the same example as above, but with a salvage value of $300. In this case, when switching in the fourth year to straight-line, the depreciation expense for the last 2 years would be $390 each year for a total depreciation over the asset's life of $4,700.

Result:

$$\frac{(\$5{,}000 - \$3{,}920) - \$300\ (\text{Salvage})}{2\ \text{Years remaining life}} = \$390$$

Total depreciation, therefore, will be:

Years 1–3 (using double declining-balance)	=	$3,920
Years 4–5 (using straight-line) $390 + $390	=	780
		$4,700

Sum-of-the-Years'-Digits Method

Another accelerated depreciation method is the sum-of-the-years'-digits method. This method gives almost as high deductions as the double declining-balance method. With this method, however, although the amount of depreciation decreases each year, it allows the user to write off the entire asset's basis less any salvage value.

How To:

$$\text{Cost less Salvage Value} \times \frac{\text{Useful life remaining}}{\text{Sum-of-the-years'-digits}} = \text{Annual Depreciation}$$

The “sum-of-the-years’-digits” is defined literally. The sum-of-the-years’-digits for an asset with a 3-year life is 6, computed as follows:

Year $\underline{1}$ + Year $\underline{2}$ + Year $\underline{3}$ = $\underline{\underline{6}}$

Example: The formula to compute the first year’s depreciation on a \$500 asset, with a salvage value of \$50, and a life of 5 years is used as follows:

Year 1:

$$(\$500 - \$50) \times \frac{5}{1 + 2 + 3 + 4 + 5\ (=15)} = \$150$$

Year 2:

$$(\$500 - \$50) \times \frac{4}{1 + 2 + 3 + 4 + 5} = \$120$$

Year 3:

$$(\$500 - \$50) \times \frac{3}{1 + 2 + 3 + 4 + 5} = \$90$$

How To:

As illustrated, the numerator decreases every year, while the denominator stays the same. There is a shortcut, however, for determining the sum-of-the-years’-digits amount to be used as the denominator in the above formula:

Where *n* represents the life in years:

$$\frac{n\,(n + 1)}{2}$$

Example: If the life of the asset is 51 years, the sum of its digits, to be used as the denominator, is 1,326:

$$\frac{51\,(51 + 1)}{2} = 1{,}326$$

Production or Use Methods

Production or use methods do not relate to the passage of time and, therefore, do not relate to years of life. These methods relate to usage patterns and recognize that some assets, such as certain machinery, will depreciate more rapidly the more they are used. These are excellent methods for a seasonal business, for example, which may run its machinery at times 24 hours a day and at other times, only 9 hours a day.

Service-Hours Method

When using the service-hours method, an asset's useful life or service life is estimated in terms of the number of hours of use rather than in terms of years or months.

How To:

The equation for calculating service-hours depreciation is:

$$\frac{\textit{(Cost less Salvage)} \times \textit{Hours used this year}}{\textit{Total Estimated Hours in asset's life}} = \textit{Annual Depreciation}$$

Example: Assume an asset costing $60,000, with a $6,000 salvage value, and a productive life in hours of 20,000, is used 3,000 hours during its first year:

Result:

$$\frac{(\$60{,}000 - 6{,}000) \times 3{,}000}{20{,}000} = \$8{,}100$$

This method could be used just as easily for a vehicle that you want to depreciate according to actual miles driven each year. To do so you would substitute miles for hours in the above formula and would estimate the total miles expected to be driven over the vehicle's life.

Productive-Output Method

Under this method, also referred to as the Units-of-Production method, depreciation will vary according to output. This method is very similar to the service-hours method, but measures an asset's useful life in terms of units of product rather than hours of use.

How To:

$$\frac{\textit{(Cost less Salvage)} \times \textit{Units of Product produced this year}}{\textit{Total Estimated Units to be produced during asset's life}} = \textit{Annual Depreciation}$$

Example: Assume an asset costing $60,000, with a salvage value of $6,000, that is expected to produce 10,000 units over its useful life, produces 2,000 units during its first year of use.

Result:

$$\frac{(\$60{,}000 - \$6{,}000) \times 2{,}000}{10{,}000} = \$10{,}800$$

Revising an Asset's Estimated Life

For financial reporting purposes, you **should** change the life of an asset if the life that was originally assigned becomes inaccurate. Unlike tax reporting, where assets are depreciated over prescribed lives, an asset's estimated life for financial reporting is, by definition, only an estimate. When assigning a life to an asset, the goal in financial accounting is to select a life that best reflects the asset's true economic usefulness. In other words, for what period of time will the asset contribute to the production of income?

Changes in estimate are a normal part of operating a company. With even the most experienced estimate, there are times when you need to revise a life originally chosen for an asset. New or better information may become available, or new events may occur.

Below are some examples of circumstances that can cause an asset's life to require revision:

- New technology can easily render an asset obsolete.
- Improper maintenance can shorten an asset's life, whereas improved standards of maintenance may lengthen its life.
- An asset may be accidentally damaged or broken.
- A work stoppage (a strike or other cause) may render an asset temporarily idle and, thus, prolong its life.
- Unscheduled overtime may cause an asset to wear out earlier than originally expected.
- Improvements made to an asset may extend its life.
- A management decision to relocate a business may result in the early retirement of an asset or building.

It is recommended, therefore, that the lives of a company's assets be reviewed periodically, and revised when necessary. When a change is needed, it should not be accounted for retroactively. Opening balances should *not* be adjusted, and no attempt should be made to "catch up" or change prior periods. Since changes in accounting estimates are a continual process, they should be prospective.

How To:

If it is necessary to revise an asset's life:

1. Determine the asset's remaining value:

   Acquired Value less Accumulated Depreciation
   (less any salvage value if using straight-line depreciation).

2. Determine the asset's remaining estimated life.
3. Resume depreciating the asset using the asset's remaining value and remaining life calculated in Steps 1 and 2, using the same method.

In accordance with FASB ASC 250-10-50, you are required to make a note to the company's financial statements in the year of the change *and in future years that are* *affected*. The note should state that a change in estimate has occurred and it should include:

- A description of the change.
- The effect of the change on income before extraordinary items, net income, and related per share amounts.

Example: Super Sage, a calendar-year company, acquired a "SLOW" machine on January 1, 2003. The machine cost $10,000, was assigned a slow 10-year life, and was depreciated using the straight-line method. After using the SLOW machine for 4 years, there was a technological breakthrough in the marketplace. In 2007 a "FAST" machine was developed and was widely marketed. Naturally, Super Sage wanted to purchase the faster "FAST" machine and so decided it would use the "SLOW" machine only through the end of the next fiscal year of 2008. At that time it would abandon it (or sell it to a slower company). Because of this decision, it is necessary to change the asset's life from 10 years to 6 years.

Result:

Years 1 through 4 (2003–2006):

$$\frac{\$10{,}000}{10} = \text{\$1,000 depreciation expense each year for the first 4 years}$$

Years 5 and 6 (2007–2008): To calculate depreciation on the asset with its new life of 6 years, use the asset's remaining value and divide it by the asset's remaining life of 2 years:

$$\frac{\$10{,}000 - \$4{,}000}{2} = \text{\$3,000 depreciation expense each year for the last 2 years}$$

With the above calculation the SLOW machine will be fully depreciated in 6 years.

Depreciation for Partial Periods

Very few assets are purchased on the first day of the year and are disposed of on the last day of a year. Rather, asset acquisitions and dispositions generally occur throughout the year. Management commonly develops a depreciation policy that simplifies the allocation of depreciation to accounting periods, so that a daily allocation isn't necessary. Three common period allocation methods, commonly called "averaging conventions," are illustrated below.

1. **Modified mid-month convention.** Compute depreciation on the basis of the nearest whole month. Assets **placed in service** on or before the 15th day of a month receive a full month's depreciation, whereas those assets **placed in service** after the 15th day receive no depreciation for that month.

If the asset is **disposed** of on or before the 15th day of the month, no depreciation is taken for that month, whereas if **disposed** of after the 15th day, a full month's depreciation is taken.

Example: A 5-year asset, costing $10,000, with no salvage value, placed in service 5/12/2004 and disposed of 6/9/2007, is depreciated using the straight-line method, by a **calendar-year** taxpayer.

Result:

$$\frac{\textit{\$10,000 Cost}}{\textit{5-Year life}} = \textit{\$2,000} = \textit{Annual Depreciation}$$

Year Ending	Current Depreciation	Accumulated Depreciation
12/31/2004	$2,000 x 8/12 = $1,333	$1,333
12/31/2005	$2,000	$3,333
12/31/2006	$2,000	$5,333
12/31/2007	$2,000 x 5/12 = $833	$6,166

Example: Now assume the same asset as above, but change its date placed in service to 5/25/2004 and its disposition date to 6/16/2007.

Result:

Year Ending	Current Depreciation	Accumulated Depreciation
12/31/2004	$2,000 x 7/12 = $1,167	$1,167
12/31/2005	$2,000	$3,167
12/31/2006	$2,000	$5,167
12/31/2007	$2,000 x 6/12 = $1,000	$6,167

2. **Full-month convention.** Compute depreciation in full month increments only. Assets **placed in service** at any time during a given month will receive a full month's depreciation in that month.

   If, before the end of its depreciable life, the asset is disposed, no depreciation is allowed for the month in which the asset is disposed.

   Example: Similar to above, assume a 5-year asset, costing $10,000, with no salvage value, placed in service 5/30/2004 and disposed of 6/25/2007.

Result:

Year Ending	Current Depreciation	Accumulated Depreciation
12/31/2004	$2,000 x 8/12 = $1,133	$1,133
12/31/2005	$2,000	$3,333
12/31/2006	$2,000	$5,333
12/31/2007	$2,000 x 5/12 = $833	$6,166

3. **Half-year convention.** All assets either **placed in service** or **disposed** of before the end of their depreciable lives, receive one-half year's depreciation. At all other times, assets receive a full year's depreciation.

   Example: As above, assume a 5-year asset, costing $10,000, with no salvage value, placed in service 5/12/2004 and disposed of 6/9/2007, is depreciated using the straight-line method, by a calendar-year taxpayer.

   Result:

Year Ending	Current Depreciation	Accumulated Depreciation
12/31/2004	$2,000 x 1/2 = $1,000	$1,000
12/31/2005	$2,000	$3,000
12/31/2006	$2,000	$5,000
12/31/2007	$2,000 x 1/2 = $1,000	$6,000

FASB ASC 740 (formerly FAS 109) and Depreciation

It is not unusual for there to be differences in the depreciation methods used for financial and tax reporting purposes. This is one of the most common causes of the differences in the amount of net income reported for tax purposes and the amount of net income reported for financial statement purposes. Some of these differences are the result of reporting transactions in different years (for example, accrual accounting versus cash basis or recognizing revenue at the time of sale versus installment sale accounting). Tax reporting follows prescribed laws and regulations, whereas financial reporting represents compliance with GAAP (Generally Accepted Accounting Principles).

Although differences in the current period do not always affect future periods, quite often they do. Such differences can result in an increase or decrease in a future tax liability. You handle this for financial reporting purposes by complying with FASB ASC 740, *Income Taxes*. The basic tenet of ASC 740 is that you must reflect future tax consequences for past transactions. This is accomplished by establishing deferred tax assets and deferred tax liabilities; also known as deferred tax accounting.

Note: "FASB" is an abbreviation for the Financial Accounting Standards Board. "FAS" is an abbreviation for Financial Accounting Standard. FAS 109 is effective for tax years beginning after December 15, 1992. It superseded FASB 96. The standards FASB ASC 740 covers Income Taxes.

Some causes of reporting differences are permanent, while others are temporary. If an item is deductible for financial purposes, but not for tax purposes, *and if it will never be deductible for tax purposes*, it is a permanent difference; for example, a fine due to a parking ticket. A temporary difference occurs when the reporting difference eventually reverses itself. This happens when differences are eliminated at the completion of the transaction or event. This is sometimes referred to as a **timing difference**.

Differences in depreciation expense between financial and tax reporting are always temporary. For example, if you are depreciating a $100 asset that does not have any salvage value, you will eventually claim $100 of depreciation expense, regardless of the depreciation method being used. If you are depreciating this asset using the straight-line method, you will expense an equal amount each year. If you are depreciating this same asset using the double-declining balance method, and later switching to straight-line, you will expense more of the asset in its early years and less later. However, both methods of depreciation will allow you to claim $100 of depreciation expense over the asset's life. Therefore, any differences created between the two sets of books, caused by the different depreciation methods, ultimately are reversed.

Of the possible causes of differences between financial reporting and tax reporting, depreciation expense is the most common. This is because most businesses have depreciable assets and use different depreciation methods, as well as different lives, for the two reporting purposes. Tax reporting mainly uses ACRS and MACRS, while financial reporting frequently uses straight-line depreciation. Tax reporting uses a prescribed recovery period for depreciation, while financial reporting uses a realistic useful life.

Example: For financial purposes, an asset costing $12,000 is depreciated using the straight-line method and a 6-year life. For tax purposes, the same asset is depreciated using MACRS with a 5-year recovery period. Eventually $12,000 of depreciation expense will be claimed for both tax and financial reporting. However, in the early years, tax reporting claims more depreciation than financial reporting. While in later years, financial reporting claims more depreciation than tax reporting. The table below illustrates how these differences are eliminated.

	Financial Reporting	Tax Reporting	Difference
Year 1	$ 2,000	$ 2,400	$<400>
Year 2	2,000	3,840	<1,840>
Year 3	2,000	2,304	<304>
Year 4	2,000	1,382	618
Year 5	2,000	1,382	618

	Financial Reporting	Tax Reporting	Difference
Year 6	2,000	692	1,308
Total Depreciation Expense	$12,000	$12,000	0

Temporary differences represent future tax consequences. The tax consequences of these differences (i.e., the expected future income or deduction from an event multiplied by the appropriate tax rate) may be set up on the financial statements as either a:

- Deferred tax liability, or
- Deferred tax asset.

Deferred Tax Liability

A deferred tax liability is established when temporary differences result in future taxable amounts. If this occurs, the income tax expense shown on the financial statements has two components: current tax expense, which is indicated by an *Income Taxes Currently Payable* account, and future tax expense, which is indicated by a *Deferred Tax Liability* account. In the previous example, a deferred tax liability account must be established. Since during the last three years of the asset's life, the depreciation expense for tax reporting is less than the depreciation expense for financial reporting, a future taxable difference is created. In the future, the current temporary difference results in a taxable difference.

Deferred Tax Asset

A deferred tax asset is established when a temporary difference or a tax attribute (such as a loss carryforward or tax credit) results in a future tax reduction. After establishing the deferred tax asset account, you must evaluate the probability that it will result in a future tax benefit. It is said to be "more likely than not" to be realized when it has a 51% or greater probability of becoming a future tax benefit. If a portion of the deferred tax asset account does not meet the "more likely than not" test, then you must also establish a valuation allowance or contra account to offset it. A deferred tax asset can occur when you are using a more accelerated depreciation method for financial reporting (double-declining balance with a shorter life) and a slower method (ADS, Alternative MACRS) for tax reporting. A benefit only occurs if there is taxable income in the future that can be offset.

Disposed Assets

A frequently asked question concerns the treatment of disposed assets when setting up a deferred tax account. If, prior to its disposal, an asset is being depreciated differently for financial and tax reporting purposes, the reversal of any remaining temporary difference is accelerated and recognized upon the asset's disposal. Since there are different amounts of depreciation expense taken to date, the basis of the asset will be different for tax versus financial reporting purposes. This, in turn, causes a different gain/loss amount to be reported on the two sets of books. When this is netted with accumulated depreciation the timing difference is resolved.

Example: Assume that an asset costing $100 has $30 of accumulated depreciation for tax reporting and $20 of depreciation for financial reporting. It is sold for $90.

Result:

	Tax Reporting	**Financial Reporting**
Depreciation (expense) =	$<30>	$<20>
Gain on sale (income) =	20	10
Net (income less expense) =	$<10>	$<10>

Establishing a Deferred Tax Account

When setting up a deferred tax account, you must include the effect of depreciation differences on it.

How To:

To calculate the differences in depreciation for financial and tax reporting purposes and to set up a deferred tax account, there are several steps you should take:

1. Project depreciation for future years for all assets, both for tax reporting and financial statement reporting. Calculate the difference between tax and financial depreciation for each year. (The projection will also show you when the differences will be reversed.)
2. Eliminate any depreciation expense for any assets that you know will be disposed of in a given year (see above explanation).
3. Multiply the annual difference by the expected tax rate for each year. In most cases, this will be a deferred tax liability account as it is much more common for assets to be depreciated under a more accelerated method for tax reporting than for financial reporting.
4. Set up a deferred liability account by making the following journal entry:

   Current income tax expense

   Income tax expense - deferred

       Deferred tax liability

       Income taxes currently payable

Example: Let's continue with our earlier example of the $12,000 asset. Assume a consistent future tax rate of 15%. Assume this is the first year of business and that the current year tax liability (after deducting the current $2,400 of depreciation expense (see Year One in the example)) is $640. In comparing the differences between financial and tax depreciation, we compute the following deferred tax amount in the first year of the asset's life (to project *forward* we, therefore, start with the second year):

Year 2:	$<1,840> ($2,000 financial depreciation less $3,840 tax depreciation) x 15%	=	$<276>
Year 3:	$<304> x 15%	=	$ <46>
Year 4:	$618 x 15%	=	$ 93
Year 5:	$618 x 15%	=	$ 93
Year 6:	$1,308 x 15%	=	$ 196
	Total deferred taxes in the first year		**$ 60**

The amount of the deferred liability account as it is initially established is $60. It will be increased in the next two years and will be decreased every year thereafter. In the sixth year the liability account will be completely eliminated. The Deferred Tax Account would appear as follows (the year of each entry is noted):

Deferred Tax Liability

Year 4:	93	Year 1:	60
Year 5:	93	Year 2:	276
Year 6:	196	Year 3:	46

The journal entry made in the first year is:

Current income tax expense	640	
Income tax expense - deferred	60	
Deferred tax liability		60
Income taxes currently payable		640

(To set up the deferred tax liability and to record the current year's tax liability and expense.)

The deferred tax liability account, therefore, reflects the future tax consequences of whatever differences exist at the end of each year between financial and tax depreciation. As the temporary difference eventually reverses itself, the deferred tax liability account is gradually eliminated.

Financial Reporting: A Summary

The goal in the financial reporting of fixed assets is to find a depreciation method, approved by GAAP, that will most realistically reflect their demise. While trying to attain the fairest presentation, all decisions, at best, are going to be based on estimates: estimates as to useful life and estimates as to what portion of that determined life will be used up in any one period. For financial reporting purposes, you should periodically review the lives assigned to your fixed assets. If a life originally assigned to an asset is no longer accurate, you need to revise it according to FASB ASC 250.

As you will see in Section IV of this guide, completely different depreciation methods, as well as useful lives, for fixed assets may be used in computing depreciation for tax purposes. Such differences must be reconciled according to ASC 740 and a deferred tax account will need to be established.

Section IV: Depreciation for Income Tax Reporting

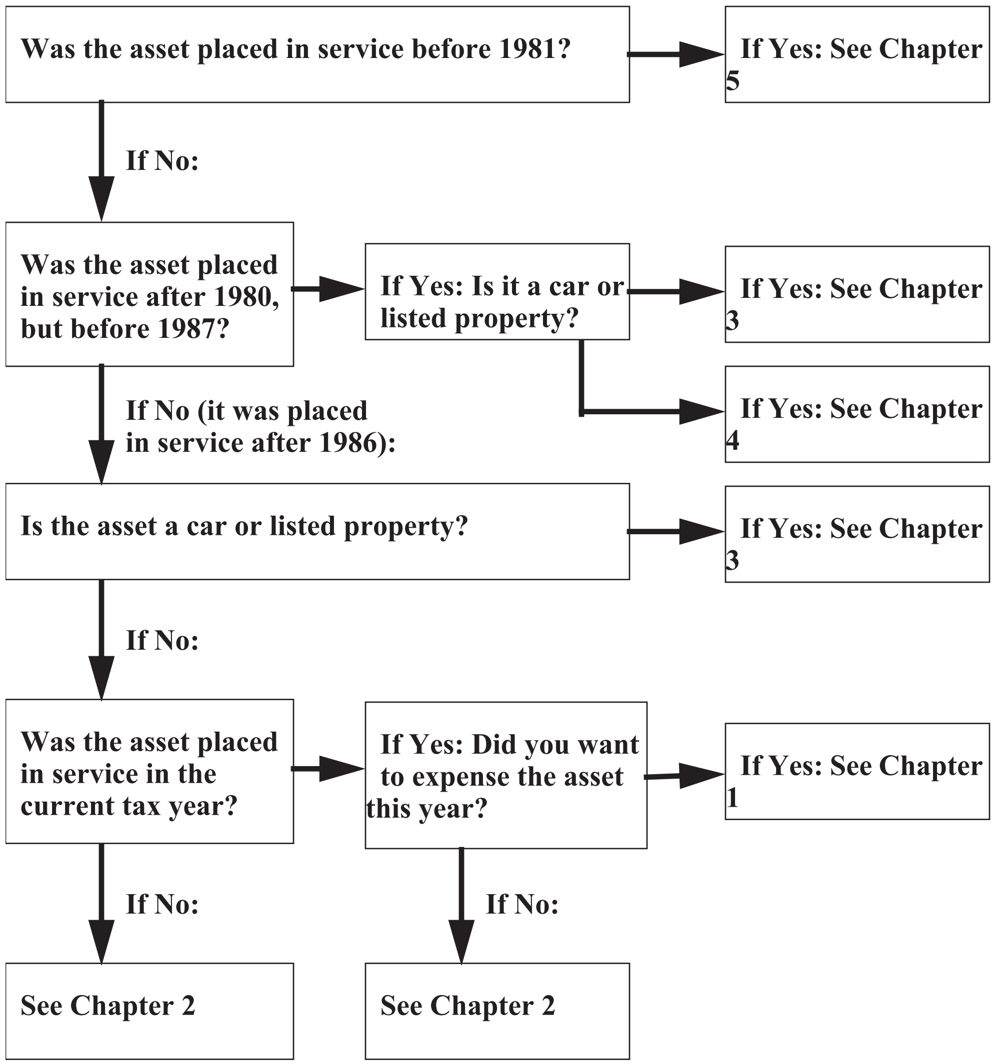
Unlike financial reporting, the depreciation methods and lives used by a business to record depreciation on fixed assets for income tax reporting purposes are set by the Internal Revenue Service (IRS). Some alternatives are available whereby the taxpayer may be able to choose between two different methods and/or lives. When this occurs, the choice will be between an accelerated method with a fairly short life and a slower method with a longer life. However, the taxpayer's choices are much more limited than if he was selecting a depreciation method or life for financial reporting purposes.

Essentially, the depreciation methods used for income tax reporting purposes are all based on the same methods used for financial reporting and explained in Section III: "Depreciation for Financial Reporting." Thus, while called by various acronyms (ACRS, MACRS, etc.), the depreciation methods prescribed by the IRS are founded on either straight-line depreciation or a declining-balance method.

The key to unlocking the puzzle of which depreciation method and life to use for any fixed asset is the **date on which the asset is placed in service**. At this point you may need to pause and review the "Elements of Depreciation," page I-7, for an explanation of how the date placed in service is determined.

Remember: The date placed in service is *not* necessarily the same date as the date on which the asset was acquired!

The following chart will refer you to the appropriate chapter in this Section of the guide that will provide you with a clear understanding of the available choices for depreciating any fixed asset:



Before moving on to the appropriate chapter, there are several matters of importance, as well as terminology, with which you need to become familiar.

For all depreciable property placed in service after 1980, we are no longer concerned with useful lives, but rather with "recovery periods." Recovery periods are 12-month periods and are not based on tax years. They are not elective, but rather are prescribed by statute according to property type. Recovery periods are generally shorter than the estimated useful lives used in other depreciation methods. Depreciation is now referred to as a deduction for "cost recovery."

There are also certain IRS rules that determine how depreciation is prorated for the year in which an asset is placed in service, as well as for the year in which an asset is disposed of (if it is disposed of before the end of its depreciable life). These are referred to as "**averaging conventions**," some of which were explained in Section III of this guide under financial reporting requirements. There are three principal averaging conventions used for tax reporting purposes. All of these averaging conventions will be further discussed in Section IV: "Chapter 2: Modified Accelerated Cost Recovery System (MACRS)."

1. **Half-year convention:** Under this convention, all assets either placed in service or disposed of before the end of their depreciable lives receive a half-year of depreciation. When you use this convention and the asset is held for its entire recovery period (and without any short years), a half-year of depreciation is allowed for the year *following* the end of the recovery period.

Note: The half-year convention is illustrated by an example in "Depreciation for Partial Periods," page III-9.

2. **Midmonth convention:** Under the midmonth convention, whatever day of the month an asset is either placed in service or disposed of, it is treated as if it occurred at the midpoint of the month.
3. **Midquarter convention:** This was created, along with MACRS, by the Tax Reform Act of 1986. Under this convention, 1 1/2 months of depreciation is allowed for the quarter of the year in which an asset is placed in service (a quarter of a year being 3 months).

The above-mentioned conventions are used for depreciable property placed in service after 1980. For property placed in service prior to 1981, you may choose to use the half-year convention, compute to the nearest whole month, or calculate the actual days in use. Averaging conventions are prescribed for assets depreciated under MACRS or ACRS, but are optional for **nonrecovery property** (i.e., property acquired before 1981).

As in financial reporting, once a depreciation method is chosen, it must be used consistently for the asset's entire depreciable life. To make a change for an asset placed in service prior to 1987, it is usually necessary to apply for a change of accounting method with the IRS. An asset placed in service in 1987 or later, however, is being depreciated under MACRS, and the various depreciation elections made can never be changed.

Note: You are permitted to change a depreciation method without the permission of the IRS when changing to straight-line depreciation from a declining-balance method on a pre-1981 asset, and only if done on an original (not an amended) tax return. For two other times when you can change a depreciation method without the prior approval of the IRS, see also "Principles for Calculating Depreciation for Nonrecovery Property," page IV-120. In addition, if you have claimed less depreciation than the allowable amount, there is now an automatic consent procedure for correcting this. See "Allowed or Allowable Depreciation," page V-2.

If you are using a 52/53-week accounting cycle, depreciation is calculated the same as if it were a taxable year consisting of 12 calendar months. However, when a tax rule's effective date is expressed in terms of a tax year beginning or ending on a specific date that is the first or last day of a month, the 52/53-week year is deemed to start and end as follows:

- Begin on the first day of the calendar month that begins nearest to the first day of that tax year, and
- End on the last day of the calendar month that ends nearest to the last day of that tax year.

Example: Consider a year that begins on 5/29/07 and ends on 6/3/08. For certain provisions of the tax code, such year is treated as beginning on 6/1/07 and ending on 5/31/08.

Section IV: Chapter 1: First-Year Expensing

In this section:

For tax reporting purposes, there are several options available for expensing part or all of an asset's cost in the year in which it is placed in service.

First, effective in 2014, there is a de minimis safe harbor rule allowing businesses to deduct items of qualifying property as long as they cost $5,000 or less each and certain other requirements are met.

A second option is to expense part of an asset's cost in the year in which it is placed in service under IRS Code Section 168(k). Code Section 168(k) allows an additional first-year amount of depreciation referred to as "bonus depreciation" to be claimed on certain qualifying property. The provision for bonus depreciation is currently only temporary.

A third option is to elect to deduct part or all of the cost of qualifying property under IRS Code Section 179. There are specified dollar limits based on the year in which the property is placed in service, as well as other restrictions.

De Minimis Safe Harbor Rule

Sometimes an asset might meet all of the requirements of a depreciable asset, and yet the asset is not capitalized because its cost fails to exceed the capitalization threshold the company has established for its business. For tax reporting purposes, tangible property regulations that became effective on January 1, 2014, have codified what had previously been tacitly understood and practiced by most companies. There is now a de minimis safe harbor election available whereby a taxpayer may deduct up to $5,000 of the cost of any item of property. The $5,000 amount is per item or per invoice, as long as the business has the following:

- An applicable financial statement,*
- Written accounting procedures for expensing amounts paid for such property under a specified dollar amount (or for property with an economic useful life of 12 months or less), and
- The taxpayer must expense such amounts on their financial statements in accordance with these procedures.

Note: An "applicable financial statement" (AFS) is one that is provided to a federal or state government (or agency), filed with the Securities and Exchange Commission, or is a certified audited financial statement used for credit or reporting purposes.

Beginning January 1, 2016, companies without an AFS may use the de minimis safe harbor to expense up to $2,500 per asset or invoice as long as there are written accounting procedures in place for expensing amounts paid for such property under a specified dollar amount (or for property with an economic useful life of 12 months or less).

Note: This is an increase from the $500 threshold amount originally issued under the tangible property regulations that became effective on January 1, 2014. The IRS will not challenge amounts deducted up to the $2,500 threshold in tax years prior to 2016, as long as the company otherwise satisfies the safe harbor requirements.

"Qualifying property" does *not* include inventory, land, and certain rotable, temporary, and standby emergency spare parts.

The expressed limit of $5,000, or $2,500 without an AFS, is a safe harbor only. It is possible that this limit may be exceeded and allowed by the IRS, depending on the facts of the case.

If the cost of an item exceeds the applicable limit (either $5,000 or $2,500, depending on the circumstances), then no portion of the item's cost is allowed to be expensed under the safe harbor rule.

The de minimis rule is a safe harbor that is elected annually by attaching a statement to the taxpayer's tax return for the year of the election. When the election is made, it applies to *all* qualifying property (and materials and supplies) and it is irrevocable.

Section 179 Expense

If a business has qualifying depreciable property, it may elect to expense all or part of it in the year in which it is placed in service. This is referred to as a Section 179 expense deduction, per IRS Code Section 179.

The Section 179 expense deduction, when taken, replaces depreciation. Therefore, when determining the depreciable basis of an asset, you need to first subtract out any Section 179 expense claimed on that asset.

The taxpayer has several different options when electing the Section 179 expense. For instance, the taxpayer may choose to expense only part of an asset and depreciate the remaining basis. The taxpayer may elect to expense the maximum amount of Section 179 allowed or may choose to expense a lesser amount. And, finally, if the taxpayer has several assets that are placed in service during the same year and that qualify under Section 179, the taxpayer may divide the Section 179 expense among them.

How To:

The election to claim the Section 179 expense is done simply by taking the deduction on IRS Form 4562. This must be done on an original return, whether or not timely filed, or on an amended return filed before the due date of the original return, including extensions. You may *not* make the election on an amended return filed *after* the original return's due date (including extensions).

How To:

To apply for a revocation of the election, send a request for consent to the Commissioner of Internal Revenue, Washington, D.C. 20224 and include the taxpayer's name, address, taxpayer identification number, description of the property, and the reason for the request.

Note: Estates and trusts may *not* claim the Section 179 expense deduction.

Property Qualifying for the Section 179 Expense Deduction

Not all property eligible for depreciation is also eligible for the Section 179 expense deduction. To qualify under Section 179, it must be recovery property (personal property and certain real property qualifies), and be both purchased and *used* predominantly by an active trade or business. The Section 179 expense *may not* be claimed on assets that are only held for the production of income (IRS Code Section **212** property).

Note: For property placed in service prior to 1991 to qualify as Section 179 property, it needed to also qualify for the Investment Tax Credit (IRS Code Section **38**).

To be entitled to be expensed under Section 179, property must qualify by type, by use, and by how it is acquired.

To Qualify By Type

Section 179 property is depreciable property, which includes:

1. Tangible personal property.
2. Other tangible property (with the exception of buildings) that is used as:
   a. an essential part of a manufacturing, production, or extraction business, or as
   b. an essential part of a business that furnishes transportation, communications, electricity, gas, water, or sewage disposal, or is
   c. either a research facility or a bulk storage facility (if used for fungible goods, i.e., goods that are interchangeable) that is used in any of the activities stated in (a) or (b) above.
3. Any railroad grading or tunnel bore (defined in IRS Code Sec. **168(e)(4)**).
4. Storage facilities, other than buildings, used in the distribution of either petroleum or a primary product of petroleum.
5. A single-purpose agricultural or horticultural structure.
6. Computer software placed into service in tax years beginning after 2002.
7. Qualified real property which includes any qualified improvement property described in section 168(e)(6) and any of the following improvements to non-residential real property:
   a. Roofs
   b. Heating, ventilation, and air-conditioning property
   c. Fire protection and alarm systems
   d. Security systems

Note: A **single-purpose structure** is one that is specifically designed, built, and used only for a qualifying purpose. The qualifying purpose of an agricultural structure is to house, raise, and feed a particular type of livestock (including poultry) and its produce, as well as to house the equipment needed to be used for this purpose. The qualifying purpose of a horticultural structure is the commercial production of either plants or mushrooms.

TIP
If the taxpayer wants to elect the Section 179 expense on a single-purpose agricultural or horticultural structure, he must be careful not to disqualify such a structure based on its use. For example, if a greenhouse has a cash register in it and someone is in the greenhouse selling plants, this will make the greenhouse ineligible under Section 179, as it is no longer used for a single purpose.

To Qualify By Use

As stated earlier, to qualify under Section 179, the property must be used in the active conduct of a trade or business. However, sometimes an asset will be used for both business and personal use. When this occurs, it must be used *more than* 50% of the time in the business in order to qualify as Section 179 property. Also, only the business portion of the asset's basis will qualify for the expense.

Example: A business purchased an asset in the current tax year for $8,000. The asset is used 60% of the time in the business and 40% of the time for personal purposes.

Result: The Section 179 deduction is limited to the business-use percentage, or $4,800 (60% x $8,000).

Remember: If an asset that qualifies in all other ways under Section 179 is used 50% or less in a business, no part of its basis may be expensed.

To Qualify By How Acquired

In order to qualify under Section 179, the property must have been purchased, as long as it was not purchased from a related party. For this purpose, related parties include:

- Family members who are spouses, ancestors, or lineal descendents.
- A corporation and any shareholder who owns directly or indirectly more than 50% of the corporation's outstanding stock.
- A partnership and any partner who owns directly or indirectly more than 50% of the partnership.
- Any two members of a controlled group.

Note: For a more detailed listing of other relationships that will disqualify property from the Section 179 expense deduction, see IRS Code Section **267**.

Since only property that has been purchased qualifies, transactions that involve a trade-in of one asset for another receive special treatment. When a trade-in occurs, that part of the newly acquired asset's basis that reflects the value of the old asset traded in will *not* qualify for the Section 179 expense deduction.

Example: A new machine costing $8,000 is purchased for $5,000 cash and a trade-in of an old machine with an adjusted basis of $2,000, but with a trade-in allowance of $3,000.

Result: Although the asset's basis for depreciation will be $7,000 ($5,000 cash plus the $2,000 basis in the old machine), the amount of basis that may be expensed is only $5,000, or the amount that was paid in cash.

TIP

If a business wants to benefit in the current year from taking the Section 179 expense deduction, it may be better to sell an older asset rather than trading it in. In the above example, although the asset that was traded in had a fair market value of $3,000, or $1,000 more than its adjusted basis of $2,000, the difference between the fair market value and the asset's adjusted basis does not increase the new machine's depreciable basis. However, if the old machine had been sold, the higher fair market value would have created a taxable gain of $1,000, but it would have also had the following positive effects:

1. The new machine would now have a depreciable basis of $8,000, since, without the trade-in, the business would have had to pay $8,000 for it, and
2. If the business claimed the Section 179 expense deduction on the asset's new basis of $8,000, this would more than offset the taxable gain of $1,000 from the sale of the old machine and thus would reduce the business's taxable income.

Remember that the key to how property needs to be acquired in order to qualify for Section 179 is that it is *purchased*. If property that is being used for personal purposes is later converted to business use, it will *not* qualify for Section 179. This is both because the business entity did not purchase it and the classification of the property occurs in the first year it is placed in service.

Examples of Qualifying and Nonqualifying Property

Qualifying Property	Nonqualifying Property *
Office equipment	Buildings
Machinery	Paved parking lots
Transportation equipment	Fences
Refrigerators	Plumbing
Livestock	Wiring
Neon signs	Swimming pools
Display racks	Air-conditioning and heating units**
Gasoline storage tanks and pumps	Property used outside the U.S.

* The Protecting Americans from Tax Hikes Act of 2015 permanently expands the definition of qualified Code Section 179 property to include qualified real property, which is defined as qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property. The Tax Cuts and Jobs Act of 2017 sunsets the terms qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property and expands the definition of qualified improvement property.

** The Protecting Americans from Tax Hikes Act of 2015 allows air-conditioning and heating units to qualify as Section 179 property for tax years beginning after 2015.

Limits on the Amount of the Section 179 Expense Deduction

Dollar Limit

For 1982 through 1986, the maximum amount that could be deducted under Section 179 in any year was $5,000. For qualifying property placed in service after 1986 and in taxable years beginning before January 1, 1993, the maximum amount that could be expensed was $10,000 per year. Finally, for qualifying property placed in service in taxable years beginning after December 31, 1992, the maximum amount that can be expensed per year is shown in the following table:

Tax Year Beginning in	Maximum Section 179
1993 - 1996	$17,500
1997	$18,000
1998	$18,500
1999	$19,000
2000	$20,000
2001	$24,000
2002	$24,000

Tax Year Beginning in	Maximum Section 179
2003	$100,000
2004	$102,000
2005	$105,000
2006	$108,000
2007	$125,000
2008 - 2009	$250,000
2010-2015*	$500,000
2016**	$500,000
2017	$510,000
2018 and thereafter***	$1,000,000

* Legislation for fiscal years beginning in 2010 through 2015 allows an election to be made that would include up to $250,000.00 of real property in the definition of qualified Section 179 property eligible for immediate expensing. Specifically the real property must be qualified leasehold improvement property, qualified restaurant property, or qualified retail improvement property. The deduction on real property is subject to the same Section 179 phase-out rules for personal property and does not apply to nonresidential real or residential rental property. Remember if you elect to claim a Section 179 deduction on real property, then you must identify all qualifying property using the Qualified §179 Property check box on the §179/Bonus Details window in Asset Detail, in order to properly calculate the phase-out limits.

** The Protecting Americans from Tax Hikes Act of 2015 permanently extends the $500,000 limit, indexed for inflation. The $250,000 cap on qualified real property is eliminated for tax years beginning 2016.

*** To be indexed for inflation.

Five types of property have a higher maximum than shown in the table: qualified zone property used by a business in an enterprise zone, New York Liberty Zone property, GO Zone property, Kansas Disaster Zone property, and Qualified Disaster Zone property. These exceptions are covered under the topic "Miscellaneous Section 179 Rules," page IV-19.

Note: Before 1993, an asset's placed-in-service date determined which dollar limitation applied. For example, if an asset was placed in service in 1986, then the limit was $5,000. Beginning in 1993, the taxpayer's fiscal year, as well as the placed-in-service date, determines which limitation applies. For example, a fiscal year taxpayer with a year starting on 11/1/2009 and ending on 10/31/2010 is subject to the $250,000 Section 179 expense. Because the fiscal year in this example begins in 2009, the taxpayer's Section 179 expense is not eligible for the 2010 deduction of $500,000.

If the business has a short tax year, the full dollar limit still may be claimed. However, the maximum allowable amount of the Section 179 expense deduction may be limited by other factors.

Remember that when using a 52/53-week accounting cycle, you may need to determine the tax year's *deemed* start and end dates. (See Section IV: "Depreciation for Income

Tax Reporting.") For example, consider a year that begins on 12/29/2009 and ends on 1/2/2011. For this purpose, the year is deemed to begin on 1/1/2010 and end on 12/31/2010. Because Section 179 is increased to $500,000 for property placed in service in taxable years beginning in 2010, the increased amount would apply for the year.

Reduction in Limitation

The limitation described above for any taxable year should be reduced by the amount by which the cost of section 179 property placed in service during a taxable year exceeds:

Year	Investment Amount
1986 - 2002	$200,000
2003	$400,000
2004	$410,000
2005	$420,000
2006	$430,000
2007	$500,000
2008 - 2009	$800,000
2010 - 2015	$2,000,000
2016	$2,010,000
2017	$2,030,000
2018 and thereafter*	$2,500,000

*To be indexed for inflation.

Example: A corporation places in service machinery costing $2,100,000 in 2012.

Result: Since the cost of the property placed in service exceeds $2,000,000 by $100,000, the maximum possible amount of the Section 179 expense that may be claimed is also reduced by $100,000 to $400,000 ($500,000 maximum less $100,000).

TIP
If a business is investing in qualifying property and the total cost of that property exceeds the investment limit, it might be to the business's tax advantage to defer certain purchases to the following year, if possible, so that the maximum Section 179 expense deduction may be taken in the current year.

Taxable Income Limit

The total amount of Section 179 expense taken in any one year is limited to the amount of the entity's taxable income that year from the conduct of an active trade or business. Taxable income is calculated without regard to the Section 179 expense deduction or any net operating loss carryforward or carryback. Any amount of Section 179 expense that is claimed but cannot be deducted due to the taxable income limit may be carried forward.

Example: As in the previous example, a corporation places in service machinery costing $2,100,000 in 2012. The corporation's taxable income for the year is $50,000.

Result: Although the investment limit reduced the maximum possible amount deducted under Section 179 to $400,000, this amount is reduced still further to $50,000, due to the taxable income limit. The corporation may deduct $50,000 under Section 179 in 2012.

Limits Applied to Partnerships, S Corporations, and Controlled Groups

The dollar limitation, the investment limit, and the taxable income limit for the amount claimed under Section 179 apply to both the partnership and the partner level. In other words, a partnership may not claim and allocate to its partners more Section 179 expense than either the partnership's taxable income limit or its investment limit will allow, and never more than the maximum dollar amount. In addition, each year no partner may take more than the maximum allowable amount of Section 179 expense even if it was allocated to him.

The Section 179 amount is further restricted to the partner's individual taxable income limit for that year. The Section 179 expense for the partnership is a "pass-through" item to the individual partners. This means that although it is the partnership that claims the Section 179 expense, subject to the partnership's taxable income and investment limits, it is not taken as an expense by the partnership but is instead passed through to the partners. Furthermore, since the taxable income limitation applies to both entities, the partner can only deduct the Section 179 expense passed through to him provided that he meets the taxable income limitation on his personal return.

Note: For purposes of taking the Section 179 expense deduction, an individual's taxable income from the active conduct of a trade or business includes wages, tips, or other compensation earned as an employee.

The same rules that apply to the claiming of the Section 179 expense by a partnership and its partners also apply to an S corporation and to each of its shareholders.

TIP

An individual may be in several different partnerships and/or S corporations, whose tax returns are being prepared by different accountants. If this is the case, the accountants should be advised of the multiple ownership so as not to claim excess Section 179 expense for which the individuals would receive no immediate benefit.

When applying the dollar limitation, the investment limit, and the taxable income limit, all of the members of a controlled group are considered to be a single taxpayer (IRS Code **Sec. 179(d)(6)**). For this purpose a controlled group is defined under IRS Code Sec. **1563(a)**, except that the phrase "at least 80%" is replaced with "more than 50%"

each place it appears in IRS Code Sec. **1563(a)(1)**. If a consolidated return is filed, the parent corporation makes the allocation.

Automobile Limit

If the asset on which a business wants to take the Section 179 deduction is an automobile, the total amount that can be claimed on it is limited to the maximum depreciation allowance for luxury vehicles. For a complete discussion on the various depreciation limits placed on cars, see "Luxury Automobiles," page IV-82.

Carryover of Disallowed Section 179 Expense

If the full amount of the Section 179 expense deduction cannot be taken because of the taxable income limitation, any excess may be carried forward indefinitely.

Note: There is no carryover allowed if the amount of the Section 179 expense deduction is reduced because of the investment limit.

Example: In 2012, a corporation places in service equipment costing $8,000. The corporation wants to expense the entire cost. The corporation has taxable income, before any Section 179 expense, for 2012 of $7,000.

Result: The corporation may deduct $7,000 of Section 179 expense. The unused Section 179 expense of $1,000, not allowed because of the taxable income limit, may be carried forward to 2013 (IRS Code Section **179 (b)(3)**).

When the excess Section 179 expense is carried forward, the portion that is carried forward is subject to the taxable income limit for that year.

When carrying over an amount of disallowed Section 179 expense, the taxpayer may select the properties to which the carryover applies, as well as the portion of each property's Section 179 expense to be carried forward. If this is not done, it will be assumed that the disallowed amount will be apportioned equally to all assets on which the Section 179 expense was claimed in the current year. This is important when disposing of property on which the Section 179 expense was claimed but not actually expensed, as any outstanding carryover amount relating to the disposed property will increase the property's basis.

Since the taxable income limit applies at both the partnership level as well as the partner level, if the partnership does not have sufficient taxable income, it cannot allocate the Section 179 expense to the partners but instead must carry it forward at the partnership level. This also applies to S corporations and their shareholders.

If, however, the partnership or S corporation is able to pass through the Section 179 expense, but the partner (or S corporate shareholder) cannot deduct the full amount of the Section 179 expense allocated to him, he may carry the excess forward but must reduce his basis in the entity (the partnership or S corporation) by the full amount allocated to him, whether or not expensed. If a partner (or S corporate shareholder) disposes of his interest in the partnership (or S corporation), he will increase the basis of his interest in the entity by any outstanding carryover of the Section 179 expense.

TIP
Claiming the maximum amount of available Section 179 expense, even though the taxable income limit bars the deduction, can serve as a good tax planning tool for the following tax year. If the taxpayer expects to have taxable income the following year but has no plans for additional investment in any fixed assets, the carryover of the previous year's Section 179 expense will provide a useful deduction, reducing taxable income.

For tax years beginning in 2010 through 2015, qualified real property may expense up to $250,000 under Section 179. In addition, section 179 deductions attributable to qualified real property that are disallowed under the business income limitation may only be carried over to taxable years in which the definition of eligible section 179 property includes qualified real property. Thus, if a taxpayer's section 179 deduction for 2010 with respect to qualified real property is limited by the business income, such disallowed amount may be carried over through 2015. Any such amounts that are not used through 2015, plus any 2015 disallowed section 179 deductions attributable to qualified real property, are treated as property placed in service in 2015 for purposes of computing depreciation. The carryover amount before 2015 is considered placed in service on the first day of the 2015 taxable year.

Example: During 2010, Sample Company purchases a section 179-eligible equipment costing $100,000 and qualified leasehold improvements costing $200,000. Sample Company has taxable income limitation of $150,000. The maximum section 179 deduction Sample Company can claim for 2010 is $150,000, which is allocated pro rata between the properties, $100,000 to qualified leasehold improvements and $50,000 to equipment.

In 2011 through 2015, Sample Company has no asset purchases and no taxable income. The $100,000 carryover from 2010 attributable to qualified leasehold improvements is treated as placed in service as of the first day of the company's 2015 taxable year. The $50,000 carryover allocated to equipment is carried over to 2016 under section 179(b)(3)(B).

Section 179 Expense Recapture Rules

If a taxpayer elects to take the Section 179 expense deduction, the amount deducted is treated as depreciation for purposes of the **recapture** rules. This means that the amount expensed under Section 179 may need to be "recaptured," or treated as income, under certain circumstances.

Note: The amount of the Section 179 deduction recaptured is computed differently depending on the type of circumstance.

Sale of Section 179 Property

Any gain realized on the disposition of business property is treated as ordinary income (versus capital gain) to the extent of depreciation and the Section 179 deduction. If a business took the Section 179 deduction on a property and then sells that property on an installment sale, in the year of sale it must include as ordinary income *all* depreciation and Section 179 deduction taken on the property to the extent of any gain. This occurs even if no payments on the sale are received the first year.

Note: If an asset to be disposed has any outstanding Section 179 expense carryover attached to it (i.e., Section 179 expense was claimed but not deducted due to the taxable income limit), the amount of the Section 179 expense carryover is added back to the asset's basis before gain or loss on the transaction is computed. There is no recapture if none of the Section 179 expense claimed was actually deducted.

TIP

Knowing that all depreciation and Section 179 deduction taken on an asset must be reported as income to the extent of gain in the year an installment sale is made, it would be advisable to have the buyer make a first-year installment payment to at least cover the tax liability on the amount of gain to be recognized.

Change of Use of Section 179 Property

A change of use for property on which Section 179 expense has been claimed may also trigger the recapture rules. If such an asset either is no longer used predominantly for business use or is converted from being actively used in a trade or business to being held for the production of income, recapture may be required. Whenever any portion of the Section 179 expense has to be recaptured, it is treated as ordinary income in the year that the change of use occurs. In addition, the recapture amount is added to the basis of the property for computing future depreciation.

Note: Previously there was a limited recapture period for property placed in service before 1987. However, this has been amended and no longer applies.

If the business use of an asset falls to **50% or less** before the end of the asset's recovery period, Section 179 recapture occurs. However, since, in most cases, this will be listed property, the rules under IRS Code Section **280F(b)(2)** for recapture will apply. For a detailed explanation of how Section 179 recapture is handled for listed property, see "Depreciation Limitations on Listed Property," page IV-78, and its segment on "Predominant Use Test Failed in Year Property Is Placed in Service," page IV-79).

If such property is *not* listed property or if the property is converted from trade or business use to being held for the production of income, then recapture of Section 179 expense occurs as follows: The amount to be recaptured is the excess of the amount expensed under Section 179 over the amount allowable as depreciation for the current and prior tax years, computed as if no Section 179 expense had been taken.

How To:

	Amount of Section 179 expense claimed	
minus	Amount of depreciation that would have been allowable had Section 179 expense not been claimed (include current year amount)	( )
equals	Amount to be "recaptured," or claimed as ordinary income in the current year	

Note: When calculating depreciation recapture for property other than listed property, you use the depreciation amounts, including any Section 179 expense, for the current tax year and for the prior tax years. This is different from computing depreciation recapture for listed property. For the latter, you do not include the current year depreciation (i.e., the year in which the recapture is triggered) in the calculation.

Example: In 2002, XYZ Corporation places in service 5-year property costing $12,000 and elects to expense $10,000. The remaining $2,000 basis is depreciated under the MACRS method (explained in the next chapter). In 2003, XYZ converts the property from use in the XYZ business to being held for the production of income.

Result: Although still entitled to be depreciated, the property is now no longer qualified to be expensed under Section 179. Therefore, in 2003 the benefit derived from Section 179 is recaptured.

Amount of Section 179 expense claimed		$10,000
Amount of depreciation that would have been allowed on the expensed amount:		
2002: 20% x $10,000	= $2,000	
2003: 32% x $10,000	= 3,200	(5,200)
Amount to be recaptured		$ 4,800

Note: The other $2,000 of basis (remember that the property cost $12,000) is depreciated as usual in 2003 (i.e., 32% x $2,000 = $640). In 2004 XYZ may take the normal third-year depreciation amount on the entire $12,000 basis of the asset.

Example: Assume the same facts as above, with XYZ converting the property from being used in its business to being held for the production of income, except that in 2002 when the property was placed in service, XYZ elected to depreciate the remaining cost of the property ($2,000) under the straight-line method over the regular MACRS recovery period (explained in the next chapter).

Result:

Amount of Section 179 expense claimed		$10,000
Amount of depreciation that would have been allowed on the expensed amount*:		
2002: 10% x $10,000	= $1,000	
2003: 20% x $10,000	= 2,000	(3,000)
Amount to be recaptured		$ 7,000

* Since the unexpensed portion of $2,000 is being depreciated under the straight-line method, XYZ must compute depreciation on the expensed amount by also using the straight-line method.

Miscellaneous Section 179 Rules

The other issues that you need to aware of are:

1. Any amount expensed under Section 179 is excluded from the uniform capitalization rules of IRS Code Section **263A**.

2. As part of the Revenue Reconciliation Act of 1993, certain "**enterprise zone businesses**" (defined in IRS Code Sec. **1397B**) can claim an additional $20,000 of Section 179 expense for qualifying property ($35,000 for 2002 and later years). Therefore, for example, in 2007 the maximum amount of Section 179 expense for an enterprise zone is $160,000 ($125,000 of regular Section 179 expense and $35,000 of enterprise zone property). An enterprise zone business must meet certain criteria to ensure that it is an active, rather than a passive, business.

   Generally, all of the other provisions of IRS Code Section 179 are applicable. The one difference is when applying the phaseout for property costing more than $500,000 in 2009, you use only one-half of the amount of the cost of the qualified zone property (IRS Code Sec. **1397A**). The cost of Section 179 property that is *not* qualified zone property is not reduced.

3. The Job Creation and Worker Assistance Act of 2002 increased the Section 179 expensing limit by the lesser of (1) $35,000, or (2) the cost of qualifying **New York Liberty Zone** property placed in service in the taxable year.

   Qualifying property is property that otherwise qualifies for Section 179 expensing and was purchased and placed in service after September 10, 2001 and before January 1, 2007 for original use in the active conduct of a trade or business by the taxpayer in the New York Liberty Zone.

   As with enterprise zone property, use only one-half of the cost of the qualified NY Liberty Zone property when calculating the phase-out range for the investment limit.

   If the property ceases to be used in the New York Liberty Zone, the recapture rules under "Section 179 Expense Recapture Rules," page IV-16, apply.

4. The **Gulf Opportunity Zone** Act of 2005 increased the Section 179 expensing limit by the lesser of $100,000 or the cost of qualified property. The additional GO Zone Section 179 limit is not indexed for inflation as is the basic Section 179 limit of $100,000. Property purchased on or after August 28, 2005 and placed in service on or before December 31, 2008 for use in the active conduct of a trade or business by the taxpayer in a GO Zone qualifies.

   The Gulf Opportunity Zone of Act of 2005 also increased the $400,000 investment limitation by the lesser of $600,000, or the cost of qualified property placed in service during the tax year. Unlike enterprise zone and New York Liberty Zone property, use the entire cost of the qualified GO Zone property when calculating the phase-out range for the investment limit.

5. The 2008 Farm Act increases the amount that a taxpayer may elect to deduct under Section 179 by the lesser of $100,000 or the cost of qualified **Kansas Disaster Zone** property for the tax year. The threshold for reducing the amount expensed is increased by the lesser of $600,000, or the cost of qualified Kansas Disaster Zone property placed in service during the tax year. Neither the $100,000 nor $600,000 amounts are indexed for inflation. Property purchased from May 5, 2007 to December 31, 2008 for use in the active conduct of a trade or business by the taxpayer in a Kansas Disaster Zone qualifies.

6. The Emergency Economic Stabilization Act of 2008 provides that the maximum expense amount that can otherwise be deducted under Section 179 for the tax year is increased by the lesser of $100,000 or the cost of **qualified Disaster Zone** property. The beginning-of-phase-out amount otherwise in effect for the year is increased by the lesser of $600,000 or the cost of qualified Disaster Zone property placed in service during the tax year. Neither the $100,000 nor $600,000 amounts are indexed for inflation. Generally, property placed in service after December 31, 2007 for disasters declared after December 31, 2007 and occurring before January 1, 2010 qualifies.

7. The **American Taxpayer Relief Act of 2012** extended the increase in the amount of Section 179 that can be taken for qualified Enterprise Zone property through December 31, 2013. The provision increases the maximum dollar amount that can be deducted by the lesser of (1) $35,000 or (2) the cost of qualifying property placed in service during the year. This amount is in addition to the amount otherwise deductible under Section 179.

8. The **Taxpayer Increase Prevention Act of 2014** extended the increase in the amount of Section 179 that can be taken for qualified Enterprise Zone property through December 31, 2014. The provision increases the maximum dollar amount that can be deducted by the lesser of (1) $35,000 or (2) the cost of qualifying property placed in service during the year. This amount is in addition to the amount otherwise deductible under Section 179.

9. The **Protecting Americans from Tax Hikes Act of 2015** extended the increase in the amount of Section 179 that can be taken for qualified Enterprise Zone property through December 31, 2016. The provision increases the maximum dollar amount that can be deducted by the lesser of (1) $35,000 or (2) the cost of qualifying property placed in service during the year. This amount is in addition to the amount otherwise deductible under Section 179.

Section 179A Expense Deduction

There is an expense deduction for clean-fuel vehicles and certain refueling property. IRS Code Section **179A** was created by the Energy Policy Act of 1992. It is similar to the Section 179 expense deduction in that it is taken in the year in which the property is placed in service and it reduces the asset's basis. (We have included IRS Code Section 179A in Section VII: "Quick Reference.")

Qualifying Property

In order to qualify for the deduction, such property must meet ***all*** of the following requirements:

- It must be new property.
- It must have been placed in service after June 30, 1993, and before January 1, 2006.
- It must be used in a trade or business or for the production of income if it is refueling property (for a vehicle this is not necessary).
- It must either use, store, or dispense "clean-burning fuel."

"Clean-burning fuel" is any of the following:

- Natural gas.
- Liquefied natural gas.
- Liquefied petroleum gas.
- Hydrogen.
- Electricity.
- Any fuel that is at least 85 percent methanol, ethanol, any other alcohol, and/or ether.

Certain types of property are mentioned specifically in IRS Code Section 179A as not qualifying for the expense deduction. The amount of an asset's cost that is expensed under the regular Section 179 and an electric vehicle that qualifies for the 10% credit under IRS Code Section **30** do not qualify (for an explanation of Section 30, see "Section 30: Tax Credit for Qualified Electric Vehicles," page IV-69). In addition, no Section 179A deduction is allowed with respect to property used by a governmental unit, used by certain tax-exempt agencies, or used predominantly outside the United States. Finally, qualified refueling property does not include buildings or their structural parts.

Limitations on the Amount of Section 179A Expense Deduction

The cost of a qualifying vehicle that may be expensed under Section 179A may not exceed:

- $50,000 if it is a truck or van with a gross vehicle weight of over 26,000 pounds or if it is a bus with a seating capacity of a least 20 adults (*not* including the driver).

- $5,000 if it is a truck or van with a gross vehicle weight of over 10,000 pounds but not over 26,000 pounds.
- $2,000 for all other qualifying motor vehicles.

The "Working Families Tax Relief Act of 2004" eliminated the scheduled phase outs for 2004 and 2005. However, the 2005 Energy Bill sunsets Section 179A deductions for clean-fuel vehicles and clean-fuel vehicle refueling property placed in service after 12/31/2005, rather than 12/31/2006. For vehicles placed in service in 2005, the 2005 Energy Bill introduced new tax credits for the purchase of hybrid, fuel cell, advanced lean burn diesel, and other alternative power vehicles.

The expense limitation for refueling property operates differently. The cost of qualifying refueling property that may be expensed under Section 179A may not exceed the excess of $100,000 over the total Section 179A expense taken in all preceding years on refueling property. In other words, $100,000 is the maximum amount that a business may take on such property during the life of this code section.

Section 179A Expense Recapture Rules

The amount expensed under Section 179A must be recaptured, in whole or in part for qualified clean-fuel vehicle property if, during the 3 years from the date the property was placed in service one of the following occurs:

- If it is a vehicle, it is modified so that it can no longer be propelled by a clean-burning fuel.
- The property is used in a manner described below (per IRS Code Section 50(b)):
  - Used outside of the United States.
  - Used in a business that furnishes lodging (although transient lodging such as a hotel is allowed).
- The property ceases to qualify in any other manner under Section 179A(c).
- The vehicle is sold or disposed of, and the taxpayer disposing of the property does not believe the property will continue to qualify under Section 179A.

For qualified clean-fuel vehicle refueling property, the amount expensed under Section 179A must be recaptured if, at any time before the end of the recovery period, the property ceases to be qualified clean-fuel vehicle refueling property. Property ceases to be qualified clean-fuel vehicle property if:

- The property no longer qualifies as clean-fuel vehicle refueling property.
- The property is no longer used predominantly in a trade or business.
- The property is used in a manner described below (per IRS Code Section 50(b)):
  - Used outside of the United States.
  - Used in a business that furnishes lodging (although transient lodging such as a hotel is allowed).
- The vehicle is sold or disposed of, and the taxpayer disposing of the property does not believe the property will continue to qualify under Section 179A.

How To:

For qualified clean-fuel vehicle property, the amount to be recaptured is:

The original amount expensed under Section 179A *times*:

- 100%, if the recapture event occurs within the first full year after it is placed in service.
- 66 2/3%, if the recapture event occurs within the second full year after it is placed in service.
- 33 1/3%, if the recapture event occurs within the third full year after it is placed in service.

For qualified clean-fuel vehicle refueling property, the amount to be recaptured is equal to the original amount expensed under Section 179A *multiplied by the following fraction*:

- Numerator - total recovery period for the property *minus* the number of recovery years prior to, but not including the recapture year.
- Denominator - total recovery period.

Section 179B Expense Deduction

The American Jobs Creation Act of 2004 introduced Section 179B, a provision that allows a small business refiner an election to deduct 75 percent of qualified capital costs paid or incurred during the tax year in order to be in compliance with the Highway Diesel Fuel Sulfur Control Requirements of EPA. These requirements, published in the Federal Register on January 18, 2001, require refiners to start producing diesel fuel with a sulfur content of no more than 15 parts per million (ppm) beginning on June 1, 2006. At the terminal level, highway diesel fuel sold as low sulfur fuel must meet the sulfur standards as of July 15, 2006. Section 179B expense is not subject to the same dollar limits or phase-out restrictions as is the Section 179 expense.

Qualifying Property

This pertains to costs paid or incurred with respect to any facility of a small business refiner during the period beginning on January 1, 2000 and ending on the earlier of the date that is one year after the date on which the taxpayer must comply with the applicable EPA regulations or December 31, 2009 to qualify for the deduction.

Small Business Refinery Defined

In order to qualify for the Section 179B Expense Deduction, a small business refinery must meet the following qualifications:

- Taxpayer who is in the business of refining crude oil.
- Employs no more than 1,500 employees in the refinery operations of the business on any day during the tax year.
- Had average domestic refinery run or average retained production for all facilities for the one year period that ended on December 31, 2002 that did not exceed 205,000 barrels. There are special rules and reduced percentages for a refinery with production in excess of 155,000 barrels for that same time period.

Basis Reduction

The basis of the property is reduced by the amount of the expense deduction.

Section 179B Expense Recapture Rules

Section 179B basis reduction is subject to the recapture rules as if it were a deduction allowable for amortization. This means that the amount expensed under Section 179B may need to be "recaptured," or treated as income, under certain circumstances.

Section 179C Expense Deduction

The 2005 Energy Bill enacted Section 179C allowing taxpayers to deduct 50% of the cost of "any qualified refinery property" for the tax year in which the qualified property is placed in service. Section 179C differs from Section 179B in that Section 179B only pertains to property relating to the reduction of sulfur requirements in diesel fuel. Section 179C expense is not subject to the same dollar limits or phase-out restrictions as is the Section 179 expense.

The Emergency Economic Stabilization Act of 2008 later extended the termination date for Section 179C from December 31, 2011 to December 31, 2013.

Qualified Refinery Property Defined

"Qualified Refinery Property" is a portion of a qualified refinery that meets the qualifications listed below:

- The original use of the property begins with the taxpayer.
- The property is placed in service after August 8, 2005 and before January 1, 2014.
- Meets the requirements of increased output or throughput requirements.
- Meets all applicable environmental laws in effect on the date the portion of a refinery was placed in service.
- No written binding contract for the construction of which was in effect before June 15, 2005.
- The construction of which is subject to a written binding construction contract entered into before January 1, 2010.

Qualified Refinery Defined

A "Qualified Refinery" is any refinery located in the U.S. that is designed to serve the primary purpose of processing liquid fuel from crude oil or "qualified fuels."

Basis Reduction

The basis of the property is reduced by the amount of the expense deduction.

Section 179C Expense Recapture Rules

Section 179C basis reduction is subject to the recapture rules as if it were a deduction allowable for amortization. This means that the amount expensed under Section 179C may need to be "recaptured," or treated as income, under certain circumstances.

Section 179D Expense Deduction

The 2005 Energy Bill enacted Section 179D allowing taxpayers to deduct an amount for the cost of "energy efficient commercial building property" placed in service after 12/31/05 and before 1/1/2008. The deduction is $1.80 per building square foot ($0.60) for certain separate building systems) less the aggregate of the Section 179D expense deductions allowed for the building in prior years. Section 179D expense is not subject to the same dollar limits or phase-out restrictions as is the Section 179 expense. The Tax Relief and Health Care Act of 2006 has extended Section 179D for one year for property placed in service through 12/31/2008.

The Emergency Economic Stabilization Act of 2008 later extended the termination date from December 31, 2008 to December 31, 2013. The Taxpayer Increase Prevention Act of 2014 extended the termination date to December 31, 2014. The Protecting Americans from Tax Hikes of 2015 extended the termination date to December 31, 2016.

Energy Efficient Commercial Building Property Defined

- Property for which depreciation or amortization is allowable.
- Property which is installed on or in a building located in the United States and within the scope of Standard 90.1-2001 of the American Society of Heating, Refrigerating and Air Conditioning Engineers and the Illuminating Engineering Society of North America.
- Property which is installed as part of the interior lighting systems, the heating, cooling, ventilation and hot water systems or the building envelope.
- Property which is created as being installed as part of a plan designed to reduce the total annual energy and power costs for the interior lighting, heating, cooling, ventilation and hot water systems of the building by 50% or more in comparison to a reference building that meets the minimum requirements of Standard 90.1-2001. If the building does not meet the overall building requirements of 50% energy savings, a

partial reduction is allowed. The energy savings will be verified in a certification process.

Basis Reduction

The basis of the property is reduced by the amount of the allowable deduction.

Section 179D Expense Recapture Rules

Section 179D basis reduction is subject to the recapture rules as if it were a deduction allowable for amortization. This means that the amount expensed under Section 179C may need to be "recaptured," or treated as income, under certain circumstances. This also applies for situations where the energy and power cost savings fall below the minimum 50% threshold. The 2005 Energy Bill also provides that any portion of real property for which the taxpayer has taken the deduction allowable under the rules of Section 179D is Section **1245** property for the purposes of recapture.

Section 179E Expense Deduction

The Tax Relief and Health Care Act of 2006 introduced this new Section 179E deduction that allows for the immediate expensing of the cost of qualified underground mine equipment that exceeds current safety requirements. This deduction applies to property placed in service after December 20, 2006 and before January 1, 2009.

The Emergency Economic Stabilization Act of 2008 extended the termination date from December 31, 2008 to December 31, 2009.

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended the termination date from December 31, 2009 to December , 2011.

The American Taxpayer Relief Act of 2012 extended the termination date from December 31, 2011 to December 31, 2013.

The Taxpayer Increase Prevention Act of 2014 extended the termination date from December 31, 2013 to December 31, 2014.

The Protecting Americans from Tax Hikes of 2015 extended the termination date from December 31, 2014 to December 31, 2016.

Bonus Depreciation

The Job Creation and Worker Assistance Act of 2002 included a provision for an additional 30% first-year depreciation deduction. This first-year deduction applied to qualifying assets acquired on or after September 11, 2001.

The Jobs and Growth Tax Relief and Reconciliation Act of 2003 increased the first-year depreciation deduction from 30% to 50% for assets placed in service after May 5, 2003 and before January 1, 2005 (before January 1, 2006 for certain property with longer production period).

The Jobs and Growth Tax Relief and Reconciliation Act of 2003 also allowed 30% first-year depreciation deduction for qualified New York Liberty Zone property placed in service after September 10, 2001 and before January 1, 2007 (before January 1, 2010 for nonresidential real property or residential rental property).

The American Jobs Creation Act of 2004 extended the 50% bonus depreciation for non-commercial aircraft placed in service through December 31, 2005.

The Gulf Opportunity Zone Act of 2005 extended the 50% bonus provision to qualified property placed in service on or after August 28, 2005 and on or before December 31, 2007 (or 2008 for real property) in a designated GO Zone.

The Tax Relief and Health Care Act of 2006 has extended the bonus depreciation for certain GO Zone property placed in service before January 1, 2011. The requirement for nonresidential real property or residential rental property was extended through December 31, 2010 for certain counties and parishes within the GO Zone. Personal property located within the buildings of one of these special counties or parishes qualifies through March 31, 2011. This act also allows for a new 50% bonus depreciation deduction for “Cellulosic Biomass Ethanol Plan Property” placed in service before January 1, 2013. The 50% bonus depreciation was also extended another year through December 31, 2006 under this act for property with longer production periods and certain aircraft affected by Hurricanes Katrina, Rita, or Wilma.

The Economic Stimulus Act of 2008 reinstituted the 50% bonus depreciation for all areas of this country for qualified property placed in service in 2008, certain types of property with longer production periods, and certain aircraft placed in service through 2009.

The 2008 Farm Act has provided 50% depreciation allowance for qualified Recovery Assistance property placed in service from May 5, 2007 to December 31, 2008 (2009 for nonresidential real property or residential rental property) located in the Kansas Disaster Area.

The Emergency Economic Stabilization Act has included cellulosic biofuel within the definition of biomass ethanol plant property for purposes of the 50% depreciation allowance. It has also allowed a 50% depreciation allowance for reuse and recycling property placed in serviced beginning after August 31, 2008, and used to collect, distribute, or recycle certain materials, including scrap, fibers, and metals.

The Emergency Economic Stabilization Act also allows the 50% special allowance for Qualified Disaster Zone property placed in service by the last day of the third calendar year following the applicable disaster date (the fourth calendar year in the case of non-residential real property and residential rental property). The property must be placed in service on or after January 1, 2008 and continues to qualify for disasters that occur prior to January 1, 2010. In effect, personal property qualifies through December 31, 2012 and real property through December 31, 2013.

The American Recovery and Reinvestment Act of 2009 extended the bonus depreciation provision under Code Section 168(k) for qualified property placed in service through 12/31/2009. Qualified property includes property with recovery period of 20 years or less, computer software [Section 167(f)(1)(B)], water utility property, qualified leasehold improvement property, certain property with longer production periods, or certain aircraft. Expiration date for certain aircraft and certain property with longer production periods is 12/31/2010.

The Small Business Jobs Act of 2010 extended the bonus depreciation provision under Code Section 168(k) for qualified property placed in service through 12/31/2010. Qualified property includes property with recovery period of 20 years or less, computer software [Section 167(f)(1)(B)], water utility property, qualified leasehold improvement property, certain property with longer production periods, or certain aircraft. Expiration date for certain aircraft and certain property with longer production periods is 12/31/2011.

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended the bonus depreciation provision under Code Section 168(k) and temporarily increased the rate for qualified property acquired and placed in service as follows (note that the definition of qualified property remains the same):

- 1/1/2010 through 9/8/2010: 50%
- 9/9/2010 through 12/31/2010: 100%
- 1/1/2011 through 12/31/2011: 100%
- 1/1/2012 through 12/31/2012: 50%
- For long-production-period property and certain aircraft, the placed-in-service dates are extended one year.

The American Taxpayer Relief Act of 2012 extended the 168 Allowance of 50% through 2013 for qualified property (2014 for certain property with longer production periods). In addition, the 168 Allowance has been extended through 2013 for second generation biofuel, which includes cellulosic biofuel plant property.

The Taxpayer Increase Prevention Act of 2014 extended the 168 Allowance of 50% through 2014 for qualified property (2015 for certain property with longer production periods). In addition, the 168 Allowance has been extended through 2014 for second generation biofuel, which includes cellulosic biofuel plant property.

The Protecting Americans from Tax Hikes of 2015 extended the 168 Allowance through 12/31/2019. The bonus rates for qualified property acquired and placed in service are as follows:

- 1/1/2015-12/31/2017: 50%
- 1/1/2018-12/31/2018: 40%
- 1/1/2019-12/31/2019: 30%
- For long production period property and certain aircraft, the placed-in-service dates are extended one year.

New Law: The Tax Cuts and Jobs Act of 2017 reinstated the 168 Allowance of 100% for qualifying assets placed in service after 9/27/2017 through 12/31/2022 (12/31/2023 for longer production period assets and certain aircraft). Certain exceptions exist, particularly for assets acquired before 9/28/2017 and placed in service after 9/27/2017.

A transition rule provides that, for a taxpayer's first taxable year ending after September 27, 2017, the taxpayer may elect to apply a 50-percent allowance instead of the 100-percent allowance.

After 12/31/2022, the 168 Allowance decreases by 20% each year until 12/31/2026. After 12/31/2026, the 168 Allowance is 0% except for reuse and recycling property which has an ongoing 168 Allowance of 50%.

Qualifying Assets

Assets placed in service outside of the New York Liberty Zone and Gulf Opportunity Zone (GO Zone)

Qualifying property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software
- Qualified leasehold improvements
- Water utility property, which has a 25-year recovery period

Property with longer production periods refers to property which has a recovery period of at least 10 years or is transportation property and which is subject to IRS code section 263A's Uniform Capitalization Rules.

The following additional rules apply:

- The original use of the property must commence with the taxpayer. Used property does not qualify.
- If property is listed property used 50% or less for business purposes it does not qualify.
- If the property is required to be depreciated under the Alternative Depreciation System, the asset does not qualify.

Assets placed in service in the New York Liberty Zone

Qualifying property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software
- Qualified leasehold improvements
- Water utility property which has a 25-year recovery period
- Residential rental and non-residential real property

New York Liberty Zone assets must be placed in service before January 1, 2007 (or January 1, 2010 for residential rental and non-residential real property).

Assets that are placed in service in the New York Liberty Zone and qualify as 168(k) property do not qualify as New York Liberty Zone property. For additional rules relating to New York Liberty Zone assets, refer to "Qualified New York Liberty Zone Property," page IV-34.

Assets placed in service in the GO Zone

Qualifying property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software
- Qualified leasehold improvements
- Water utility property which has a 25-year recovery period
- Residential rental and non-residential real property

Go Zone assets must be placed in service on or after August 28, 2005 and before January 1, 2008 (or January 1, 2009 for residential rental and non-residential real property).

The Tax Relief and Health Care Act of 2006 has extended the bonus depreciation for certain GO Zone property placed in service before January 1, 2011.

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 ex-tended the bonus depreciation for certain GO Zone property placed in service before January 1, 2012.

For additional rules relating to GO Zone assets, refer to "Qualified Gulf Opportunity Zone Property," page IV-33.

Assets placed in service in the Kansas Disaster Zone

Qualifying property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software
- Qualified leasehold improvements
- Water utility property which has a 25-year recovery period
- Residential rental and non-residential real property

Kansas Disaster Zone assets must be placed in service on or after May 5, 2007 and on or before December 31, 2008 (or 2009 for residential rental and non-residential real property).

For additional rules relating to Kansas Disaster Zone assets, refer to "Qualified Recovery Assistance Property," page IV-36.

Assets placed in service in the Qualified Disaster Zone

Qualifying property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software
- Qualified leasehold improvements
- Water utility property which has a 25-year recovery period
- Residential rental and non-residential real property

Qualified Disaster Zone assets must be placed in service after December 1, 2007 with respect to disasters declared after December 31, 2007 and occurring before January 1, 2010. The property must also be placed in service by the end of the third calendar year (fourth calendar year for non-residential real property and residential rental property).

For additional rules relating to Qualified Disaster Zone assets, refer to "Qualified Disaster Assistance Property," page IV-37.

Electing Out of the Bonus Depreciation

The first-year depreciation deduction is mandatory for qualifying assets unless an election out is made. You make the election out by class of assets (i.e., 3-year, 5-year, and so forth) for each applicable tax year in which qualified assets are placed in service. To make the election, attach a statement to that effect to your tax return.

Note: If you do not take the first-year depreciation deduction and you fail to make the election out, you must still reduce the basis of the property on which you calculate MACRS depreciation by the first-year depreciation deduction.

Calculating the Bonus Depreciation

Calculate the first-year depreciation deduction by multiplying the depreciable basis of the property by either 30%, 40%, 50%, or 100%.

How to:

	Asset's **Acquired Value**, including freight and installation costs
minus	**Section 179A expense** (clean fuel deduction)
minus	**Electric Vehicle Credit** reduction amount
times	**Business + Investment-use percentage**
minus	**Section 179 expense**
minus	**Deduction for the removal of barriers**
minus	**Disabled access** credit
minus	**Enhanced oil** recovery credit
minus	**Investment Tax Credit** reduction amount
equals	**Basis for calculation of the first-year depreciation deduction**
times	**0.30 [or .50 , or .40, or 1.00]**
equals	First-year depreciation deduction

The adjusted basis of the property is then reduced by the first-year depreciation deduction before regular depreciation is calculated in the placed-in-service year and following years.

Example: ABC Services, a calendar year taxpayer, opens a new office in December 2001 and places in service qualifying office furniture and fixtures totaling $100,000. The property is eligible for Section 179 expensing of $24,000 and the 30% first-year depreciation deduction.

Result: Section 179 expense is subtracted from the basis before the 30% first-year depreciation deduction is calculated. The 30% first-year depreciation deduction further reduces the depreciable basis before MACRS depreciation is calculated.

The depreciable basis is:

Cost	$100,00
Less Section 179 Expense	- 24,000
Basis for 30% First-Year Depr. Deduction	76,000
Less 30% First-Year Depreciation Deduction	- 22,800
Depreciable Basis	$ 53,200

The 2001 MACRS depreciation is:

7-year assets using the HY convention -

$$\frac{\$53{,}200}{7 \text{ years} \times 200\% \times 1/2 \text{ year}} = \$7{,}600$$

Miscellaneous Rules

Previously, the first-year depreciation deduction limitation for qualifying passenger automobiles and light trucks and vans increased by $4,600 if placed into service before May 6, 2003, and by $7,650 if placed into service after May 5, 2003, but only for those vehicles on which the 30% or 50% first-year depreciation deduction was taken.

The first-year depreciation deduction limitation for qualifying passenger automobiles and light trucks and vans increases by $8,000 if placed in service from January 1, 2008 through December 31, 2018 but only for those vehicles on which bonus depreciation deduction is taken.

If the 30%, 40%, 50%, or 100% first-year depreciation deduction was taken for regular tax purposes, there is no AMT adjustment for the additional first-year depreciation deduction, or for the depreciation deductions to be taken over the remainder of the asset's recovery period.

Qualified Gulf Opportunity Zone Property

The Gulf Opportunity Zone Act of 2005 enacted bonus depreciation for designated GO Zones with 50% bonus depreciation allowed for both and real property.

In order for property to qualify for bonus depreciation, all of the following requirements must be met:

- The property must be property to which the general rules of MACRS apply.
- Original use of property in the GO Zone must start with the taxpayer on or after August 28, 2005. The GO Zone property can be used or new as long as the original use of property criteria is met.
- The property must be acquired by the taxpayer by purchase on or after August 28, 2005, but only if no written binding contract for the property was in effect before August 28, 2005, and must be placed in service on or before December 31, 2007, or December 31, 2008 in the case of residential rental or non-residential real property.

The Tax Relief and Health Care Act of 2006 extended the 50% bonus depreciation for certain property placed in service in the GO Zone through December 31, 2010. This extension applies to nonresidential real property, residential real property, and personal property used in a building within 90 days of the date the building is placed in service.

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended the 50% bonus depreciation for certain property placed in service in the GO Zone through December 31, 2011. This extension applies to nonresidential real property, residential real property, and personal property used in a building within 90 days of the date the build-ing is placed in service.

As is the case with New York Liberty Zone property, the taxpayer can elect out of bonus depreciation.

Increase in Section 179 for Qualified Gulf Opportunity Zone Property

Under the provision within the Gulf Opportunity Zone Act of 2005, the maximum amount that a taxpayer may elect to deduct under section 179 is increased by the lesser of $100,000, or the cost of qualified section 179 Gulf Opportunity Zone property for the taxable year.

The provision also provides a special rule for the reduction in the maximum deduction for the cost of qualified section 179 Gulf Opportunity Zone property. Under this rule, the reduction in limitation is increased by the lesser of $600,000, or the cost of qualified section 179 Gulf Opportunity Zone property placed in service during the tax year. The $600,000 amount is not indexed.

Qualified New York Liberty Zone Property

The Job Creation and Worker Assistance Act of 2002 created additional tax incentives for taxpayers located in a New York Liberty Zone. In general, the provisions of the Act that apply to the New York Liberty Zone allow the taxpayers additional time to claim incentives and also include:

- Expansion of the 30% Allowance to additional types of property
- Decrease in depreciable life for leasehold improvements
- Increase in the Section 179 deduction

Note: The 30% allowance is deductible for both regular tax and AMT purposes.

The New York Liberty Zone is defined under IRS Code Sec. **1400L** as the area located on or south of Canal Street, East Broadway (east of its intersection with Canal Street), or Grand Street (east of its intersection with East Broadway) in the Borough of Manhattan in the City of New York, New York.

Qualifying NY Liberty Zone property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Water utility property, with a 25-year recovery period
- Section 167(f)(1)(B) computer software
- Residential Rental and Non-Residential Real property, to the extent that it rehabilitates real property damaged, or replaces real property destroyed or condemned, as a result of the September 11, 2001 terrorist attack.

NY Liberty Zone property must also meet the following tests:

- Property must be acquired after September 10, 2001.
- If property is acquired after September 10, 2001 and before September 11, 2004, it must be "used" (since new property would qualify under 168(k), as defined under "Qualifying Assets," page IV-29). If acquired after September 10, 2004, it can be either new or used.
- Property must be placed into service before January 1, 2007 (January 1, 2010 for Residential Rental and Non-Residential Real property).
- Substantially all property must be in use in the NY Liberty Zone, and used in the active conduct of a trade or business in the NY Liberty Zone.
- The original use of the property in the NY Liberty Zone must have begun after September 10, 2001. Used property qualifies if it has not previously been used within the NY Liberty Zone.

The following property does not qualify as NY Liberty Zone property:

- Property to which section 168(k) applies (the additional 30% or 50% depreciation deduction, as defined under "Qualifying Assets," page IV-29)
- Listed property that is used 50% or less for business purposes
- Property that is required to be depreciated under the Alternative Depreciation System (ADS)
- Qualified NY Liberty Zone Leasehold Improvement Property (as defined below)

Example: On December 15, 2002, you purchased and placed into service the following assets:

- New office furniture
- Used computer

Assuming these assets meet all of the tests for NY Liberty Zone property (excluding the "new" or "used" test), the office furniture would not be eligible for the special NY Liberty Zone allowance because it is new property. However, it would be eligible for the 30% allowance under Section 168(k). On the other hand, the computer would qualify for the special NY Liberty Zone allowance because it is used property.

Electing Out of the First-Year Depreciation Deduction for NY Liberty Zone Property

You may elect out of the first-year depreciation deduction for NY Liberty Zone Property by property class, similar to how you'd elect out of the first-year depreciation deduction to which section 168(k) applies (refer to "Electing Out of the Bonus Depreciation," page IV-31, for those specific rules).

5-Year Recovery Period for Certain NY Liberty Zone Leasehold Improvement Property

Qualified NY Liberty Zone Leasehold Improvement Property qualifies for a shorter 5-year recovery period (as opposed to the normal 39-year life), in lieu of the first-year depreciation deduction. Eligible property must be placed in service after September 10, 2001 and before January 1, 2007. The class life of this property for purposes of the Alternative Depreciation System is 9 years. As with all MACRS leasehold improvement property, the SL method of depreciation is required.

The Working Families Tax Relief Act of 2004 included a technical correction that allows a taxpayer to elect out of the 5-year recovery period for depreciation of qualified NY Liberty Zone Leasehold Improvement Property. The rules for electing out are similar to those for electing out of bonus depreciation under code Section 168 (k)(2)(c)(iii).

Increase in Section 179 for Qualified NY Liberty Zone Property

The provisions within the Job Creation and Worker Assistance Act of 2002 include an increase in the amount of Section 179 that can be taken for qualified NY Liberty Zone property, effective for taxable years beginning on December 31, 2001 and before January 1, 2007.

The provision increases the maximum dollar amount that can be deducted by the lesser of (1) $35,000 or (2) the cost of qualifying property placed in service during the year. This amount is in addition to the amount otherwise deductible under Section 179.

To qualify for this increased Section 179 deduction, the following must apply:

1. The property must be placed into service after September 10, 2001 and before January 1, 2007,
2. The original use of the property must commence in the NY Liberty Zone, and
3. The property must be substantially used in a trade or business located within the NY Liberty Zone.

For purposes of calculating the phase-out of the Section 179 deduction, only 50% of the cost of NY Liberty Zone property is included in the Total Cost of Section 179 property placed in service during the year, similar to the rules for enterprise zones.

If the property ceases to be used in the NY Liberty Zone, the recapture rules apply (refer to "Section 179 Expense Recapture Rules," page IV-16).

Qualified Recovery Assistance Property

The 2008 Farm Act provides additional first-year depreciation deduction equal to 50 percent of the adjusted basis, and increases Section 179 expense deduction for qualified Recovery Assistance property located within the Kansas Disaster Area. The following 24 counties make up the Kansas Disaster Area as defined under IRS Code Section **1400N(d)**: Barton, Clay, Cloud, Comanche, Dickinson, Edwards, Ellsworth, Kiowa, Leavenworth, Lyon, McPherson, Osage, Osborne, Ottawa, Phillips, Pottawatomie, Pratt, Reno, Rice, Riley, Saline, Shawnee, Smith, and Stafford.

Qualifying Recovery Assistance property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software

- Qualified leasehold improvements
- Water utility property which has a 25-year recovery period
- Residential rental and non-residential real property

Qualifying Recovery Assistance property must also meet the following tests:

- Substantially all property must be used in the Kansas Disaster Zone, and in the active conduct of a trade or business in the Kansas Disaster Zone.
- The original use of the property in the Kansas Disaster Zone must commence on or after May 5, 2007. Used property may qualify so long as it has not previously been used within the Kansas Disaster Zone.
- The property must be acquired by purchase on or after May 5, 2007 and placed in service on or before December 31, 2008 (or 2009 for nonresidential real property and residential rental property).

The following property does not constitute qualified Recovery Assistance property:

- Alternative depreciation property (ADS)
- Tax-exempt bond-financed property
- Qualified revitalization buildings

Electing Out of the First-year Depreciation Deduction

You may elect out of the first-year depreciation deduction for qualified Recovery Assistance property by property class, similar to how you would elect out of the first-year depreciation deduction to which section 168(k) applies (refer to "Electing Out of the Bonus Depreciation," page IV-31, for those specific rules).

Increase in Section 179 for Qualified Recovery Assistance Property

Under the provision within the 2008 Farm Act, the maximum amount that a taxpayer may elect to deduct under section 179 is increased by the lesser of $100,000, or the cost of qualified section 179 Recovery Assistance property for the taxable year. The provision applies with respect to qualified section 179 Recovery Assistance property acquired on or after May 5, 2007, and placed in service on or before December 31, 2008.

The provision also provides a special rule for the reduction in the maximum deduction for the cost of qualified section 179 Recovery Assistance property. Under this rule, the reduction in limitation is increased by the lesser of $600,000, or the cost of qualified section 179 Recovery Assistance property placed in service during the tax year. The $600,000 amount is not indexed.

Qualified Disaster Assistance Property

The Emergency Economic Stabilization Act of 2008 provides a new tax relief package for victims of all Federally-declared disasters occurring after December 31, 2007 and before January 1, 2010 to include the bonus 50% first year depreciation for property placed in service through December 31, 2012 (December 31, 2013 for real property), and the increase in Section 179 expense deduction.

Qualifying Disaster Assistance property is one of the following:

- MACRS property with a recovery period of 20 years or less
- Section 167(f)(1)(B) computer software
- Qualified leasehold improvements
- Water utility property which has a 25-year recovery period
- Residential rental and non-residential real property

Qualifying Disaster Assistance property must also meet the following tests:

- Substantially all property must be used in the disaster area with respect to a federally declared disaster occurring before January 1, 2010, and in the active conduct of a trade or business in that disaster area.
- The property must rehabilitate property damaged, or replace property destroyed or condemned, as a result of the federally declared disaster,
- The original use of the property in the disaster area must begin on or after the applicable disaster date.
- The property must be acquired by purchase on or after the applicable disaster date and placed in service by the end of the third calendar year (or fourth calendar year for nonresidential real property and residential rental property). An applicable disaster date is the date on which the disaster occurs.

The following property does not constitute qualified Disaster Assistance property:

- Qualified property to which the 50% bonus depreciation and exemption from the AMT depreciation adjustment applies
- Gambling, racing and certain other leisure facilities
- Alternative depreciation system property (ADS)
- Tax-exempt bond financed property
- Qualified revitalization buildings

Electing Out of the First-year Depreciation Deduction

You may elect out of the first-year depreciation deduction for qualified Disaster Assistance property by property class, similar to how you would elect out of the first-year depreciation deduction to which section 168(k) applies (refer to "Electing Out of the Bonus Depreciation," page IV-31, for those specific rules).

Increase in Section 179 for Qualified Disaster Assistance Property

Under the provision within the Emergency Economic of Stabilization Act of 2008, the maximum amount that a taxpayer may elect to deduct under section 179 is increased by the lesser of $100,000, or the cost of qualified section 179 Disaster Assistance property for the taxable year. The provision applies with respect to qualified section 179 Disaster Assistance property acquired on or after the applicable disaster date and placed in service by the end of the third calendar year (or fourth calendar year for nonresidential real property and residential rental property).

The provision also provides a special rule for the reduction in the maximum deduction for the cost of qualified section 179 Disaster Assistance property. Under this rule, the reduction in limitation is increased by the lesser of $600,000, or the cost of qualified section 179 Disaster Assistance property placed in service during the tax year. The $600,000 amount is not indexed.

If the property ceases to be used predominantly in a trade or business within the disaster area, the recapture rules apply (refer to "Section 179 Expense Recapture Rules," page IV-16).

Section IV: Chapter 2: Modified Accelerated Cost Recovery System (MACRS)

In this section:

The Tax Reform Act of 1986 changed the depreciation methods and lives for assets placed in service after December 31, 1986. Because these changes modified the depreciation system existing at the time (known as the Accelerated Cost Recovery System; ACRS), the new depreciation method became known as “Modified” ACRS, and thus MACRS came into existence.

The principal changes made by MACRS, as compared to ACRS, were:

- Revised property classes.
- Longer recovery periods for most assets, especially for real property.
- A faster cost recovery rate for personal property, generally using the double declining-balance method rather than the 150% declining-balance method used under ACRS.
- A slower rate for real property, mainly using the straight-line method.

The MACRS methods created by the Tax Reform Act of 1986 are mandatory for depreciable property placed in service by a business after 1986. There is, however, an exception for certain property placed in service after 1986 that, due to an earlier contract, construction, or fund commitment, is depreciated under ACRS. Also, transitional rules were created for property placed in service after July 31, 1986, whereby the taxpayer could elect to treat such assets according to either MACRS or ACRS.

MACRS consists of two systems of depreciation. The principal system, sometimes referred to as the General Depreciation System (GDS), is used the majority of the time. The secondary system, called the Alternative Depreciation System (ADS), is used only if required by law or if the business elects it. The main difference between the two systems is that the latter generally uses a longer recovery period and always uses straight-line depreciation.

MACRS Recovery Periods

There are eleven classes of property according to MACRS that determine the property's recovery period. We will list them here along with a brief description of each, as well as the depreciation method generally used if the Alternate MACRS method (ADS) is not elected.

Class	Deprec. Method	Description
3-year	DDB	Property with a class life of 4 years or less, including any race horse placed in service before January 1, 2017, any race horse more than 2 years old placed in service after December 31, 2016, any horse other than a race horse more than 12 years old, and qualified rent-to-own property.
5-year	DDB	Property with a class life of 5 to 9 years, including any automobile or light general purpose truck, semi-conductor manufacturing equipment, computer-based telephone central office switching equipment, qualified technological equipment, property used in research and experimentation, certain energy property, and machinery or equipment used in a farming business placed in service from January 1, 2009 to December 31, 2009.
7-year	DDB	Property with a class life of 10 to 15 years, including any railroad track, motorsports entertainment complex, Alaska natural gas pipeline, and natural gas gathering line placed in service after April 11, 2005.
10-year	DDB	Property with a class life of 16 to 19 years, including any single purpose agricultural or horticultural structure, tree or vine bearing fruit or nuts, qualified smart electric meter, and qualified smart electric grid system.
15-year	1.5 DB	Property with a class life of 20 to 24 years, including any municipal wastewater treatment plant, telephone distribution plant and comparable equipment, retail motor fuels outlet, qualified leasehold improvement property and qualified restaurant property placed in service after October 22, 2004 and before December 31, 2017, qualified improvement property after December 31, 2018 initial clearing and grading land improvements with respect to gas utility property, property used in the transmission at 69 or more kilovolts of electricity for sale placed in service after April 11, 2005, natural gas distribution line placed in service after April 11, 2005 and before January 1, 2011, and qualified retail improvement property placed in service after December 31, 2008.
20-year	1.5 DB	Property with a class life of more than 24 years, including any initial clearing and grading land improvements with respect to any electric utility transmission and distribution plant.
25-year	SL	Water utility property and municipal sewers, placed in service after June 12, 1996.

Class	Deprec. Method	Description
27.5-year	SL	**Residential rental property** where 80% of the gross rental income is derived from providing living accommodations (as opposed to transient accommodations, e.g., hotels), including low-income housing. **Note:** To be considered transient, more than half of the units need to be used on a temporary basis.
31.5-year	SL	Nonresidential real property placed in service before May 13, 1993.
39-year*	SL	Nonresidential real property placed in service after May 12, 1993.
50-year	SL	Any railroad grading or tunnel bore (these will not be covered in this guide—for more information, see IRS Code Sec. **168(d)**, **168(e)(4)**, etc.).

* As frequently happens when a tax law change involves real property, there are transitional rules for 39-year property. The 39-year recovery period does not apply to nonresidential real property placed in service before January 1, 1994 if:

a. The taxpayer, or qualified person, entered into a binding written contract to purchase or construct the property before May 13, 1993, or

b. Construction of the property was begun by or for the taxpayer, or qualified person, before May 13, 1993.

If either of the above applies, such property will have a 31.5-year recovery period.

How To:

Once property is identified as MACRS property, you will need to turn to **Tables 1–3** in Section VI: "Tables." For each asset we have shown a class life, a recovery period for MACRS, and a recovery period for Alternate MACRS (ADS). We have alphabetized the tables to assist you in determining the correct asset class. See "Tables 1–3," page VI-2, which will help you locate a particular asset quickly.

Note: For purposes of MACRS, the "class lives" are used to determine the property's class and, thus, the recovery period. Since we have determined the recovery periods for you, you may ignore the class lives in these tables for the time being.

Additions or improvements made to property, including leased property (i.e., leasehold improvements), are treated as separate property items. However, they are depreciated in the same manner as the underlying property would be *if such property had been placed in service on the same date as the improvement.* The recovery period for any additions or improvements begins on the later of:

- the date the addition or improvement is placed in service, or

- the date the property to which the addition or improvement is made is placed in service.

MACRS Averaging Conventions

In the beginning of this section of the guide, we described the principal averaging conventions used for income tax reporting purposes. Under MACRS, these conventions are not optional but are determined, generally, by the type of property. There is also a special rule for when a large amount of property is placed in service late in the tax year:

- *Half-Year Convention:* Used for all MACRS property *except* residential rental and nonresidential real property.
- *Midmonth Convention:* Used for residential rental and nonresidential real property.
- *Midquarter Convention:* Used when more than 40% of qualifying property is placed in service during the last 3 months of the tax year.

Half-Year Convention

The half-year convention treats all property placed in service, or disposed of, as if occurring at the midpoint of the tax year. Therefore, the same amount of depreciation will be taken regardless of when, during a taxable year, property is placed in service. The half-year convention applies whether you use regular MACRS (GDS) or the alternate MACRS (ADS), as well as to partial years.

When property is held for its entire recovery period, a half-year of depreciation is allowable in the tax year following the tax year in which the recovery period ends. For example, if it is a 5-year asset, the business actually claims depreciation on it for 6 tax years: a half-year of depreciation in the year placed in service, then for 4 full years, and, finally, a half-year of depreciation in the sixth year.

How To:

To calculate the amount of depreciation under the half-year convention, simply compute the full year's depreciation and divide by two.

Midmonth Convention

The midmonth convention treats all property either placed in service or disposed of as if the event occurred at the midpoint of the month. In other words, whether property is placed in service on the first day of a month or the last day of the month, it will be treated as if placed in service in the middle of the month (normally the 15th day). The midmonth convention is always applied without regard to the tax year, and therefore is not affected by a short year.

How To:

To calculate the amount of depreciation under the midmonth convention, compute the full year's depreciation and multiply by the following fraction:

$$\frac{\textit{Number of full months property was used for the year} + .5}{12}$$

Example: XYZ, a calendar-year corporation, placed in service MACRS residential rental property on March 30. It is an apartment building in the 27.5-year class and cost $500,000. A full year's depreciation for the property is $18,182.

Result: The depreciation for the first year of the property's recovery period is $14,394, computed as follows:

$$\$18,182 \times \frac{9.5}{12} = \$14,394$$

TIP
Since property placed in service on the last day of the month is still entitled to a half month's depreciation for that month, it is possible to claim an additional month's depreciation just by placing property in service a few days earlier (when possible), rather than the first day of the following month. For example, if property can be placed in service on March 30 rather than on April 1, an additional month of depreciation may be deducted.

Midquarter Convention

Earlier we mentioned a special rule for when a large amount of property is placed in service late in the tax year. This is known as the midquarter convention. **The midquarter convention is mandatory when applicable, takes precedence over the half-year convention, and applies to whichever MACRS depreciation method you are using, including the MACRS Alternative Depreciation System (ADS)**.

The 40% Test

If during any tax year **more than 40%** of the total depreciable basis of *qualifying property* (defined later) is placed in service **during the last 3 months of the tax year**, the midquarter convention applies. Under the midquarter convention, all property either placed in service or disposed of is treated as if occurring at the midpoint of the quarter.

Note: Since it is "the last 3 months of the year," *not* "the last quarter of the year," if, for example, the tax year only consists of 3 months, the midquarter convention will automatically apply to all qualifying depreciable property placed in service that year.

The 40% test is usually applied at the partnership or S corporate level *unless* the IRS determines that the entity is being used for the principal purpose of avoiding or inappropriately applying the midquarter convention. If this is the case, the 40% test will be applied at the individual partner or shareholder level instead.

Generally, when an affiliated group files a consolidated tax return, all of the members included on the return are treated as one taxpayer when applying the 40% test. For further information on how the midquarter convention is applied to an affiliated group of corporations, see IRS Reg. **1.168(d)-1(b)(5)**.

In certain transactions between corporations and their shareholders, and between partnerships and their partners, transfers of property may be made and no gain or loss will be recognized (IRS Code Sec.**168(i)(7)(B)(i)**). If such a transfer occurs in the year in which property is placed in service, the 40% test will be applied by treating the transferee as the owner of the property. The transferred property is deemed placed in service by the transferee on the date of the transfer. In other words, if the total basis of the transferee's property placed in service during the last 3 months of the tax year, including the transferred property, exceeds 40% of the basis of all property placed in service that year, the midquarter convention will apply. The transferred property will not be taken into account by the transferor when applying the 40% test for the year.

Depreciable Basis Determination for Midquarter

Since only the "depreciable basis" of qualifying property is to be considered when applying the 40% test, this means that the following is *excluded from the determination of basis:*

1. The percentage of the property's basis that is *not* used in the trade or business or held for production of income.

   Example: If an asset that is normally depreciable under MACRS is acquired by a taxpayer who uses it in his business only 80% of the time the first year it is acquired, only 80% of the asset's basis is considered in determining if the 40% test applies. The personal use portion of 20% is not considered.

2. Any portion of the property expensed under Section 179 (explained in the previous chapter).

TIP
By electing to use the Section 179 expense, a taxpayer may avoid the midquarter convention if it would be to his tax advantage to do so.

Example: XYZ, a calendar-year corporation, places in service two assets during the year: Machine A costing $14,500 on May 1, and Machine B costing $10,500 on December 31. The midquarter convention will apply, since **more than 40%** of the XYZ property was placed in service during the last 3 months of the tax year. However, XYZ may avoid the midquarter by electing to expense the $10,500 cost of Machine B under Section 179.

Property Qualifying for Midquarter

Property that must be included when determining whether or not a business has placed in service more than 40% of its property in any one tax year is all MACRS depreciable property *except* for:

- Residential rental property.
- Nonresidential real property.
- Property that is both placed in service and disposed of in the same tax year (although if *reacquired* and again placed in service, it will be taken into account for the 40% test, but only on the later of the dates it was used).

Note: Since property must be depreciated under MACRS to be included in the midquarter calculation, property being depreciated under a Production or Use method is *not* included.

Calculating MACRS Depreciation Under the Midquarter Convention

How To:

To calculate the amount of depreciation under the midquarter convention, compute the full year's depreciation on each asset and then multiply by the following percentage, based on which quarter of the tax year the property is placed in service:

Quarter of the tax year property placed in service	Percentage
1st	10.5/12 = 87.5%
2nd	7.5/12 = 62.5%
3rd	4.5/12 = 37.5%
4th	1.5/12 = 12.5%

TIP
Although the midquarter convention was intended to reduce the amount of depreciation for a business that places most of its property in service late in the tax year, it actually can be advantageous to the taxpayer, at times resulting in a larger depreciation deduction. This is because **the midquarter convention will result in a larger amount of depreciation than the half-year convention for those assets placed in service during the first two quarters of the tax year.**

Example: A calendar-year business places in service two 5-year assets: an $850 asset on January 1 and a $650 asset on December 31.

Result: The midquarter convention applies:

Depreciable Basis	Full Year Depreciation	X	Percentage	=	Depreciation Allowed
$850	$340	x	87.5%	=	$297.50*
$650	$260	x	12.5%	=	32.50
			Total Depreciation	=	$330

Example: Same example as above except both assets are now placed in service on May 1.

Result: The midquarter convention no longer applies and the half-year convention must be used:

Depreciable Basis	Full Year Depreciation	X	Percentage	=	Depreciation Allowed
$850	$340	x	50%	=	$170*
$650	$260	x	50%	=	130
			Total Depreciation	=	$300

* More depreciation may be deducted when the midquarter convention is used than when the half-year convention is used. Although the asset acquired later in the year for $650 received a lot less depreciation under the midquarter convention, the asset placed in service in the first quarter of the year, in the first example, received much more depreciation under the midquarter convention.

However, in the majority of instances, less depreciation is in fact allowed under the midquarter convention than when using the half-year convention. Each set of circumstances needs to be computed under both conventions if you want to make the best decision for the business.

Remember that when the midquarter convention applies, it is mandatory to use it. The only flexibility you *may* have is either in the timing of when the property is placed in service or by electing to use the Section 179 expense.

MACRS Depreciation Methods

There are five different depreciation methods under MACRS. All except the last one (the Alternative Depreciation System; ADS) are restricted to certain classes of property. They will all recover 100% of an asset's depreciable basis, since they ignore salvage value, but they will do so at different rates. We will list them here in descending order, according to their speed of cost recovery:

1. 200%, or double declining-balance method (DDB), over the GDS (General Depreciation System) life. This is used for property in the 3-, 5-, 7-, and 10-year classes.*

2. 150%, or 1.5 declining-balance method (1.5 DB), over the GDS life. This is used for property in the 15- and 20-year classes, and for all property placed in service in a farming business after 1988.*

3. You can *elect* to use the 150% declining-balance method either over the GDS life, for property placed in service after 12/31/98, or over the longer ADS life, for property placed in service before 1/1/99. (The change in the recovery period used for this election was due to the IRS Restructuring and Reform Act of 1998.) This election may only be made for property described in **1.** or **2.** above.*

How To:

This election is made by entering "150 DB" in column (f) of Part II of IRS Form 4562, Depreciation and Amortization.

* In all three of the above methods you *must* switch to the straight-line method when that method results in a larger deduction! (For an explanation of how to compute "Remaining Value Over Remaining Life", see Section III: "Depreciation for Financial Reporting.")

4. Straight-line method over the GDS recovery period. This method *must* be used for all property in the 25-, 27.5-, 31.5-, and 39-year recovery classes and for trees and vines that bear fruit or nuts. The taxpayer may also *elect* to use it for any property over the regular (GDS) recovery period.

How To:

The election for using straight-line depreciation is made by entering "SL" in column (f) of Part III of IRS Form 4562, Depreciation and Amortization.

5. Straight-line method over the fixed Alternative Depreciation System (ADS) lives. This method is required to be used for certain types of property and may be *elected* for all others. It differs from the straight-line method mentioned in **4.** above, as it has longer recovery periods for many types of property. This is, therefore, the slowest of all the MACRS depreciation methods and is described in detail later in this chapter.

How To:

The ADS election is made by completing line 20 of Part III of IRS Form 4562, Depreciation and Amortization.

Note: All depreciation methods under MACRS that require an election (see **3.**, **4.**, and **5.** above) must be elected on a *timely filed income tax return* (including extensions). The elections are *irrevocable*, and they apply to *all assets within the same class* placed in service in the tax year of the election, with the following exception: if electing ADS for 27.5-, 31.5-, or 39-year property, the election only applies on a property-by-property basis.

Since the first three of these methods use accelerated depreciation methods for the early years of an asset's recovery period, they will result in larger deductions for those years. The last two methods use straight-line and will, therefore, result in equal amounts of depreciation over an asset's full recovery period, except for the first and last years due to the application of the averaging conventions.

Except for the limitations mentioned above, which restrict most of these methods to certain property classes, the selection is left to the taxpayer, who will choose whichever method he feels is most appropriate.

TIP
The following are some of the factors used in deciding which depreciation method to use:

- The straight-line methods obviously simplify record keeping and income forecasting, since future years' depreciation amounts are relatively easy to calculate once an asset is set up on a depreciation schedule.
- Depending on the taxable income a business expects, it may want to choose a method whereby the largest deductions are available in the years of greatest income. For example, if a business purchases an asset and knows that it already has a large amount of taxable income for the year, it might select the accelerated method in 1. or 2. above, in order to maximize its depreciation deductions for the year, thereby reducing income.
- Using the Alternative Depreciation System (ADS) for either personal or real property, or the 150% declining-balance method for personal property, will eliminate the depreciation adjustment for the Alternative Minimum Tax computation.
- The business may have a net operating loss (NOL) being carried over from prior years that is about to expire and, therefore, will elect to use a slower method of depreciation. This will increase the current year's taxable income that can then be absorbed by the NOL, while preserving the depreciation deductions for future years.

Calculating MACRS Depreciation

You can compute MACRS depreciation in two ways:

- either by using percentage tables or
- by making a manual calculation.

Percentage Tables

The easiest method is to use the percentage tables given in Section VI: "Tables." Preceding these tables is a guide to choosing the appropriate table, based on the type of MACRS depreciation method chosen and the averaging convention used. These tables cannot be used if the business has a short tax year or if, for example, the basis of the asset needs to be adjusted for a casualty loss.

How To:

The process of calculating MACRS depreciation when using the percentage tables involves the following 4 steps:

1. Determine the property's recovery period by looking at **Tables 1–3** in Section VI: "Tables." The assets are listed in alphabetical order. The GDS life, needed for the first three depreciation methods described above, is found in these tables and is identified as the MACRS Recovery Period. These tables also give the Alternate MACRS Recovery Period, for use under ADS. For assistance, see "Tables 1–3,"

page VI-2.

2. Turn to "MACRS Percentage Tables," page VI-14, and select the appropriate Percentage Table. To do this you need to know the property's recovery period (determined in Step 1) and the applicable averaging convention, as well as having made a decision as to which method of depreciation you want to use.
3. Turn to the Percentage Table selected in Step 2, and find the applicable percentage by first locating the property's recovery period (or the month placed in service if it is real property) and then finding the year of recovery for which you are computing depreciation.
4. Multiply the property's "unadjusted basis" by the percentage. When using the percentage tables, the unadjusted basis is the basis *not* reduced by any prior depreciation claimed, although it is reduced by any amount for which you elected the Section 179 expense.

In describing the first three MACRS depreciation methods (DDB and 1.5 DB), we mentioned that you must switch to straight-line when it provides a larger deduction. This switch to straight-line is already built into the percentage tables for you.

Example: You need to determine the depreciation for a computer placed in service *last year* that cost $10,000. The business did not need to use the midquarter convention last year, did not elect the Section 179 expense, and used the most accelerated depreciation method possible, 200% DB. The computer is used 100% in the business.

Result:

1. As found in **Table 1**, a computer has a 5-year recovery period.
2. Find the Percentage Table (**Table M 1**) for the 5-year recovery period, using the DDB method of depreciation, and for the half-year convention.
3. Looking down at the far left-hand column, find the *second year* of recovery and then look across to the 5-year column. The percentage is 32%.
4. Multiply 32% times the $10,000 cost for the current year's depreciation of $3,200.

Manual Calculation

You can also compute the deduction using the applicable depreciation method and averaging convention, over the property's recovery period.

The actual mechanics for making the calculations under double- declining balance (DDB), 150% declining-balance (1.5 DB), and straight-line (SL) are all described in Section III: "Depreciation for Financial Reporting." Remember that unlike using the MACRS Percentage Tables, when computing the declining-balance depreciation methods manually, each year the asset's basis will be reduced by any accumulated depreciation taken. Also, when depreciating property under MACRS, although you are using the same basic depreciation methods as for financial reporting, there are three differences:

1. *You must switch to the straight-line method when it provides a larger deduction than the declining-balance method* (this is not optional).
2. *If in the first or final year of depreciation, you must use the correct applicable averaging convention* (the correct convention to use is dictated by statute, not by choice).
3. *Salvage value is never taken into account under the accelerated methods, and it does not reduce depreciable basis under the straight-line method.*

Manual Calculations for Different Methods

For *all* examples below, assume a calendar-year taxpayer and no Section 179 expense is elected.

MACRS Straight-Line Depreciation

We are referring to this as the "MACRS straight-line method," rather than the Alternative MACRS method (ADS), because it is used for property being depreciated over either its GDS or ADS recovery period.

How To:

When computing straight-line depreciation, simply compute what the depreciation would be for a full 12-month year and then multiply this amount by the applicable averaging convention if it is the first or final year.

Example: 5-year property with a depreciable basis of $1,000. Assume the half-year convention.

Result: 1/5 x $1,000 =$200, which is a full year's depreciation.

Year 1:	$200 x 6/12 (half-year convention)	=	$100
Year 2:		=	$200
Year 3:		=	$200
Year 4:		=	$200
Year 5:		=	$200
Year 6:	*$200 x 6/12 (remaining half year)	=	$100
	Total Depreciation	=	$1,000

* Remember that one additional year after the recovery period is always allowed.

Example: Same as above, except assume that the property was placed in service on May 30, and that the midquarter convention applies (due to other property placed in service the same year).

Result:

Year 1:	$200 x 7.5/12 (or 62.5%)	=	$125
Year 2:		=	$200
Year 3:		=	$200
Year 4:		=	$200
Year 5:		=	$200
Year 6:	*$200 x 4.5/12*	=	$75
	Total Depreciation	=	$1,000

* Since the asset was placed in service on May 30, and the midquarter convention applies, it is as if the asset was placed in service at the midpoint of the second quarter of the year. Therefore, it is treated as if used for 7.5 months during its first year. In the final year after the recovery period, the asset is deemed to be used the remaining 1.5 quarters, or 4.5 months (12 months less 7.5 months = 4.5 months).

Example: Consider residential rental property costing $25,000 that has a 27.5-year recovery period and is put into service on September 3. Remember that the midquarter convention never applies to 27.5-year property, so the applicable convention is *always* midmonth.

Result: 1/27.5 x $25,000 = $909, which is a full year's depreciation.

Therefore:

Year 1:	$909 x 3.5/12	=	$265	
Year 2-28:	$909 each year (for 27 years)	=	$24,545	
Year 29:	$909 x 2.5/12*	=	$190	(rounding = 2)
	Total Depreciation	=	$25,000	

* In the year it was placed in service, it received 3.5 months of depreciation. Therefore, since it has a 27.5-year life, it had 2.5 months left to depreciate in the year after the end of the recovery period (27 years, 6 months less 27 years, 3.5 months = 2.5 months).

MACRS Declining-Balance Methods

Both the 200% and the 150% declining-balance methods are available. Again, the simplest way to handle the computations is to compute depreciation for a full year and then apply the applicable averaging convention.

How To:

Taken by steps:

1. Divide 1 by the recovery period to determine the rate.
2. Determine the depreciable basis of the asset, reduced by prior depreciation taken.
3. Determine the declining-balance rate: 2 for 200% and 1.5 for 150%, depending on the class of property being depreciated and the method being used.
4. Determine the applicable averaging convention if this is the first or final year for depreciating the property.
5. Multiply the result of each step by the following step.

Example: Consider 5-year property with a depreciable basis of $1,000. Assume no depreciation elections are made and the half-year convention applies.

Result: 5-year property uses the 200% declining-balance method.

1. 1/5 = 20%.
2. For year 1, the depreciable basis is $1,000.
3. 5-year property uses the 200% rate (we are not electing to use the 150% rate over the ADS life), so we use “2”.
4. Half-year convention is 6/12.
5. 20% x $1,000 x 6/12 x 200% = $200 = Depreciation for year 1.

For year 2: Same as above, except subtract out the prior depreciation ($200) from the basis, and the averaging convention does not need to be considered:

20% x ($1,000 – $200) x 2 = $320

Example: Same as above, but assume the midquarter convention, with the asset being placed in service February 20.

Result: Same as above, except the midquarter convention results in:
10.5/12 = 87.5% for Step 4.

Year 1:	20% x $1,000 x 2 x 87.5%	=	$350
Year 2:	20% x ($1,000 – $350) x 2	=	$260
Year 3:	20% x ($1,000 – $610) x 2	=	$156
Year 4:	20% x ($1,000 – 766) x 2	=	$ 93.60

However, switching to straight-line depreciation (Remaining Value over Remaining Life) is required when it produces a greater amount, which it does in year 4:

Year 4: $\dfrac{\textit{Remaining basis (\$1,000 – \$766)}}{\textit{Remaining life of 2.125 years}}$ = $110

Year 5: Continuing with the straight-line method:

$\dfrac{\textit{Remaining basis (\$1,000 – \$876)}}{\textit{Remaining life of 1.125 years}}$ = $110

Year 6: When converting to straight-line from a declining-balance method, at the beginning of any tax year when the remaining recovery period is less than 1 year, the applicable rate for that year is 100%. Therefore, the final year's depreciation is $14.

MACRS Alternative Depreciation System (ADS)

The Alternative Depreciation System under MACRS may be elected for any class of property. It basically uses the straight-line method (although salvage value is ignored), with the same MACRS averaging convention rules, but usually over a longer recovery period.

When ADS Is Required

There are certain types of property for which ADS *must* be used:

- "Luxury" cars and "Listed" property if used 50% or more for personal use. (See Section IV: "Chapter 4: Passenger Automobiles and Other Listed Property.")
- Tangible property used predominantly outside the United States (see IRS Code Sec. **168(g)(4)**).
- Any tax-exempt use property (see IRS Code Sec. **168(h)**).
- Tax-exempt bond financed property (see IRS Code Sec. **168(g)(5)**).
- Certain imported property (see IRS Code Sec. **168(g)(6)**).
- All farm property, if the farm has elected not to apply the uniform capitalization rules, per IRS Code Sec. **263A(d)(3),** to any plant or animal produced.

Note: ADS must also be used by a corporation when computing depreciation on any MACRS property for calculating Earnings and Profits.

When ADS Is Elected

The Alternative Depreciation System may be used for any MACRS depreciable property. For residential rental property and for nonresidential real property, the election may be made on a property-by-property basis. For all other property, when the election is made, it will apply to all property in that particular property class that is placed in service during the tax year of the election. For example, let's say the election is made to use ADS on a computer placed in service this year. Since a computer is 5-year property, ADS must also be used on any other 5-year property placed in service this year. The election to use ADS is made on a year-by-year basis.

How To:

The election to use ADS is made by completing line 20 of Part III of IRS Form 4562, Depreciation and Amortization.

Recovery Periods Under ADS

Although sometimes the recovery periods under the Alternative Depreciation System are the same as under regular MACRS, generally they are longer. The chart below lists some of the property types that have significantly longer recovery periods. Remember that the ADS recovery periods for all property may be found by looking at **Tables 1–3** in Section VI: "Tables."

Property Type	ADS Recovery Period
Personal property with no class life	12 years
Residential rental property	40 years
Nonresidential real property (31.5- and 39-year property)	40 years
Single-purpose agricultural structures	10 years
Trees and vines bearing fruit or nuts	20 years

Short Tax Years

MACRS depreciation is computed on a tax-year basis. Recovery periods, however, are based on 12-month periods, without regard to the tax year. This is why, for example, 3-year property using the half-year convention is actually depreciated over 4 tax years.

A short tax year is any year with less than 12 months. This can happen at any time, such as when a taxable entity changes its tax year, but most commonly occurs when an entity first starts doing business. If depreciable property is placed in service during a short year, the process of calculating depreciation is different from when the short year occurs after you have started to depreciate an asset. This is due to the averaging conventions that need to be used when property is first placed in service.

In either case, however, the percentage tables may *not* be used when a short tax year is involved. The basic procedure is first to determine depreciation for a full 12 months and then to multiply it by a fraction:

$$\frac{\textit{Number of months (including half months) property is deemed placed in service}}{12^{*}}$$

* Note that the denominator is *always* 12, even when making a short-year calculation. The objective is to determine the number of *months* the property is considered to be in service, and then multiply this by the calculated full year's depreciation on the property.

Property Placed in Service in a Short Year

A short tax year will affect the application of both the half-year and the midquarter averaging conventions. It has no effect on the midmonth convention, however.

Half-Year Convention

Since under the half-year convention the asset receives a half-year's worth of depreciation, this will obviously be a lesser amount if the year is less than 12 months.

How To:

When applying the half-year convention to a short year, the averaging convention, instead of being: 6 months/12 months, will now have a numerator that reflects half of the number of months the tax year consists of, and a denominator that will always be 12.

All tax years are considered to start as of the first day of a month. Therefore, if a corporation starts doing business on September 23, the tax year is treated as beginning on September 1. Also, if there are successive short years with 1 year ending and the next year beginning in the same month, the first short year will not include the "shared" month. This prevents any month being taken into account twice.

Example: XYZ, a calendar-year corporation, starts doing business on May 17 and places in service all of its equipment on the same day.

Result: The tax year has 8 months, and its equipment, using the half-year convention, will be treated as being used for 4 months. When computing depreciation on the equipment, go through the same steps as usual, except use 4/12 when multiplying by the averaging convention.

Example: Assume the above corporation had started business on June 3.

Result: The short year consists of 7 months. The fraction to be used would, therefore, be 3.5/12.

Example: A business has 2 short tax years. The first year begins May 1 and ends August 5. The second year starts August 6 and ends January 31.

Result: The first year is deemed to have 3 months, consisting of May, June, and July. The second year has 6 months, consisting of August through January.

The above computation is slightly more complex when a short tax year begins on a day other than the first day of a month *and* ends on a day other than the last day of a month. When this occurs the computation must be made initially on the basis of days.

How To:

Determine the number of days in the short year and then divide by 2. If the resulting date is not either the first or midpoint of a month, then the property is treated as placed in service (or disposed of) on the nearest *preceding* first or midpoint of that month.

Example: A business has a short tax year beginning March 4 and ending June 21.

Result: The short tax year consists of 110 days, with the midpoint being 55 days, or April 27. The property is considered to be put in service on April 15.

Property subject to the half-year convention is, therefore, always treated as placed in service (or disposed of) on either the first day or on the midpoint of a month.

Midquarter Convention

Remember that when determining whether or not the midquarter convention applies, you need to look at the depreciable basis of qualifying property placed in service during the **last 3 months of the year**. It is immaterial how short the tax year is. Therefore, a tax year of 3 months or less will automatically require that the midquarter convention be used.

How To:

1. Determine the number of months in the year and divide by 4, thereby dividing the year into quarters.
2. Divide a quarter by 2 to determine the midpoint.

   If the year has either 4 or 8 months, you can determine the length of a quarter on the basis of whole months. If this is *not* the case, you need to determine the quarters on the basis of actual days. Then, if the quarter divided by 2 results in a day that is not either the first or midpoint of a month, treat the property as being placed in service on the *nearest* preceding first or midpoint of that month.
3. Calculate the depreciation for a full year and then multiply by the following fraction:

$$\frac{\textit{Number of months (including half months) property is deemed placed in service}}{12}$$

Example: XYZ started business on April 10, and is a calendar-year corporation. 5-year property costing $1,000 was placed in service November 7, and the midquarter convention applies.

Result: Since the tax year consists of 9 months, you must calculate on the basis of days. The tax year has 264 days. Divide 264 by 4 to determine that a quarter consists of 66 days. Divide 66 by 2 to get the midpoint of each quarter, which is the 33rd day. The following chart shows the quarters for the year, the midpoint of each quarter, and the date in each quarter when property will be considered to be placed in service:

Quarter	Midpoint	Date Deemed Placed in Service
April 10–June 14	May 12	May 1
June 15–Aug. 19	July 17	July 15
Aug. 20–Oct. 24	Sept. 22	Sept. 15
Oct. 25–Dec. 31	Nov. 26	Nov. 15

In this example the property will be treated as placed in service on November 15. The calculation is as follows:

1/5 x $1,000 x 2 (DDB) x 1.5/12 = $50

Subsequent Tax Years

When property is placed in service during a short year, you will need to manually compute the depreciation in all subsequent years for that property. This may be done by one of two methods: the **simplified method** or the **allocation method**. Whichever method is chosen must be used consistently until the year of change to the straight-line method.

Simplified Method

How To:

Compute depreciation in all subsequent years by multiplying the unrecovered basis of the property (i.e., its depreciable basis less all prior year's depreciation) by the applicable depreciation rate.

Example: In the last example above, XYZ placed in service 5-year property in a short year, costing $1,000, and deducted $50 of depreciation the first year, using the midquarter convention.

Result: The applicable depreciation rate is:

1/5 x 2 (DDB) = 40%

Tax Year	Method			Depreciation
1	DDB	40% x $1,000 x 1.5/12	=	$ 50
2	DDB	40% x ($1,000 – $50)	=	380
3	DDB	40% x ($1,000 – $430)	=	228
4	DDB	40% x ($1,000 – $658)	=	137
5	SL*	($1,000 – $795) / 1,875	=	109
6	SL		=	96
		Total Depreciation	=	$1,000

* Note that in the fifth year, the deduction is greater under the straight-line method, so the switch to straight-line is made. During the first year, the property was depreciated for 1.5 months. Therefore, in the fifth year, the remaining life is:

	5 years	or	60 months
less	3 years and 1.5 months	or	37.5 months
equals	1 year and 10.5 months	or	22.5 months
therefore	22.5 months / 12	=	1.875 years

Allocation Method

How To:

Compute depreciation in all subsequent years by allocating to the tax year the amount of depreciation attributable to each recovery year, or part of a recovery year that falls within that tax year. For each recovery year included in a tax year, multiply the attributed amount of depreciation by a fraction:

$$\frac{\textit{Number of months (including half months) of recovery year included in tax year}}{12}$$

Because of the short tax year and averaging convention, the first year that an asset is depreciated the taxpayer will deduct only the depreciation from a portion of the recovery period's first 12-month period. Therefore, the second (and each subsequent) tax year the taxpayer will claim depreciation for:

- the remaining portion of the previous year's recovery period's depreciation *and*
- a portion of the current recovery period's depreciation.

Example: XYZ, a calendar-year corporation, placed in service 5-year property costing $1,000 on April 3. It started business on March 15 and the half-year convention applies.

Result:

Tax Year	Method				Depreciation
1	DDB	40% x $1,000 x 1.5/12*	=		$ 167
2	DDB	40% x $1,000 x 7/12	=	$233	
	plus	40% x ($1,000 – $400) x 5/12	=	100	333
3	DDB	40% x ($1,000 – $400) x 7/12	=	$140	
	plus	40% x ($1,000 – $640) x 5/12	=	60	200
4	DDB	40% x ($1,000 – $640) x 7/12	=	$ 84	
	plus	40% x ($1,000 – $784) x 5/12	=	36	120
5	SL	$\frac{(\$1,000 - \$820)}{1.58^{**}}$	=		114
6	SL		=		66
		Total Depreciation	=		$1,000

* Since the half-year convention applies and this is a short tax year of 10 months, the half-year convention fraction is 10 : 2 = 5, which is then divided by 12.

** Note that the switch to straight-line is made the fifth year. At the start of the fifth year, the property had been depreciated for 3 years and 5 months, leaving 19 months of the recovery period: 19/12 = 1.58 years.

TIP
Generally, both the simplified and the allocation methods will result in the same amount of depreciation. However, if after the first year, but before the year switching to straight-line, there is either another short year or a disposition of the property, then the simplified method will produce less depreciation than under the allocation method.

Bonus Depreciation

If property is placed into service in a short year, and either the 30%, 40%, 50%, or 100% first-year depreciation deduction is claimed, this first-year deduction is NOT prorated for the short year.

Short Year After the Property Is Placed in Service

Sometimes although the property has only been depreciated during 12-month tax years, at some time before the end of its recovery period, a short tax year may occur. At that point, if you had been using the percentage tables, you will not be able to continue to do so for any property being held and not yet fully depreciated.

How To:

Multiply the unrecovered basis of the property by the applicable depreciation rate, and then by the following fraction:

$$\frac{\textit{Number of months (including half months) in the tax year}}{12}$$

Property Disposed Of in a Short Year

Basically all of the preceding discussion also pertains to when you dispose of property during a short year. For further clarification, see "If a Short Year Occurs in the Year of Disposition," page IV-65.

Early Dispositions

An early disposition occurs when property is sold, exchanged, retired, abandoned, or destroyed before the end of its recovery period. **If a business acquired and disposed of personal property in the *same tax year*, no depreciation is allowed for that asset** (per *final* IRS Reg. **1.168(d)-1**, effective for tax years ending after 1/30/91). For all other MACRS property, you are allowed to depreciate the property in the year of the disposition. You must use the same averaging convention as you did in the year when the property was initially placed in service.

TIP
If a business sells depreciable property on an installment sale, it must include as ordinary income to the extent of gain in the year of sale, all depreciation taken on the property, even if no payments on the sale are received the first year. It is, therefore, advisable to have the buyer make a first-year installment payment to at least cover the tax liability on the amount of gain to be recognized.

If the Midmonth Convention Was Used

If the midmonth convention was used when the property was first placed in service and, in a later year, the property is disposed of, it is treated as if disposed of in the middle of the month in which the disposition occurs.

How To:

If you have been using the percentage tables, you may do so in the year of disposition. Determine the amount of depreciation for the full year as if it had not been disposed of. Next multiply by the following fraction:

$$\frac{\textit{Number of months (including half months) in service for the year}}{12}$$

Example: XYZ, a calendar-year business, purchased 27.5-year property (residential rental property) costing $100,000 on July 10. It sold the property the following year on April 2.

Result: When using the percentage tables:

In the first year, you used **Table M 6** and the column for the seventh month, the month placed in service. Look at the same chart, in the same seventh month column, and the percentage for the second year is 3.636%. Compute depreciation for the full year but then multiply the result by the number of months held this year (3.5 months) and divide by 12:

10 = $100,000 x .03636 x 3.5/12 = $1,060

Result: When computing depreciation manually:

Determine the depreciation for the full year and multiply by the same fraction as above:

1/27.5 x $100,000 x 3.5/12 = $1,060

If the Half-Year Convention Was Used

If the half-year convention was used in the year in which the property was placed in service and the property is disposed of anytime during a subsequent year, it is treated as if disposed of in the middle of the year.

How To:

As above, whether using the percentage tables or computing depreciation manually, determine the amount of depreciation for the full year and multiply by the following fraction:

$$\frac{\textit{Half the number of months in the tax year}}{12}$$

If the Midquarter Convention Was Used

If the midquarter convention was used initially and the property is later disposed of, the property is treated as if the disposition occurred during the middle of the quarter of the tax year.

How To:

Determine the depreciation for the full year and multiply by the percentage for that quarter of the tax year in which the disposition occurred:

Quarter of the year in which property is disposed	Percentage
1st	12.5%
2nd	37.5%
3rd	62.5%
4th	87.5%

If a Short Year Occurs in the Year of Disposition

If a disposition of property occurs in a short tax year and either the half-year or midquarter convention was used during the year the property was first placed in service, observe the following formula:

How To:

$$\begin{matrix}\textit{Unrecovered Basis} \\ \textit{of the Property}\end{matrix} \times \begin{matrix}\textit{Depreciation} \\ \textit{Rate}\end{matrix} \times \frac{\textit{Number of Months Property was in service for the yr.*}}{12}$$

* In order to determine the number of months the property was in service for the year of disposition, refer to the preceding segment "Short Tax Years," page IV-57.

Remember the following:

1. *You cannot use the percentage tables in a short year.*
2. *If it is 27.5-, 31.5-, or 39-year property, the midmonth convention was used, and a short year will have no effect on the computation.*

Property Excluded From MACRS

Certain categories of property are specifically excluded from being depreciated under MACRS. When this occurs, such property must be depreciated under ACRS (explained in Section IV: "Chapter 5: Accelerated Cost Recovery System (ACRS).") or one of the other methods of depreciation that existed before ACRS (discussed in Section IV: "Chapter 6: Depreciation of Nonrecovery Property."). Property that is *excluded* from MACRS includes:

- Any portion of an otherwise depreciable asset for which the Section 179 expense was elected (see Section IV: "Chapter 1: First-Year Expensing.").
- Property that the business elected to depreciate over a method that is not based on a life in years, such as a Production or Use Method (see Section III: "Depreciation for Financial Reporting."), or the **Income Forecast Method** (explained in Section IV: "Chapter 6: Depreciation of Nonrecovery Property.").
- Films, videotapes, and sound recordings (see Section IV: "Chapter 6: Depreciation of Nonrecovery Property.").
- Intangible assets, which are amortized (see Section II: "Amortization.").
- Certain public utility property, unless a normalization method of accounting is used.
- Property subject to the anti-churning rules explained below.

Anti-Churning Rules

Special rules were created to prevent the "churning," or conversion, of pre-1981 depreciable property into recovery property (which results in larger depreciation deductions), without an appropriate change in ownership or use. These rules were, therefore, initially enacted to prevent the use of ACRS for certain property, and then were continued to apply to certain MACRS property as well.

Anti-Churning Transactions

In order for property acquired after 1986 to fall under the anti-churning rules, and thus not be subject to MACRS, the property must be acquired in one of the following types of transactions:

- The taxpayer or a related party owned or used the property in 1986.
- The taxpayer leases the property to an entity (or a related party) that owned or used the property in 1986.
- It is personal property that was acquired from someone who owned it in 1986 and, as part of the transaction, the user of the property does not change.
- It is personal property that was not MACRS property in the hands of the previous owner from whom acquired and the user of the property does not change after the acquisition.
- It is real property that was acquired in a transaction in which some gain or loss was not recognized. MACRS only applies to the portion of the basis for which the business paid cash or gave unlike property.

Note: The first two types of transactions apply to both personal and real property, the third and fourth types apply only to personal property, and the last transaction type applies only to real property. Also, under the anti-churning rules, property is not considered as owned before it is placed in service.

Exceptions to Anti-Churning Rules

Even though the anti-churning rules are designed to prevent the conversion of pre-1981 property into MACRS property, there are several important exceptions. The following property placed in service after 1986 and acquired by the taxpayer in one of the types of transactions described above must still be depreciated under MACRS:

1. All 27.5-year residential rental property.
2. All 31.5- and 39-year nonresidential real property.

   Note: The reason that real property placed in service after 1986 is generally depreciated under MACRS is because MACRS produces less depreciation on real property, in the above two classes, than ACRS with its shorter recovery periods.

3. **Any property for which the ACRS deduction for the first year in which the property is placed in service would be greater than the MACRS deduction** (assuming the half-year convention).

   In other words, if the property falls under the anti-churning rules, you must depreciate it under whichever method (ACRS or MACRS) will give you the **least** amount of depreciation the **first** year it is placed in service.

   The following chart will assist you in determining if a larger deduction will be claimed under MACRS or ACRS (although you will need to study Section IV: “Chapter 5: Accelerated Cost Recovery System (ACRS).”, on ACRS to determine the assigned recovery period under ACRS, since the property classes for the two methods are not the same):

Recovery Period	First-Year Depreciation Percentage	
	MACRS	ACRS
3-year	33.33%	25%
5-year	20%	15%
7-year	14.29%	N/A
10-year	10%	8%

TIP
If property has the same recovery period under both ACRS and MACRS, then the depreciation deduction under ACRS will always be less.

4. Any real property that is used for personal use before 1987 and converted to business use after 1986. The anti-churning rules do not apply to such property, and MACRS must be used.

Related Party Rules

The rules for determining whether or not a person is a related party for the anti-churning rules are applied at the time the property is acquired by the taxpayer. Some examples of related parties (see IRS Code Sec. **267** and **707** for more detail) are:

- An individual and a member of his immediate family.
- A corporation and an individual who owns, directly or indirectly, more than 10% of the outstanding stock.
- Two corporations that are members of the same controlled group.
- A partnership and a person who owns, directly or indirectly, more than 10% of the capital or profits of the partnership.
- Two partnerships if the same persons own, directly or indirectly, more than 10% of the capital or profits of each.
- Two S corporations if the same persons own more than 10% of the outstanding stock.
- An S corporation and a C corporation if the same persons own more than 10% of the outstanding stock of each corporation.
- A corporation and a partnership if the same persons own more than 10% of the outstanding stock of the corporation and more than 10% of the capital or profits of the partnership.

Anti-Churning Depreciation Methods

If property falls under the anti-churning rules and, therefore, cannot be depreciated under MACRS, then the original date placed in service determines the correct depreciation method to use:

Date First Placed in Service	Depreciation Method
Before 1981	Pre-ACRS methods: SL or DB and based on useful life
After 1980	ACRS *unless* MACRS is less

Section 30: Tax Credit for Qualified Electric Vehicles

The Energy Policy Act of 1992 created a 10% credit for qualified electric vehicles placed in service after June 30, 1993, and before the year 2005, of up to $4,000 (IRS Code Sec. **30**). The Job Creation and Worker Assistance Act extended the credit to purchases through December 31, 2006. The 2005 Energy Bill sunsets the deduction for certain clean fuel vehicles and refueling property after 2005 instead of after 2006 as had previously been scheduled but new credits for alternative fuel powered vehicles were introduced in this bill.

The depreciable basis of the asset is reduced by the full amount of the credit. Any portion of a qualified vehicle that is expensed under IRS Code Sec. 179 is not eligible.

If an amount of the Section 30 credit is not used in the year in which it is claimed—because of the lack of tax liability—it is lost. Any unused credit may not be carried back or forward.

How To:

The Section 30 credit for qualified electric vehicles is claimed on IRS Form 8834.

Section 30 Recapture Rules

The Section 30 credit must be recaptured if, within 3 years from the date the vehicle was placed in service, it ceases to qualify as an electric vehicle. A disposition of the vehicle does *not* trigger recapture unless the seller knows that it will be modified in such a way that it will no longer qualify for the credit.

How To:

The amount to be recaptured is:

The original amount of the Section 30 credit *times*:

- 100%, if the recapture event occurs within the first full year after it is placed in service.
- 66 2/3%, if the recapture event occurs within the second full year after it is placed in service.
- 33 1/3%, if the recapture event occurs within the third full year after it is placed in service.

The recapture amount is included in taxable income for the year in which the recapture event occurs. It will also increase the basis of the property.

We have included IRS Code Section 30 in Section VII: "Quick Reference."

Section IV: Chapter 3: Tax Credits for Fixed Assets

In this section:

Investment Tax Credit

The investment tax credit (ITC) provides several tax credits that are available for fixed assets. As a reminder, a tax credit reduces the amount of tax to be paid, whereas a tax deduction reduces the amount of net income subject to tax. A general tax credit of 6% or 10% was available for a wide range of qualifying assets placed in service 1976 through 1985. Since then, the ITC has been focused on specific types of property. Current credits include:

- Qualified rehabilitation credit
- Energy credit
- Qualifying advanced coal project credit
- Qualifying gasification project credit
- Qualifying advanced energy project credit

Each credit is determined separately and has different provisions. The amount of each credit varies and can range from 10%-30% of the asset's cost. Generally, when a credit is claimed on an asset, the asset's depreciable basis is reduced by the amount of the credit. Furthermore, most credits claimed on fixed assets are temporary and are only available for a limited time period.

The investment tax credit is claimed on Form 3468 and is a component of the General Business Credit.

ITC Recapture

When an asset, for which ITC was taken, is disposed of before the end of its estimated life, a portion of the ITC is added back to the tax liability, also known as the ITC recapture. The ITC recapture amount is calculated by multiplying the ITC taken by a recapture percentage which is based on how long the asset was held. The ITC recapture is reported on Form 4255. If the asset's basis was reduced for the original ITC, a percentage of the recaptured amount must be added back to the asset's basis.

Section IV: Chapter 4: Passenger Automobiles and Other Listed Property

In this section:

When you think of listed property, that is a good way of remembering some of the included categories, although listed property encompasses much more. Properties that lend themselves to personal use are listed property (IRS Code Sec. **280F**). The most common type of listed property is passenger automobiles.

There are special rules for the depreciation of listed property, as well as record-keeping requirements, which differ from other types of property. These special rules cannot be avoided by leasing listed property, since there are specific limitations on leasing arrangements as well.

The limitations on the amounts of depreciation that may be claimed on listed property are based on the type of property (a passenger car, defined below, will *always* be limited) and by type of use (qualified business use is explained below). Furthermore, for this purpose, "depreciation" includes the Section 179 expense deduction as well.

Definition of Listed Property

Listed property consists of the following property placed in service after June 18, 1984:

- Passenger automobiles.
- Any other type of transportation property.
- Any property generally used for entertainment, recreation, or amusement.
- Any computer and related peripheral equipment. *
- Any cellular telephone or similar telecommunications equipment. **

* The Tax Cuts and Jobs Acts removes computers and related peripheral equipment from their current classification as listed property under Code Section 280F for tax years beginning after December 31, 2017.

** The Small Business Jobs Act of 2010 removes cell phones and similar personal communication devices from their current classification as list property under Code Section 280F for tax years beginning after December 31, 2009.

Passenger Automobiles

A passenger automobile is any four-wheeled vehicle intended by the manufacturer to be primarily used on public streets, roads, and highways and is placed in service after June 18, 1984. Such a vehicle is rated at 6,000 pounds or less of unloaded gross vehicle weight. Trucks and vans are treated the same as automobiles under this rule if their gross vehicle weight is 6,000 pounds or less. A passenger automobile includes all parts, components, or items physically attached to the automobile or traditionally included in the purchase price of the vehicle.

Note: Although such automobiles are referred to as "luxury" vehicles, they do not have to be luxurious in any way.

A passenger automobile does *not* include:

- Ambulances.
- Hearses.
- Any vehicle used directly in a business that transports people or property for hire (e.g., taxis, limousine services, etc.).
- Certain commuter highway vehicles placed in service before 1986 (IRS Code Sec. **46(c)(6)(B)**).
- Qualified nonpersonal use vehicles.

Other Transportation Property

Other transportation property includes trucks, buses, boats, airplanes, trains, motorcycles, and any other vehicles used for transporting people or goods.

It does *not* include transportation property that by its nature is not likely to be used more than a minimal amount for personal purposes. Examples of such vehicles are police and fire vehicles (including unmarked police vehicles if their use is officially authorized), cement mixers, dump trucks, garbage trucks, forklifts, refrigerated trucks, moving vans, and any vehicle designed to carry cargo with a loaded gross vehicle weight over 14,000 pounds. Delivery trucks are not included if they have seating for the driver only or for the driver only plus a folding jump seat. School buses are never included, nor are other buses with a seating capacity of 20 or more passengers.

Property Used for Entertainment

Property used for entertainment, recreation, or amusement includes property such as photographic, phonographic, communication, and video recording equipment. It does *not* include such property, however, if it is used either exclusively at the business establishment or in connection with a principal trade or business.

Computers and Peripheral Equipment

The Tax Cuts and Jobs Acts removes computers and related peripheral equipment from their current classification as listed property under Code Section 280F for tax years beginning after December 31, 2017.

Computers and peripheral equipment are listed property unless they are used exclusively at the business establishment. Peripheral equipment is any auxiliary machine (whether on-line or off-line) that is designed to be controlled by the central processing unit of a computer.

Computer or peripheral equipment does *not* include:

- Equipment that is an essential part of other property that is not a computer.
- Typewriters, calculators, copiers, and similar equipment.
- Equipment used mainly for the user's amusement or entertainment.

Telecommunications Equipment

The Small Business Jobs Act of 2010 removes cell phones and similar personal communication devices from their current classification as list property under Code Section 280F for tax years beginning after December31, 2009.

All cellular telephones and similar telecommunications equipment qualify as listed property if either placed in service or leased in tax years beginning after 1989.

Qualified Business Use

If listed property is *not* used predominantly for business, the amount of depreciation claimed will be limited and no Section 179 expense deduction will be allowed. To be used predominantly for business means that the property must be used *more than 50%* of the time for "qualified business use" during any tax year. This is referred to as either the "predominant use test" or the "more than 50% test."

Note: When we speak of qualified business use and its predominant use test, keep in mind that these are specialized terms used in connection with listed property only. Earlier, both in our previous explanations of the "Elements of Depreciation," page I-7, and again in "Depreciable Basis Determination for Midquarter," page IV-47, we discuss "depreciable basis," which includes that portion of the property's basis that is used in the business rather than for personal purposes. Here, qualified business use is much more restrictive.

Qualified business use is any use in a trade or business (*it cannot simply be held for the production of income*), but does *not* include:

1. Leasing of property to any *more than 5%* owner or related party to the extent that it is used by such owner or related party.

   Note: See the discussion of related parties under the "Anti-Churning Rules," page IV-66, except substitute "more than 50%" ownership for the "more than 10%" ownership used for the anti-churning rules.

2. Use of property as compensation for services performed by:
   - **a.** Any *more than 5%* owner or related party, or
   - **b.** Any other person. However, unlike the *more than 5%* owner or related party, if the value of the property's use is included in the person's taxable income, such use will still be included as qualified business use.

Note: If an aircraft is used at least 25% of the time for qualified business use, the above exclusions do not apply. Any use by a more than 5% owner or related party will be considered qualified business use (IRS Code Sec. **280F(d)(6)(C)(ii)**).

Example: A business uses a computer 50% of the time to manage its investments (usually off site), 40% of the time in its consumer research business, and 10% of the time for an employee to play games on it (such time is *not* considered compensation for services).

Result: The qualified business use does not exceed 50% and the computer, therefore, fails the predominant use test. However, its depreciable basis will be 90% of its acquired value: 50% that is used for investment purposes plus the 40% that is used for business purposes.

Example: A business owns several vehicles that are used for business purposes, but that the employees are allowed to use occasionally for personal use. The value of any such use is added to the employees' gross income and tax is withheld.

Result: Since the personal use is reported as income to the employees, the vehicles are considered to be used 100% of the time in qualified business use.

Example: Same as above, except that instead of employees using the vehicles, they are being used occasionally for personal use by the two 50% shareholders.

Result: Even though the value of the vehicles' use is being added to the shareholders' gross income, because the two shareholders are more than 5% owners, any personal use by them will not be considered qualified business use.

The Predominant Use Test Requires Allocation

If any property is used for more than one purpose, its use must be allocated to the various functions for which it is used. For transportation vehicles, you may allocate their usage based on mileage. For all other property, the allocation should be made based on units of time.

Note: Commuting cannot be qualified business use even if work, such as a business call or a meeting, is performed during the trip. Also, if the vehicle has an advertising display on it, that will not convert any otherwise personal use to business use.

Example: XYZ Corporation has a vehicle that is driven by the 100% shareholder to and from work. The vehicle has the company's logo painted on the side. The value of the vehicle's use is reported to the shareholder as income and tax is withheld. The vehicle was driven 20,000 miles this tax year, of which 10,000 was for the shareholder's commute.

Result: Since the vehicle is used by a more than 5% owner, the mileage it is driven for commuting purposes is not qualified business use, even though its value is reported as income and tax is withheld. It is also of no importance that the company's logo is on the vehicle. To compute the vehicle's qualified business-use percentage:

$$\frac{\text{10,000 qualified business use miles}}{\text{20,000 total miles driven for year}} = 50\%$$

Therefore the vehicle does *not* pass the 50% test, since the qualified business use must be *more than 50%*.

Example: XYZ has a desktop computer that it allows its employees to use at home for personal purposes after hours (this is not considered compensation for services). This past tax year, the computer was used for 2,500 hours, of which 2,000 were used strictly in the business.

Result: The qualified business use exceeds 50%:

$$\frac{\text{2,000 hours used in the business}}{\text{2,500 hours of total use}} = 80\%$$

However, only 80% of the asset's basis may be depreciated this year, as the personal use portion does not qualify for depreciation purposes.

Applying the Predominant Use Test

If listed property is used more than 50% for qualified business use the first year it is placed in service, for each tax year thereafter, a new determination must continue to be made to see if it still passes the predominant use test. This must be done every year during the longer straight-line recovery period, which would have been required if the property had failed the test (see the next segment, "Depreciation Limitations on Listed Property," page IV-78).

Example: Five-year ACRS class property is placed in service in 1985 and is used 100% for qualified business use.

Result: The predominant use test must be applied each year for 12 years, since that is the recovery period it would have been depreciated over had it previously failed the test. This continues to hold true even after the property is fully depreciated at the end of its 5-year recovery period.

Once listed property fails the more than 50% use test, the straight-line method must be used for that year and *all later years*. This is true even if the qualified business use increases to over 50%. *Straight-line depreciation must continue to be used.*

Depreciation Limitations on Listed Property

If any listed property is not used more than 50% in qualified business use, the Section 179 expense may not be elected for it and the property must be depreciated under the straight-line method.

If the property was placed in service after 1986, it must be depreciated under the MACRS Alternative Depreciation System (ADS). Under ADS, the property will be depreciated using the straight-line method, generally over a longer recovery period (see Section IV: "Chapter 2: Modified Accelerated Cost Recovery System (MACRS)." for a complete description of the ADS method).

If the property was placed in service before 1987, determine the ACRS class of property and depreciate it using the straight-line method over the following periods:

Class of Property	Recovery Period for Listed Property
3-year property	5 years
5-year property	12 years
10-year property	25 years
18- or 19-year real property	40 years

If you are required to use the above recovery periods for ACRS listed property, use the percentages from **Tables ALP 1 and 2** in the back of this guide for computing depreciation.

Note: The required use of straight-line depreciation for listed property does not constitute an "election." Therefore, it will not have to be used for all property with the same class life.

Any improvements made to listed property that are capitalized (i.e., recorded as depreciable assets) must be depreciated under the same method as the listed property to which they are attached and are subject to the same limitations.

Since the predominant business use test must be applied each tax year, listed property may initially fail the test either in the year it is first placed in service or in any subsequent year during its recovery period.

Predominant Use Test Failed in Year Property Is Placed in Service

If during the first tax year when listed property is placed in service, it is not used more than 50% of the time in qualified business use, the property is not eligible for the Section 179 expense deduction. Depreciation must be computed according to ADS if it is MACRS property, or by straight-line ACRS over the listed property recovery lives if it is ACRS property.

Example: XYZ buys a computer for $5,000 and uses it:

- 40% of the time in the business,
- 35% for investment purposes (i.e., held to produce income) for the business, and
- 25% for personal use by a shareholder at home.

Result: Since the qualified business use is only 40%, XYZ cannot elect the Section 179 expense deduction and must use the ADS method for depreciating the computer. The computer has a 5-year recovery period under ADS. Only the business use portion of the asset may be depreciated:

40% + 35%* = 75%

1/5 x 5,000 x 75% (business use portion) x 6/12 (half-year convention) = $375

* Even though the 35% portion used for investment purposes of the business constitutes business use for claiming depreciation, it does not constitute qualified business use for the listed property's predominant business use test.

Later Years' Deductions

As stated earlier, once listed property fails the predominant use test, the straight-line method must continue to be used for the remainder of its straight-line recovery period. However, additional consideration needs to be given if, in a later year during the recovery period, the property's personal use is either reduced or eliminated. When this occurs, you will need to determine if there is any unrecovered basis still to depreciate in that later year.

How To:

To make this determination, compute depreciation for the earlier tax years as if the property had been used 100% for business (per IRS Reg. **1.280F-4T(a)(1)**).

Example: Assume that the computer in the previous example is depreciated for its full recovery period and that its use remained the same. Each year, therefore, only 75% of the otherwise allowable depreciation was deducted. In the year following the recovery period, the asset is changed to being used 100% in business.

Result: No more depreciation may be taken on the asset. If the asset had been used 100% in business, it would have been fully depreciated after 6 years (5-year MACRS property is depreciated in 6 years due to the use of the half-year convention). Therefore, there is no remaining basis to be recovered.

Predominant Use Test Failed in Subsequent Tax Year

Sometimes although listed property is used predominantly for qualified business use when it is first placed in service, during a later year that use may fall to 50% or less. If this occurs during any year during its recovery period (and remember that you must make this determination during the longer recovery period, as if ADS or straight-line ACRS is being used), depreciation recapture occurs, and income will need to be recognized.

The amount of income to be recognized (with the same amount also to be added back to the property's depreciable basis) is the difference between the amount of depreciation previously taken (before failing the more than 50% test) and the amount of depreciation that would have been allowed had the property failed the more than 50% use test the first year it was placed in service.

Note: When calculating depreciation recapture for listed property, you use only the depreciation amounts for the tax years before the first tax year in which the property was not predominantly used for qualified business use. This is different, therefore, from computing depreciation recapture for nonlisted property. For the latter, you include the year in which the recapture is triggered.

How To:

	Accelerated Depreciation Taken to Date (i.e., before failing the more than 50% use test)	=	________		
plus	Any Section 179 Expense (but only if actually deducted*)	=	________		
	Subtotal			=	________
minus	Straight-Line Depreciation: ADS or SL ACRS (computed from year 1 of the asset's recovery period)**			=	( )
equals	Amount of Depreciation Recapture (to be recognized as income and added back to the asset's depreciable basis)			=	________

* If the Section 179 expense deduction was claimed but not expensed, due to the taxable income limit, any *outstanding* carryover is not included here and is eliminated from the carryover amount available.

** For MACRS property, use the same averaging convention as originally used in the year the property was placed in service and the percentages in **Tables M 8–12**. If it is ACRS property, use the special listed property recovery periods, described earlier under "Depreciation Limitations on Listed Property," page IV-78, and the percentages in **Tables ALP 1 and 2** (the half-year averaging convention is built into the tables).

Example: In 2000, a business places in service a computer, costing $11,000, which it uses 100% for qualified business use. It elected to expense $6,000 of its cost per Section 179 and the half-year convention applies. In 2001, the qualified business use drops to 40%.

Result: A computer is 5-year property for both regular MACRS and the ADS method.

	Accelerated Depreciation Taken: 1/5 x $5,000 x 2 x 6/12	=	$1,000		
plus	Any Section 179 Expense Deduction	=	6,000		
	Subtotal			=	$7,000
minus	Straight-Line Depreciation: 1/5 x $11,000 x 6/12			=	(1,100)
equals	Amount of Depreciation Recapture			=	$5,900

Example: In 1986, a business places in service a copier costing $20,000. It is used 100% for qualified business use until 1994, when it is used 60% for personal use. Using ACRS, it is 5-year property and is fully depreciated.

Result: Being 5-year ACRS property, it has a recovery period of 12 years for straight-line purposes for depreciating listed property. (See **Table ALP 1** on page VI-49 for the straight-line percentages used below.)

	Accelerated Depreciation Taken			=	$20,000
minus	Straight-Line Depreciation:				
	Year 1: 1986: $20,000 x 4%	=	$ 800		
	Years 2–5: 1987–1990:				
	$20,000 x 9% = 1,800				
	x 4 years	=	7,200		
	Years 6–8: 1991–1993:				
	$20,000 x 8% = 1,600				
	x 3 years	=	4,800		
	SL Depreciation through 1993			=	(12,800)
equals	Amount of Depreciation Recapture			=	$ 7,200

In 1994, the $7,200 of depreciation recapture is added to taxable income and the basis of the asset is increased by the same amount. The 1994 depreciation deduction is:

$20,000 x 8% (9th year percentage) x 40% (business-use percentage) = $640

Summary of Depreciation Limits

The depreciation limits on listed property, when it is not used 100% for business purposes, are summarized below:

Use	Result
50% or Less Business Use from first year placed in service	No Section 179 Expense Straight-Line Depreciation
Changing to **50% or Less** Business Use *after* first year of use	Recapture of Depreciation Straight-Line Depreciation

Luxury Automobiles

A passenger automobile, as defined earlier, is frequently referred to as a “luxury automobile.” This is not “luxury” as defined by a car dealership, but rather by the IRS Code Section **280F**. If, for example, a Cadillac were to weigh more than 6,000 pounds, it would not be deemed a luxury automobile for tax purposes. However, it may still be included as listed property under “other transportation property.”

Although luxury automobiles are listed property and subject to the predominant use test (the over 50% use test), they are also subject to some additional depreciation limitations, which are applied first. For passenger automobiles acquired after June 18, 1984, there is a maximum amount of depreciation that may be claimed. Here, also, "depreciation" includes any Section 179 amount.

If there are any improvements made to a luxury automobile that must be capitalized, these maximum depreciation limits are applied to the combination of the automobile plus improvements. The only exception to this rule applies to the installation of a device that converts a nonclean-fuel vehicle into a clean-fuel vehicle. According to the Taxpayer Relief Act of 1997, the cost of such a device is not subject to the luxury auto limits for vehicles placed in service after August 5, 1997 and before January 1, 2005. However, the rest of the vehicle's cost continues to be subject to the limitations.

Note: There is a special credit available for qualified electric vehicles. Under IRS Code Sec. **30**, there is a 10% credit of up to $4,000 for qualifying electric vehicles placed in service after June 30, 1993, and before the year 2007. For more information, see "Section 30: Tax Credit for Qualified Electric Vehicles," page IV-69.

Sport Utility Vehicles

Sport Utility Vehicles, defined as having a gross vehicle weight rating greater than 6,000 pounds and less than 14,000 pounds, do not fall under the luxury auto rules of Section 280F. SUVs are not subject to the annual depreciation limits because they are not considered passenger automobiles. However, the "American Jobs and Creation Act" limits the Section 179 expense to $25,000 that can be taken on SUVs placed in service after October 22, 2004. The Tax Cuts and Jobs Act of 2017 increases the limit annually for inflation, starting with tax years beginning in 2019.

Light Trucks and Vans

On July 7, 2003, the IRS published temporary regulations that will benefit taxpayers who purchase and use light trucks or vans for valid business purposes. First, the depreciation limitaitons will be increased for light trucks and vans, and second, trucks and vans used in a specified manner will be exempt from the limits.

Increase in 280F(a) limitations for light trucks and vans

Section 280F(a) of the Internal Revenue Code of 1986 limits the annual depreciation deductions for passenger automobiles purchased for use in business. Passenger automobiles are defined in Section 280F(d)(5)(A) as any 4-wheeled vehicle rated at 6,000 pounds unloaded gross vehicle weight (or, in the case of a truck or van, 6,000 pounds gross vehicle weight) or less.

For automobiles placed in service after December 31, 2007 and before January 1, 2018, the annual limits are increased by $8,000 (if the 168 first-year bonus is taken).

Section 280F(a) exclusion for certain light trucks and vans

Treasury and the IRS concluded that an exclusion from the Section 280F(a) depreciation limits for trucks, vans and other vehicles used in a specified manner is appropriate as long as it is based on objective factors and does not provide an incentive to purchase a truck or van when a less expense automobile would meet the taxpayer's business needs. Therefore the temporary regulations exclude vans and light trucks purchased on or after July 7, 2003 from the depreciation limitations if it is a qualified nonpersonal use vehicle as defined in Section 1.274-5T(k)(2) and Section 1.274-5T(k)(7). Section 1.274-5T(k)(2) is a list of 17 vehicles including bucket trucks, qualified moving vans and refrigerator trucks.

Treasury Decision 9133 and the final regulations, issued June 25, 2004, went one step beyond and retroactively reclassified qualified nonpersonal use vehicles as not falling under the Code Section 280F depreciation dollar caps. T.D. 9133 paves the way for increased Section 179 expense deduction to be taken for qualified nonpersonal use vehicles for tax year 2003 and going forward. Qualified nonpersonal use vehicles are defined as light trucks and vans that have been specially modified for business purposes and by reason of their nature and design are not likely to be used more than a de minimus amount for personal use.

Depreciation Limitations on Luxury Automobiles

The depreciation limitation for luxury automobiles takes precedence over the amount that may be claimed because of the predominant use test. Furthermore, the amount of depreciation allowed on a luxury automobile is based on the date on which the automobile is placed in service by the taxpayer. The dollar limitations each year are adjusted by inflation.

Automobile Placed in Service		Maximum Depreciation [1]				
After	Before	Year 1	Year 2	Year 3	Year 4	Add'l Years [2]
6/18/84	1/1/85	4,000	6,000	6,000	6,000	6,000
12/31/84	4/3/85	4,100	6,200	6,200	6,200	6,200
4/2/85	1/1/87	3,200	4,800	4,800	4,800	4,800
12/31/86	1/1/89	2,560	4,100	2,450	1,475	1,475
12/31/88	1/1/91	2,660	4,200	2,550	1,475	1,475
12/31/90	1/1/92	2,660	4,300	2,550	1,575	1,575
12/31/91	1/1/93	2,760	4,400	2,650	1,575	1,575
12/31/92	1/1/94	2,860	4,600	2,750	1,675	1,675
12/31/93	1/1/95	2,960	4,700	2,850	1,675	1,675

Automobile Placed in Service		Maximum Depreciation [1]				
After	Before	Year 1	Year 2	Year 3	Year 4	Add'l Years [2]
12/31/94	1/1/97	3,060	4,900	2,950	1,775	1,775
12/31/96	1/1/98	3,160	5,000	3,050	1,775	1,775
12/31/97	1/1/99	3,160	5,000	2,950	1,775	1,775
12/31/98	1/1/00	3,060	5,000	2,950	1,775	1,775
12/31/99	1/1/04	3,060 [3]	4,900	2,950	1,775	1,775
12/31/03	1/1/05	2,960	4,800	2,850	1,675	1,675
12/31/04	1/1/06	2,960	4,700	2,850	1,675	1,675
12/31/05	1/1/07	2,960	4,800	2,850	1,775	1,775
12/31/06	1/1/08	3,060	4,900	2,850	1,775	1,775
12/31/07	1/1/09	2,960 [4]	4,800	2,850	1,775	1,775
12/31/08	1/1/10	2,960 [5]	4,800	2,850	1,775	1,775
12/31/09	1/1/12	3,060 [6]	4,900	2,950	1,775	1,775
12/31/11	1/1/15	3,160 [6]	5,100	3,050	1,875	1,875
12/31/14	1/1/16	3,160 [6]	5,100	3,050	1,875	1,875
12/31/15	1/1/17	3,160 [7]	5,100	3,050	1,875	1,875
12/31/16	1/1/18	3,160 [7]	5,100	3,050	1,875	1,875
12/31/17	1/1/19	10,000 [8]	16,000	9,600	5,760	5,760

1 This chart is based on a 12-month tax year and 100% business use. Therefore, if either is not the case, these amounts will need to be adjusted. See "How To" below.

2 Notice that regardless of the auto's recovery period (3 years for ACRS and 5 years for MACRS), you may continue to depreciate a luxury auto for however many years it takes until the full basis is completely depreciated.

3 The Job Creation and Worker Assistance Act of 2002 increases the first-year luxury auto limitation by $4,600 for autos purchased after September 10, 2001 for which the additional 30% first-year depreciation deduction was claimed. The Jobs and Growth Tax Relief Reconciliation Act increases the auto limitation by $7,650 for autos purchased after May 5, 2003 for which the 50% or 30% additional first-year depreciation deduction was claimed. Refer to the rules in "Bonus Depreciation," page IV-62, for more information on this special first-year depreciation deduction.

4 The Economic Stimulus Act of 2008 increases the first-year luxury auto limitation by $8,000 for autos purchased between January 1, 2008 and December 31, 2008 for which the additional 50% first-year depreciation deduction was claimed.

5 The American Recovery and Reinvestment Act of 2009 increases the first-year luxury auto limitation by $8,000 for autos placed in service during 2009 for which the additional 50% first-year depreciation deduction was claimed.

6 The Small Business Jobs Act of 2010 increases the first-year luxury auto limitation by $8,000 for autos placed in service during 2010 for which the additional first-year depreciation deduction was claimed. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation of 2010 increases the first-year luxury auto limitation by $8,000 for autos placed in service during 2011 and 2012 for which the additional first-year depreciation deduction was claimed. The American Taxpayer Relief Act of 2012 increases the first-year luxury auto limit by $8,000 for autos placed in service during 2012 and 2013 for which the additional 168 first-year bonus is claimed. The Taxpayer Increase Prevention Act of 2014 increases the first-year luxury auto limit by $8,000 for autos placed in service during 2014 for which the additional 168 first-year bonus is claimed.

7 The Protecting Americans from Tax Hikes Act of 2015 increases the first-year luxury auto limit by $8,000 for autos placed in service during 2015-2017 for which the additional 168 first-year bonus is claimed.

8 The Tax Cuts and Jobs Act of 2017 nearly triples the luxury auto limits for 2018 along with the additional first year bonus of $8,000. The first-year amount for 2018 with bonus is $18,000.

Truck or Van Placed in Service		Maximum Depreciation				
After	Before	Year 1	Year 2	Year 3	Year 4	Add'l Years
12/31/02	1/1/04	3,360	5,400	3,250	1,975	1,975
12/31/03	1/1/05	3,260	5,300	3,150	1,875	1,875
12/31/04	1/1/07	3,260	5,200	3,150	1,875	1,875
12/31/06	1/1/08	3,260	5,200	3,050	1,875	1,875
12/31/07	1/1/09	3,160 [1]	5,100	3,050	1,875	1,875
12/31/08	1/1/10	3,060 [2]	4,900	2,950	1,775	1,775
12/31/09	1/1/11	3,160 [3]	5,100	3,050	1,875	1,875
12/31/10	1/1/12	3,260 [3]	5,200	3,150	1,875	1,875
12/31/12	1/1/14	3,360 [3]	5,400	3,250	1,875	1,875
12/31/13	1/1/15	3,460 [3]	5,500	3,350	1,975	1,975
12/31/14	1/1/16	3,460 [3]	5,600	3,350	1,975	1,975
12/31/15	1/1/17	3,560 [4]	5,700	3,350	2,075	2,075
12/31/16	1/1/18	3,560 [4]	5,700	3,450	2,075	2,075
12/31/17	1/1/19	10,000 [5]	16,000	9,600	5,760	5,760

1 **Note:** The Economic Stimulus Act of 2008 increases the first-year luxury auto limitation by $8,000 for light trucks and vans purchased between January 1, 2008 and December 31, 2008 for which the additional 50% first-year depreciation deduction was claimed.

2 The American Recovery and Reinvestment Act of 2009 increases the first-year luxury auto limitation by $8,000 for autos placed in service during 2009 for which the additional 50% first-year depreciation deduction was claimed.

3 The Small Business Jobs Act of 2010 increases the first-year luxury auto limitation by $8,000 for autos placed in service during 2010 for which the additional first-year depreciation deduction was claimed. The Tax Relief,

Unemployment Insurance Reauthorization, and Job Creation of 2010 increases the first-year luxury auto limitation by $8,000 for autos placed in service during 2011 and 2012 for which the additional first-year depreciation deduction was claimed. The American Taxpayer Relief Act of 2012 increases the first-year luxury auto limit by $8,000 for autos placed in service during 2012 and 2013 for which the additional 168 first-year bonus is claimed. The Taxpayer Increase Prevention Act of 2014 increases the first-year luxury auto limit by $8,000 for autos placed in service during 2014 for which the additional 168 first-year bonus is claimed.

4 The Protecting Americans from Tax Hikes Act of 2015 increases the first-year luxury auto limit by $8,000 for autos placed in service during 2015-2017 for which the additional 168 first-year bonus is claimed.

5 The Tax Cuts and Jobs Act of 2017 nearly triples the luxury auto limits for 2018 along with the additional first year bonus of $8,000. The first-year amount for 2018 with bonus is $18,000.

Note: The Taxpayer Relief Act of 1997 included two provisions that affect the luxury automobile limits:

- It tripled (approximately) the luxury automobile limits on depreciation allowed for electric automobiles.
- Where a vehicle is modified to burn clean fuel, the cost of the installed device that converts a non-clean fuel vehicle into a clean-fuel vehicle is no longer subject to the luxury automobile limits. However, the rest of the vehicle's cost continues to be subject to the limitations.

Both of the above provisions were effective for vehicles placed in service after August 5, 1997 and before January 1, 2007. Note that there is a fundamental difference between the kinds of property covered in these two provisions. In the first provision, the vehicle, an electric car, is originally designed and built by the manufacture to use a clean fuel. In the second provision, the vehicle is modified to burn clean fuel after it is built.

The above charts are appropriate for electric vehicles placed in service after 2006.

The process should proceed as follows:

How To:

If placed in service in current year:

1. Look at the chart on the preceding page and determine the maximum amount of depreciation that may be taken, based on the date placed in service and the year of the recovery period. If this is a short tax year, multiply the amount in the chart by the following fraction:*

$$\frac{\textit{Number of Months in the Tax Year}}{\textit{12}}$$

* **Note:** If the 30%, 50%, or 100% first-year depreciation deduction was claimed, the additional $4,600, $7,650, or $8,000 does NOT have to be prorated for the short year.

2. Apply the predominant use test to the property:

2A. If the qualified business use is more than 50%, go to Step 3, or

2B. If the qualified business use is 50% or less, compute depreciation under ADS, *without any limitations*,* except for the applicable averaging convention, and go to Step 4.

3. Compute depreciation using regular MACRS (or one of the elective MACRS depreciation methods if preferred), *without any limitations*,* except for the applicable averaging convention.

* If this is a short tax year, the applicable averaging convention may need to be adjusted (for determining the correct calculation, see Chapter 2, MACRS, and the segment on “Short Tax Years,” page IV-57). Do not adjust, however, for the property being used less than 100% for business if this is the case, as this adjustment will be handled in Step 5.

4. Compare the amount in Step 1 with Step 2B or 3 and use the smaller amount.
5. Determine the business-use percentage (the portion of the property *not* used for personal purposes) and multiply this by the result of Step 4. The result is the amount of depreciation allowed this year.
6. If the business claims the 50% special allowance, the 2004 depreciation for the automobile would increase by $7,650 to a total of $10,610 for the year.

Example: In 2012, a business places in service a luxury automobile, costing $40,000 and used 100% in the business. The car is 5-year property and the half-year convention applies. The tax year consists of 12 months.

Result:

1. Looking at the chart, the maximum amount of depreciation that may be taken this year is $3,160.
2. Since the auto is used 100% in the business, it passes the predominant use test.
3. Computing depreciation for the year using regular MACRS (DDB):

1/5 x $40,000 x 2 x 6/12 = $8,000

4. Comparing Step 1 with Step 3, $3,160 is the lesser amount.
5. Business use is 100%; therefore, depreciation for the year is <u>$3,160</u>.

Note: Claiming the 168 first-year bonus depreciation would decrease the basis to $32,000 ($40,000 - $8,000). It would be necessary to return to Step 3 to recalculate depreciation for the year using regular MACRS (DDB):

1/5 x $32,000 x 2 x 6/12 = $6,400

Once again comparing Step 1 with Step 3, $3,160 is still the lesser amount and along with the special allowance of $8,000, the depreciation for the year would be <u>$11,160.</u>

Example: Assume the same facts as in the previous example, except that the auto cost $30,000 and was only used 60% in the business.

Result:

1. Looking at the chart, the maximum amount of depreciation is $3,160.
2. Since the auto is used 60% in the business, it passes the predominant use test of more than 50% qualified business use.
3. Computing depreciation for the year using regular MACRS (DDB):

   1/5 x $30,000 x 2 x 6/12 = $6,000
4. Comparing Step 1 with Step 3, $3,160 is the lesser amount.
5. Business use is 60%; therefore, depreciation for the year is <u>$1,896</u> ($3,160 x 60%).

Example: Assume the same facts as above, except the auto is used only 40% in business and it is a short tax year of 6 months.

Result:

1. The maximum depreciation per the chart is $3,160. However, since this is a short year of 6 months:

   $3,160 x 6/12 = $1,580 = the maximum amount of depreciation
2. Since the auto is only used 40% in the business, it fails the more than 50% test and depreciation must be computed under ADS: A 5-year asset also has a 5-year recovery period for ADS.

   1/5 x $30,000 x 3*/12 = $1,500

   * Since this is a short year, the averaging convention needs to reflect this.
3. Skip to Step 4.
4. Comparing Step 1 with Step 2, $1,500 is the lesser amount.
5. Business use is 40%; therefore, depreciation for the year is <u>$600</u> ($1,500 x 40%).

TIP
Due to the limitations described above, there is no benefit to electing the **Section 179 expense on luxury automobiles**.

How To:

If calculating depreciation on a luxury automobile in a subsequent tax year:

1. Look at the "Maximum Depreciation" Chart on page IV-84, and determine the maximum amount of depreciation that may be taken, based on the date placed in service and the year of the recovery period. If this is a short tax year, multiply the amount in the chart by the following fraction:

$$\frac{\textit{Number of Months in the Tax Year}}{\textit{12}}$$

2. Apply the predominant use test to the property:

   2A. If the qualified business use is more than 50%, go to Step 3, or

   2B. If the qualified business use is 50% or less:

   2B(a). Calculate the amount of depreciation recapture (for an explanation of "How To," see "Predominant Use Test Failed in Subsequent Tax Year," page IV-80, and

   2B(b). Compute depreciation either under ADS (if MACRS property) or under straight-line ACRS over the listed property recovery lives with the percentage from **Table ALP 1** (if ACRS property) and go to Step 4.*

3. Compute depreciation using regular MACRS or ACRS (or one of the elective methods if preferred), depending on the year the property was placed in service.*

   * If this is a short tax year, the applicable averaging convention may need to be adjusted (if MACRS property, see "Property Placed in Service in a Short Year," page IV-58, and, if ACRS property, see "Short Tax Years," page IV-106, for determining the correct calculation). Do not adjust, however, for the property being used less than 100% in business if this is the case, as this adjustment will be handled in Step 5.

4. Compare the amount in Step 1 with Step 2B(b) or 3 and use the smaller amount.

5. Determine the business-use percentage (the portion of the property *not* used for personal purposes) and multiply this by the result of Step 4. The result is the amount of depreciation allowed this year.

Leased Listed Property

Just as the luxury automobile and other listed property rules limit the available depreciation deductions for listed property, the leasing limitations are intended to limit the amount of leasing expense available for such property. We need to consider the consequences to both the lessor and the lessee when discussing leased listed property.

For the lessor, the same limitations on the amount of depreciation expense allowed on listed property, which we have just explained, will not apply if certain conditions are met. If the lessor is regularly engaged in the business of leasing listed property, the depreciation limitations will not apply. "Regularly engaged in the business of leasing" is defined by whether or not the leasing contracts for the listed property are entered into with some frequency over a continuous period of time. Individual facts and circumstances will need to be considered, but an occasional leasing of listed property will not qualify.

Example: A business has one passenger automobile, which it rents out during the year.

Result: The business is not regularly engaged in the business of leasing, and the limitations for leased listed property will apply.

For the lessee, the limitations on leased listed property are affected by including certain amounts in income, thereby reducing the lease expense. The limitations apply only if the lease lasts for a period of 30 days or more. The rules governing the inclusion amount are different for passenger automobiles (luxury autos) and for other listed property. The remainder of this segment pertains to the lessee.

Passenger Automobiles

Beginning after June 18, 1984, if a business *leases a car for 30 days or more*, it may need to include in income an "inclusion amount." This inclusion amount is the business-use percentage* multiplied by the amount by which the fair market value** of the leased car exceeds a specified amount. The specified amount, which the car's fair market value must exceed, depends on the date on which the lease starts. The inclusion amount is then prorated for the number of days that the car is actually leased during the tax year.

* If the business use (i.e., the use not attributable to personal use) of a leased luxury car is **50% or less**, there may be an **additional inclusion amount**, based on the fair market value of the car and the date it is first leased. The following IRS Code Sections are provided as reference (we have not included these tables in this guide):

Date First Leased	IRS Code Section
Pre-April 3, 1985	**1.280F-5T(d)(2)**
April 3, 1985 thru Dec. 31, 1986	**1.280F-5T(e)(6)**
After December 31, 1986	No additional inclusion when less than predominant use

** The fair market value is determined on the first day of the lease.

Pre-April 3, 1985

The following steps explain how to compute the inclusion amount for a car that is first leased after June 18, 1984, but before April 3, 1985.

How To:

1. Determine the Fair Market Value of the leased car on the first day of the lease.
2. Determine the number of tax years for which the car has been leased and subtract 3.*
3. Multiply Step 2 by $6,000 and add $16,500 to the product.
4. Subtract Step 3 from Step 1. This cannot be less than zero.
5. Multiply Step 4 by 6%.
6. If it is either a short tax year or the car was not leased for the full tax year, prorate Step 5 by the number of days it was leased during the tax year.
7. If the car was not used 100% in business (either in an active trade or business or held for the production of income), multiply Step 6 by the percentage of business use.

* The inclusion amount for the first 3 years depended on whether or not the Investment Tax Credit, in effect at that time, was passed through to the lessee. Therefore, a different percentage was in effect for those years.

April 3, 1985, Through December 31, 1986

The following steps explain how to compute the inclusion amount for a car that is first leased after April 2, 1985, but before January 1, 1987.

How To:

1. Determine the Fair Market Value of the leased car on the first day of the lease.
2. Determine the number of tax years for which the car has been leased and subtract 3.
3. Multiply Step 2 by $4,800 and add $13,200 to the product.
4. Subtract Step 3 from Step 1.
5. Multiply Step 4 by 6%.
6. If it is either a short tax year or the car was not leased for the full tax year, prorate Step 5 by the number of days it was leased during the tax year.
7. If the car was not used 100% in business (either in an active trade or business or held for the production of income), multiply Step 6 by the percentage of business use.

Post-1986

If a car is first leased after December 31, 1986, the fair market value must be over $12,800 ($19,000 for leases beginning in 2013) for there to be a possible inclusion amount. Each year in a Revenue Procedure, the IRS publishes a new table for determining the inclusion amount for automobiles with a lease beginning in the current year. You can locate the tables by searching the internet for “lease inclusion table 20xx” where xx is the desired year of the table, i.e. “lease inclusion table 2013” for the 2013 table. To use these tables, you need to know the fair market value of the leased car on the first day of the lease. You also need to know the year of the lease the business is now in. The amounts from the tables also need to be prorated for the number of days that the car was leased during the tax year.

Note: For the last year of the lease, as long as the lease did not both start and end in the same tax year, use the dollar amount from the applicable table, but for the **preceding tax year**.

Example: A calendar-year business leased a luxury car on April 1, 1998, which had a fair market value of $32,300 on the first day of the lease. The lease will run for 5 years, ending March 31, 2003. The car was used 80% for business until 2003, when it is only used 40% for business purposes.

Result: For tax years 1998 through 2003, the business must include the following amounts in income:

Tax Year	Amount From IRS Table	Proration	Business Use	Inclusion Amount
1998	$137	275/365 days	80%	$ 83
1999	$301	365/365 days	80%	$241
2000	$449	366/366 days	80%	$359
2001	$540	365/365 days	80%	$432
2002	$624	365/365 days	80%	$499
2003	$624	90/365 days	40%	$ 62

Other Leased Listed Property

Similar to the rules governing leased luxury automobiles, there are rules for other leased listed property. Again, there is an inclusion amount based on the fair market value of the listed property on the first day of the lease term, and the amount of inclusion is determined differently depending on the date the lease began.

As there are similarities to the leased luxury auto rules, there are also differences. The inclusion amount for other leased listed property is:

1. Only required when the business use falls to 50% or less.

> **Note:** This is different, since the business use for luxury autos can be 100% and the income inclusion will still be required. Furthermore, if the lease on a luxury auto begins prior to 1987, a second and *additional* inclusion amount is required if the business use falls to 50% or less.

2. Only added to income the first year when the business use falls to 50% or less (subsequent years are *not* affected, although see number 5 below).

3. Prorated based on the actual number of days in the lease term, if the lease term is for less than 1 year. It is important to point out that this proration is required even if the short lease term occurs over *two* consecutive tax years, since this is **a one time inclusion amount**.

4. Limited to the sum of all deductible amounts incurred with respect to the leased listed property for the tax year in which the inclusion amount must be added to income.

5. Added to the lessee's income in the *next* tax year (instead of in the tax year when the business use first falls to 50% or less) when:

- **a.** The lease term begins within 9 months before the close of the lessee's tax year in which the 50% or less business use occurs, *and*
- **b.** The lease term continues into the lessee's next tax year.

When the circumstances in **5.** above apply, the inclusion amount is determined by using the applicable percentage taken from the tables for the *first* year of the lease and multiplying it by the *average* of the business-use percentages for *both* tax years (IRS Reg. **1.280F-5T(g)(1)**). (An example of this is at the end of this segment.)

The Lease Term

For ACRS 18- or 19-year property and for MACRS 27.5-, 31.5-, or 39-year property, the lease term does not include any options to renew. For all other listed property the options to renew are included in the lease term. Also, 2 or more successive leases that are part of the same transaction for the same or substantially the same property are treated as one lease.

Lease With Option To Buy

A lease with an option for the lessee to purchase the property at the end of the lease may be treated either as a lease or as a sales contract, depending on the terms and intent of the parties. Some of the deciding factors will include whether interest is to be paid, whether any equity is given, and whether there is a "bargain purchase price" (i.e., less than fair market value) at the end of the lease term.

Pre-1987

If listed property (other than luxury automobiles) is first leased after June 18, 1984, but before January 1, 1987, the income inclusion amount is determined by the following formula:

$$\text{FMV of property (on 1st day of lease)} \times \text{Business-use percentage (all use that is not personal)} \times \text{Percentage (from table*)}$$

* **Tables ALL 1 and 2** are included in the back of this guide for your convenience.

Post-1986

For listed property (other than luxury automobiles) leased after 1986, the lessee must include in income an inclusion amount, which is the sum of the following:

FMV × Business use % × Applicable % from Table MLL 1*

plus

*FMV × Average business use %** × Applicable % from Table MLL 2*

* This should be the business-use percentage for the first tax year when it drops to 50% or less.

** The average business-use percentage is determined by averaging the business-use percentages for all tax years in which the property is leased that *precede* the first tax year in which the business-use percentage is 50% or less.

Example: On August 15, 1998, a calendar-year business begins leasing a computer with a fair market value of $10,000. It is a 5-year lease. In 1998 the business use is 50%, and in 1999 the business use is 90%. All business use is also "qualified" business use, and the rest of the use is all personal use. In 1999, the business's deductible rent for the computer is $3,000.

Result: Since the computer is used only 50% for qualified business use, it fails the predominant use test and ADS straight-line depreciation must be used. The computer is 5-year MACRS property with a 5-year recovery period under ADS.

$10,000 (FMV) x 70%* x 2.1% (from **Table MLL 1**)	=	$147
plus		
$10,000 x 70%* x 0% (from **Table MLL 2**)	=	0
Inclusion Amount in 1999*	=	$147

* Since the lease term began within the last 9 months of the tax year, the business-use percentage is the average of the 2 years' percentages (90% + 50%/2), or 70%, and the inclusion amount is added to income in 1999, the *next* tax year.

Example: On January 15, 1997, a calendar-year business starts leasing a computer with a fair market value of $6,000. It is a 3-year lease. In 1997 the business use is 80%, and in 1998 and 1999 the business use is 40%. All business use is also "qualified" business use, and the rest of the use is personal. In 1998, the business's deductible rent for the computer is $1,100.

Result: The inclusion amount must be added to income in 1998, since that is the first tax year when the business use fell to 50% or less. 1998 is the second year of the lease, and the computer has a 5-year recovery period for ADS.

$6,000 (FMV) x 40%* x -7.2% (from **Table MLL 1**)	=	– $173
plus		
$6,000 x 70%* x 10% (from **Table MLL 2**)	=	480
Inclusion Amount in 1998	=	$307

* Notice that the percentages in **Table MLL 1** are, except for the first year percentages, all *negative* amounts.

Record-Keeping Requirements for Listed Property

No deduction is allowed for any listed property *unless the use is substantiated by adequate records*.

For listed property placed in service after June 18, 1984, such records must be kept for the length of the longer recovery periods required by ADS or the longer ACRS straight-line recovery periods for listed property, even if the straight-line method is not required to be used. Remember that the predominant use test must be applied each year of the straight-line recovery periods to determine if the listed property continues to pass the predominant use test (i.e., to see if the qualified business use remains over 50%) and, therefore, whether depreciation recapture will be required.

In order to substantiate all deductions for the listed property, including depreciation expense, either records, or sufficient evidence to corroborate the taxpayer's statements, must prove:

1. The amount of each expenditure for the listed property, such as acquisition cost, repair expenses, and lease payments.
2. The amount of business use, as well as total use for the tax year, including personal use (for example, the mileage for all cars, divided between qualified business use, other business use and personal use).
3. The date for each expense or use.
4. The business or investment purpose for the expense or use.

A contemporaneous log book is not required, but the sooner an expense or use of the property is recorded after the fact, the more credible the records become. A weekly accounting is usually recommended.

It is also possible to keep an adequate record for a portion or portions of the tax year and then use that record to substantiate the business use for the entire year, if it can be proven that this is a true representation for the full year.

Section IV: Chapter 5:
Accelerated Cost Recovery System (ACRS)

In this section:

The Economic Recovery Tax Act of 1981 (ERTA) introduced the Accelerated Cost Recovery System (ACRS). ACRS is a modification of the Asset Depreciation Range (ADR) method used during the 1970s. It applies to most depreciable property placed in service after 1980 but before 1987.

Although both MACRS and ACRS "sound" similar, there are major differences between the two, such as the class life categories, which determine the recovery periods for property, depreciation methods allowed, averaging conventions, short-tax year rules, and the rules governing dispositions.

Both systems do, however, use the same terminology of "recovery periods" and "cost recovery," rather than "useful lives" and "depreciation."

For the most part, ACRS was well received, as it shortened the assets' depreciable lives (i.e., recovery periods) and speeded the rate of depreciation (i.e., rate of recovery). ACRS was created to stimulate capital investment. By 1984, however, times had changed and the Tax Reform Act of 1984 increased the recovery periods for certain property.

Although ACRS is mandatory for depreciable property placed in service after 1980 and before 1987, there are exceptions for certain property, due to either the anti-churning rules (discussed later), the transitional rules, or a special election. The transitional rules applied to certain property placed in service after 1986 that because of prior contracts or construction caused it to be subject to ACRS. Also, there was an election allowed whereby the taxpayer could use MACRS for qualifying property placed in service after July 31, 1986, and before January 1, 1987. This election is irrevocable and was made on a property-by-property basis.

Note: Generally, the recovery period was shorter under ACRS than under MACRS, making it the preferable method when there was a choice.

Even though assets now acquired are, for the most part, depreciated under MACRS (there are exceptions that are discussed under the anti-churning rules), many businesses still have fixed assets that are being depreciated under ACRS. These businesses must continue to use ACRS until the end of the assets' recovery periods. Therefore, it is important to be knowledgeable about ACRS, as well as MACRS. This chapter will give you a thorough understanding of the treatment of the ACRS property that is still being depreciated, and will give you a general overview of how these assets were originally recorded.

ACRS Recovery Periods

There are seven classes of property according to ACRS that determine the property's recovery period. The assignment to a property class does not have anything to do with the property's actual useful life. The recovery periods are set by statute. The following describes briefly each property class:

Class	Description
3-year	Property with a class life of 4 years or less and machinery and equipment used for research and development. It includes cars and light trucks (less than 13,000 pounds), breeding hogs, race horses over 2 years old, and other horses over 12 years old.
5-year	Most personal property with a class life of over 4 years (i.e., *personal property not included in any other class*), single-purpose agricultural structures, and petroleum storage facilities (other than buildings). It includes heavy trucks and office furniture and equipment.
10-year	Real property with a class life of 12.5 years or less, and public utility property that is not real property and that has a class life of more than 18 but less than 26 years. It includes amusement park structures, mobile homes, and railroad tank cars.
15-year	*Real property* with a class life of over 12.5 years and placed in service *before 3/16/84*, and public utility property with a class life of over 25 years.
15-year	Low-income housing (it is given its own class as it has a special depreciation rate).
18-year	*Real property* with a class life of over 12.5 years and placed in service *after 3/15/84* and before 5/9/85.
19-year	*Real property* with a class life of over 12.5 years and placed in service *after 5/8/85* and before 1987.

Note: The recovery period for real property with a class life of over 12.5 years is dependent on when it was placed in service. This is because the tax laws changed the prescribed recovery periods for such property twice.

By using the ADR class lives, determining the ACRS recovery periods for depreciable property was not that difficult. There were, however, some special rules when determining the recovery periods for improvements made to real property prior to 1987. Currently, however, any improvements, additions, or components placed in service after 1986 are depreciated using MACRS, even though the building to which they are attached is ACRS property.

Note: Prior to ACRS, a business could depreciate its real property using "component depreciation." In other words, each of a building's components could be depreciated under a separate depreciation method and life, as compared to the rest of the building (i.e., the shell). Under ACRS, this was replaced by "composite depreciation," whereby the building and all of its components had to use the same recovery period and method. There were two exceptions to this rule:

1. The first post-1980 (but pre-1987) component, constructed for a building placed in service before 1981, was treated as a separate ACRS asset. Any such component was depreciated as 15-, 18-, or 19-year property, depending on when it was placed in service. Thereafter, all future components added to the same building were depreciated over the same recovery period and method as the first ACRS component.
2. If an improvement to a building was "substantial" (i.e., equal to 25% or more of the building's basis), it was treated as a separate building and depreciated over its own recovery period, using whichever ACRS method the taxpayer wanted, with no correlation to the building's original ACRS method.

For the rules governing leasehold improvements placed in service after 1980 but before 1987, see "Property Excluded From ACRS," page IV-109).

ACRS Depreciation Methods

There are two basic methods for depreciating ACRS property:

- Prescribed rates, which use accelerated depreciation, and for which percentage tables are provided.
- An alternate ACRS method that uses straight-line depreciation over one of three elective recovery periods.

Calculating ACRS Depreciation

In using either the percentage tables or the alternate straight-line method, you will be using the property's depreciable basis, which is first reduced by any Section 179 expense elected and any Investment Tax Credit basis reduction, but is not reduced by any previous depreciation taken. Salvage value is ignored for ACRS purposes.

Basis Reduced by Investment Tax Credit

Qualifying property placed in service after 1982 and before 1986 was subject to Investment Tax Credit (ITC), which gave the business a choice: it could have taken a lesser amount of Investment Tax Credit and not reduced the asset's basis, or it could have elected to have taken the full amount of allowable Investment Tax Credit and reduced the asset's basis by 50% of the credit claimed. Investment Tax Credit was repealed for property placed in service after 1985.

Note: There is also a required basis reduction for 50% of the allowable energy investment credit (a 10% credit), and for 100% (50% before 1987) of the investment credit for rehabilitating certified historic structures (currently a 20% credit).

If the full amount of Investment Tax Credit was taken (thereby causing the asset's basis to be reduced), the amount of the credit depended on the recovery class of the property:

Class of property	Amount of basis on which the credit was taken*	Amount of credit
3-year	60%	10%
4 or more years	100%	10%

How To:

To determine the amount by which an asset's basis must be reduced if the full amount of Investment Tax Credit was taken:

$$\begin{matrix}\textit{Property's}\\ \textit{ITC Basis}\end{matrix} \times \begin{matrix}\textit{Applicable}\\ \textit{Percentage*}\end{matrix} \times \textit{10\% ITC} \times \textit{50\%} = \textit{Basis Reduction}$$

Note: There were several other factors that could have reduced the amount of Investment Tax Credit and, thus, the amount of the basis reduction:

- The Investment Tax Credit was taken on the asset's cost, not its basis. If an asset was acquired by trading in an old asset, the Investment Tax Credit could only be claimed on the amount of cash paid.
- If the acquired property was purchased as a replacement for an old asset within 60 days of the old asset's disposition, the business could only claim the credit on the excess of the cost of the new property over the basis of the old property, *unless* there was **Investment Tax Credit recaptured** on the old property.
- The property's ITC basis was reduced by any percentage of personal use.

- If the tax liability of the business was more than $25,000 in the year in which the Investment Tax Credit was claimed, the credit was limited to $25,000 plus 85% of the excess.
- The credit could not exceed $1,000 for luxury automobiles placed in service before 4/3/85 and $675 for luxury automobiles placed in service after 4/2/85.

Miscellaneous Investment Tax Credit Rules

As you can see from just the above, the Investment Tax Credit, which was quite simple when first created, became more and more complex. The following are various other points to remember when depreciating an asset whose basis is reduced due to this credit:

1. There were certain transitional rules whereby qualified property placed in service after 1985 received Investment Tax Credit. The depreciable basis of such property was reduced by 100% of the credit claimed. (See IRS Code Sec. **49** for the amount of credit allowed, as well as which property qualified for it.)
2. If the business elected to depreciate ACRS property over a longer recovery period under the Alternate ACRS Method (i.e., straight-line), this did not change the property's class for the Investment Tax Credit. For example, depreciating 3-year recovery property over 5 years, under the Alternate ACRS Method, did *not* change the amount of basis on which the credit was taken from 60% to 100%.

ACRS Averaging Conventions

A half-year averaging convention is used for 3-, 5-, and 10-year property. All other property that is real property, uses either a full-month convention (if placed in service before 6/23/84) or a midmonth convention (if placed in service after 6/22/84). The averaging conventions are built into the percentage tables for you.

- The *half-year convention* treats all property placed in service as if occurring at the midpoint of the tax year and allows a half year of depreciation for that year. The half-year convention also allows a half year of depreciation in the property's final year, as long as it is still in service. **In the year of disposition, no depreciation is allowed for 3-, 5-, and 10-year property if disposed of before the end of its recovery period!**
- The *full-month convention* treats all property placed in service during a particular month as placed in service on the first day of that month. If the asset is disposed of, it allows no depreciation for the month in which the disposition occurs.
- The *midmonth convention* treats all property either placed in service or disposed of as if occurring at the midpoint of the month, thereby allowing a half month of depreciation for the first and final months in which it is in service.

Percentage Tables

For 3-, 5-, and 10-year recovery property, the percentages from the tables below are applied regardless of when during the year the property was placed in service. For real property in the 15-, 18-, or 19-year class, the percentage used depends on which month in the tax year the property is first placed in service.

Note: Remember that the averaging conventions are built into the tables for you, so no further adjustment needs to be made.

Generally, the prescribed rates used in the percentage tables are as follows:

- 150% declining-balance for personal property
- 175% declining-balance for most real property
- 200% declining-balance for low-income housing

Note: All of the above declining-balance methods will switch to the straight-line method when that method results in a higher deduction. Again, this is built into the tables for you.

All property with either an ACRS 3-year recovery period (except luxury automobiles) or an ACRS 5-year recovery period is, by now, fully depreciated.

The ACRS 3-year recovery percentages were:

Year 1	25%
Year 2	38%
Year 3	37%

The ACRS 5-year recovery percentages were:

Year 1	15%
Year 2	22%
Years 3-5	21%

The ACRS recovery percentages for 10-year property are:

Year 1	8%
Year 2	14%
Year 3	12%
Years 4-6	10%
Years 7-10	9%

The ACRS recovery percentages for 15-year public utility property* are:

Year 1	5%
Year 2	10%
Year 3	9%
Year 4	8%
Years 5-6	7%
Years 7-15	6%

* Public utility property with a class life of over 25 years and that is not real property is handled differently from real property in the same 15-year class. It is, in fact, treated basically the same as 3-, 5-, and 10-year recovery property and will be given no further detailed explanation in this guide.

The recovery percentages for all other ACRS property are found in the ACRS Percentage **Tables A 1–15** starting on page 43.

How To:

1. Determine the property's basis, reduced by any Section 179 expense claimed (whether or not an actual deduction for the Section 179 amount has yet been taken due to the taxable income limitation). Do *not* reduce the basis by any prior year's depreciation.
If it is 10-year property or 15-year public utility property, go to Step 2 and stop. If it is 15-, 18-, or 19-year real property, go to Step 3.

2. If it is either 10-year property or 15-year public utility property, use the percentages given above and apply the applicable percentage (based on the tax year in which it is currently in service) to Step 1. *This is the depreciation for a full 12-month tax year.*

3. If it is 15- (including if it is low-income housing), 18-, or 19-year real property, turn to "ACRS Percentage Tables," page VI-41, and:

3A. Choose the correct table based on the date the property was placed in service.

3B. Find the applicable horizontal column by the month of the *tax* year in which it was originally placed in service.

3C. Find the applicable vertical column for the tax year in which you are calculating depreciation for the property.

3D. Apply the applicable percentage to Step 1. *This is the depreciation for a full 12-month tax year.*

Example: On March 11, 1986, XYZ Corporation placed in service an amusement park structure (10-year property) costing $10,000.

Result: The following depreciation is calculated:

Tax Year	Depreciation Calculation
1986	$10,000 x 8% = $ 800
1987	$10,000 x 14% = $1,400
1988	$10,000 x 12% = $1,200
1989–1991	$10,000 x 10% = $1,000 each year
For 1992 and each of the next 3 years (if not disposed of)	$10,000 x 9% = $ 900 each year

Example: On April 2, 1985, XYZ, a calendar-year corporation, placed in service a building costing $100,000.

Result: This is 18-year recovery property (determined by the date it was placed in service) and was put in service during the fourth month of the tax year. The following depreciation is calculated to date, using the percentages in **Table A 5**:

Tax Year	Depreciation Calculation
1985	$100,000 x 7% = $7,000
1986	$100,000 x 9% = $9,000
1987	$100,000 x 8% = $8,000
1988	$100,000 x 7% = $7,000
1989	$100,000 x 7% = $7,000
1990	$100,000 x 6% = $6,000
1991	$100,000 x 5% = $5,000
1992	$100,000 x 5% = $5,000

Alternate ACRS Method

An election to depreciate ACRS property by the straight-line method, over either the regular recovery period or a longer recovery period, could have been made on a timely filed tax return for the year the property was placed in service. This election can only be revoked with the IRS Commissioner's consent, which will be given only in extraordinary circumstances.

While this election could be made on a property-by-property basis for most real property, for property in the 3-, 5-, and 10-year classes, the election, if made, applied to all other property in the same class placed in service that year.

The following are the choices of recovery periods that could have been made:

Class	Choices for Recovery Periods
3-year	3, 5, or 12 years
5-year	5, 12, or 25 years
10-year	10, 25, or 35 years
15-year*	15, 35, or 45 years
18-year	18, 35, or 45 years
19-year	19, 35, or 45 years

* This includes low-income housing.

Based on the above recovery periods available, the straight-line percentages to be used for a **full year's depreciation** are:

Recovery Period	Percentage*
5 years	20%
10 years	10%
12 years	8.333%
15 years	6.667%
25 years	4%
18, 19, 35, or 45 years	Use the ACRS percentage tables at the back of this guide for the Alternate ACRS Method

* Unlike using the tables, where you must know the tax year in which the property is currently in service in order to determine the percentage to be used, here the required averaging conventions must be applied to these percentages. This must be done when electing to use the Alternate ACRS Method over a recovery period of 5, 10, 12, 15, or 25 years and, thereby, using the above percentages.

To apply the half-year convention if you elected straight-line depreciation for property in the 3-, 5-, or 10-year classes, you would have used one-half of the above percentage figures in the year it was placed in service, and again in its last year of depreciation, if the property is still in service. If the property is disposed of before the end of the recovery period, however, it receives no depreciation in the year of disposition.

Example: A business elects to use the Alternate ACRS Method for 5-year ACRS property and decides to elect the 5-year recovery period.

Result: The property's depreciable basis will actually be recovered over 6 years (assuming no short tax years occur): a half year of depreciation (10%) in year 1, followed by 4 full 12-month years of depreciation (20% each year), and finally, another half year of depreciation (10%) in year 6.

Example: XYZ, a calendar-year corporation, placed in service the following two properties in March of 1986:

1. 5-year property, costing $500, which it elected to depreciate over the Alternate ACRS Method, using a 12-year recovery period.
2. 19-year real property, costing $100,000, which it elected to depreciate over the Alternate ACRS Method, using a 35-year recovery period.

Result: For 1986, you need to use the half-year convention for the 5-year property and the midmonth convention for the 19-year property. However, remember that unlike the 5-year property, the adjustment for the 19-year property, which uses the midmonth convention, is already built into the tables.

Therefore, for 1986, the following depreciation is calculated:

5-Year Property:

12-year straight-line percentage = 8.333%

8.333% x $500 = $42 (rounded)

$42 x 1/2 (half-year convention)	=	$ 21

19-Year Property:

Using **Table A 13**, the percentage for the first year, placed in service in the third month, is 2.3%

$100,000 x 2.3%	=	2,300
Total 1986 ACRS Deduction	=	$2,321

For 1992, the following depreciation is calculated:

5-Year Property:

12-year straight-line percentage = 8.333%

8.333% x $500	=	$ 42

19-Year Property:

Using **Table A 13**, the percentage for the 7th year, placed in service in the third month, is 2.9%

$100,000 x 2.9%	=	2,900
Total 1986 ACRS Deduction	=	$2,942

Short Tax Years

The ACRS percentages in the tables are all based on a full 12-month tax year. If at any time a tax year is less than 12 months, the depreciation should be determined for a full year, and then prorated.

How To:

Using the percentage found in the table, apply it to the property's basis to determine the deduction for a 12-month year. Multiply this by the following fraction:

$$\frac{\textit{Number of Months in the Short Year}}{12}$$

Thereafter, you can continue to use the percentage tables in the following years, with no further adjustment required. The property will still have depreciable basis, however, after the recovery period has ended. The remaining unrecovered basis (the amount that could not be deducted in the short tax year) may be deducted in the year following the recovery period, **as long as it does not exceed the amount of the deduction normally allowed in the last year of the recovery period**. If the latter is not the case (probably due to more than one short tax year occurring during the property's recovery period), the remaining basis, in the same amount as allowed in the last year of the recovery period, may continue to be deducted each year until completely recovered.

The above rules apply to both regular ACRS (accelerated depreciation) and the Alternate ACRS Method (straight-line).

If a short tax year occurs in the year in which the asset is disposed of, no adjustment is required. However, see the next segment for an explanation of why this is so.

Example: XYZ, a calendar-year corporation, places in service 10-year property, costing $1,000, on January 1, 1982. In 1985, XYZ changed its **accounting period** to a July 31 year end, and filed a 7-month short-year return.

Result: The following depreciation is calculated:

Tax Year Ending	Depreciation Calculation		
12/31/82	$1,000 x 8%*	=	$ 80
12/31/83	$1,000 x 14%	=	140
12/31/84	$1,000 x 12%	=	120
7/31/85	$1,000 x 10% x 7/12 (7-month short tax year)	=	58
7/31/86 and 1987	$1,000 x 10%	=	100 each year
7/31/88 – 7/31/91	$1,000 x 9%	=	90 each year
7/31/92	The remaining basis	=	42

* No adjustment needs to be made for the half-year averaging convention, since this is already built into the tables.

Early Dispositions

An early disposition occurs when property is sold, exchanged, retired, abandoned, or destroyed before the end of its recovery period.

If the early disposition involves 3-, 5-, or 10-year property, **no depreciation is allowed in the year of the disposition!**

If the early disposition involves 15-, 18-, or 19-year real property, depreciation is taken in the year of disposition for the number of months in service and according to the proper averaging convention. This is best summarized in the chart below:

Dispositions of ACRS Real Property		
Class	**Averaging Convention**	**Result**
15-year	Full-month	No depreciation in month of disposition
18-year in service before 6/23/84	Full-month	No depreciation in month of disposition
18-year in service after 6/22/84 *and* 19-year	Midmonth	Half month depreciation in month of disposition

Note: If the year of disposition is a short tax year, it has no effect on the calculation, since the 15-, 18-, and 19-year real property is only depreciated for the number of months in which it is in use.

Example: XYZ, a calendar-year corporation, placed in service a rental house, costing $100,000, on February 4, 1984, and sold it on June 2, 1992.

Result: This is 15-year property. Using **Table A 1**, the full year's depreciation for 1992 is $100,000 x 6% = $6,000. This amount is then prorated for the 5 months in 1992 (the month of disposition is not counted):

$6,000 x 5/12 = $2,500, which is the 1992 ACRS deduction.

Example: XYZ, a calendar-year corporation, placed in service a rental house, costing $100,000, on August 9, 1984, and sold it on October 20, 1992.

Result: This is 18-year property, and since it was placed in service after 6/22/84, the midmonth convention applies. Using **Table A 4**, the full year's depreciation for 1992 is $100,000 x 5% = $5,000. Prorate this for the 9.5 months it was used in 1992 (a half month's depreciation is given for the month of disposition):

$5,000 x 9.5/12 = $3,958

Property Excluded From ACRS

There are certain categories of property that are specifically excluded from being depreciated under ACRS. The following types of property are *excluded* from ACRS:

1. Any portion of an otherwise depreciable asset for which the Section 179 expense was elected.
2. Property that the business elected to depreciate over a method that is not based on a life in years, such as a Production or Use Method, or the Income Forecast Method.
3. Certain pre-1985 motion picture film or videotape.
4. Assets that are amortized (intangible assets and certain leasehold improvements).

Note: For leasehold improvements placed in service after 1980 and before 1987, if the remaining lease term was shorter than the prescribed ACRS recovery period, the leasehold improvements were amortized over the lease term, rather than depreciated over the ACRS recovery period of 15, 18, or 19 years (depending on when the building was placed in service). The remaining lease term included renewal periods if (a) the term remaining on the lease (excluding renewal periods) was less than 60% of the ACRS recovery period *and* (b) it could *not* be shown that the lease would *not* be renewed.

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5. Certain public utility property, unless a normalization method of accounting is used.
6. Property subject to the anti-churning rules, explained below.

Anti-Churning Rules

As previously discussed in Chapter 2 on MACRS, special rules were created to prevent the "churning," or conversion, of pre-1981 property into recovery property in order to claim the larger ACRS depreciation deductions. These rules, which originally were created for ACRS property, were continued under MACRS, with some modifications.

Anti-Churning Transactions

To come under the anti-churning rules, and thus not be subject to ACRS, the property must be acquired after 1980, in one of the following types of transactions:

1. The taxpayer or a related party owned or used the property in 1980.
2. The taxpayer leases the property to an entity (or a related party) that owned or used the property in 1980.
3. It is personal property that was acquired from someone who owned it in 1980, and as part of the transaction, the user of the property does not change.
4. It is personal property that was not ACRS property in the hands of the previous owner from whom acquired, and the user of the property does not change after the acquisition.
5. It is real property that was acquired in a transaction in which some gain or loss was not recognized. ACRS only applies to the portion of the basis for which the business paid cash or gave unlike property.

Note: The first two types of transactions apply to both personal and real property, the third and fourth transaction types apply only to personal property, and the last transaction type applies only to real property.

Also, under the anti-churning rules, property is not considered as owned before it is placed in service. However, the property does not have to be used for business or income-producing purposes to be considered as placed in service. Thus, if the property is available for its intended function, even if it is being used personally, it is still considered as placed in service.

If the anti-churning rules apply, the property should be depreciated under the pre-1981 rules (see the next chapter).

For a discussion of the related party rules for all anti-churning transactions, see "Property Excluded From MACRS," page IV-66.

Changes in How Property Is Used

There are special rules for when a business changes the use of ACRS property (former IRS Code Sec. **168(f)(13)**). If the type of business use changes, the ACRS property class may change. A good example of this is when ACRS property starts or ceases to be used for research and development. When this occurs, the property is reclassified, and this may result in the property acquiring either a shorter or longer recovery period.

Change to a Shorter Recovery Period

If a change in the use of the property results in its acquiring a shorter recovery period, the business has a choice. The business may continue to depreciate the property as if the change did not occur, or it may calculate the depreciation deduction for the year, and all future years, as if the property was placed in service in the year the change occurred (IRS Code Reg. **1.168-2(j)(3)(A)**). If the latter is chosen, depreciation will be calculated on the property's adjusted basis (per IRS Code Sec. **1016(a)(2)&(3)** that *includes* an adjustment for prior year depreciation).

Example: In 1984, a business with 5-year ACRS property costing $1,000, which it had placed in service the previous year, begins to use the property solely for research and development.

Result: The change in use for research and development causes the property to be reclassified from 5-year property to 3-year property:

Property Class	Recovery Year	Depreciable Basis		ACRS %		Depreciation
5-year	1983	$1,000	x	15%	=	$ 150
3-year	1984	$ 850*	x	25%	=	212
3-year	1985	850	x	38%	=	323
3-year	1986	850	x	37%	=	315
		Total Depreciation			=	$1,000

* $1,000 basis less $150 depreciation previously taken.

Change to a Longer Recovery Period

If a change in the use of the property results in its acquiring a longer recovery period, depreciation will be calculated as if the property was originally assigned to the longer recovery class (IRS Code Reg. **1.168-2(j)(3)(B)** and **1.168-2(d)(3)**). In the year in which the change occurs, however, depreciation must also be recalculated on the property as if it had always had the longer recovery period since first placed in service. An adjustment is then made for the excess depreciation claimed under the originally shorter recovery period. When making the calculation, no change in the property's unadjusted basis is made.

How To:

1. Calculate depreciation on the property as if the property had always used the longer recovery period percentage.
2. Subtract the result of Step 1 from the amount of depreciation originally calculated using the shorter recovery period. This determines the excess of depreciation claimed.

3. Multiply the result of Step 2 by the current year's applicable percentage for the now longer recovery period, divided by the sum of the remaining unused recovery percentage:

$$\begin{array}{c}\textit{Result of Step 2}\\ \textit{(Excess Deprec.)}\end{array} \times \frac{\textit{Applicable Recovery \% for current year}}{\begin{array}{c}\textit{100\% minus Sum of prior deprec. \% that should have been}\\ \textit{claimed (if the longer recovery period had been used)}\end{array}}$$

4. Calculate current year depreciation on the unadjusted basis using the current year's applicable percentage for the longer recovery period.
5. Deduct the result of Step 3 from the result of Step 4. This is the amount of allowed depreciation for the current year.

Example: In 1986, a business with 3-year ACRS property costing $1,000, which it had placed in service the previous year for use in research and development, converts the property's use to its now being used daily in the operation of the business.

Result: The change in the property's use causes it to be reclassified from 3-year property to 5-year property.

Originally, in 1985, depreciation was calculated as follows:

Property Class	Recovery Year	Depreciabl e Basis		ACRS %		Depreciatio n
3-year	1985	$1,000	x	25%	=	$250*

1. Depreciation is recalculated for 1985, using the longer recovery period:

Property Class	Recovery Year	Depreciabl e Basis		ACRS %		Depreciatio n
5-year	1985	$1,000	x	15%	=	$150*

2. * Subtract the result of Step 1 from the amount of depreciation originally claimed. This determines that the amount of excess depreciation is $100 ($250 – $150).
3. Multiply the result of Step 2 ($100) by the current year's (1986) applicable percentage for the 5-year recovery period (22%), divided by the sum of the remaining unused recovery percentage:

$$\textit{\$100 (excess depreciation)} \times \frac{22\%}{100\% - 15\%} = \$26$$

4. In 1986, depreciation is calculated as follows, using the second-year percentage (22%) for 5-year recovery property:

$1,000 x 22% = $220

5. Deduct the result of Step 3 from the result of Step 4:

$220 – $26 = $194

Therefore, $194 of depreciation may be taken in 1986.

Note: In order to determine the amount of allowable depreciation on foreign property (i.e., property used outside of the United States) for which there is a change in use, see IRS Proposed Reg. **1.168-2(j)(4).**

Section IV: Chapter 6: Depreciation of Nonrecovery Property

In this section:

Property that is not subject to either ACRS or MACRS is often referred to as "nonrecovery" property. Just as there are still assets being depreciated under ACRS, so are there assets first placed in service before 1981 and that are still being depreciated according to the methods available at that time. Such methods must continue to be used until the property's depreciable basis has been fully recovered, or until the property's useful life has expired.

In addition to property placed in service by a business prior to 1981, there are other situations that cause property to be classified as nonrecovery. We have already mentioned that there are certain types of fixed assets that lend themselves better to a depreciation method not based on a life in years, and for which an election is made to utilize a production or use method of depreciation. For other property, the income forecast method may be used. Also, due to the anti-churning rules, there exists some property that was originally placed in service prior to 1981 and, although not used in a business until much later, may not be considered recovery property; for this property, the older methods of depreciation must be used. Finally, there are certain states that for state income tax purposes have not accepted the federal government's rules for MACRS or ACRS and continue to use the pre-1981 methods.

Differences Compared With Recovery Property

There are three basic differences between depreciation for recovery versus nonrecovery property:

1. *Prescribed Life.* While the depreciable basis of recovery property is deducted over a statutory recovery period, for nonrecovery property there is more of a choice. A business may use the property's realistic useful life, the class life under the Asset Depreciation Range System (ADR), or a depreciation method not related to a measurement of time.

Note: The ADR class life can only be used for property placed in service after 1970 (IRS Reg. **1.167(a)-11**).

2. *Salvage Value.* While MACRS and ACRS both recover the property's entire depreciable basis, nonrecovery property usually has an amount determined to be its salvage value that is not recovered through depreciation.
3. *Depreciation Method.* While MACRS and ACRS use depreciation methods prescribed by law, nonrecovery property may use any reasonable method of depreciation. There are, however, a few limitations that will be discussed later in this chapter.

Depreciation Methods

There are various depreciation methods used for nonrecovery property. Except for certain limitations, which will be discussed shortly, any reasonable method may be used.

Straight-Line, Declining-Balance, and Sum-of-the-Years'-Digits

The most common depreciation methods used for nonrecovery property are straight-line, declining-balance, and sum-of-the-years'-digits. All of these are described in detail in Section III: "Depreciation for Financial Reporting." To use any of these methods, you need to first determine the property's useful life, its depreciable basis, and its salvage value, if any. To understand everything that needs to be considered when deciding on the property's life, basis, and salvage value, you may want to refer to Section I: "Fundamentals of Depreciation."

Production or Use Method

If the property's usefulness is more dependent on its frequency of use, many businesses elect to use a production or use method of depreciation. These methods are described in detail in Section III: "Depreciation for Financial Reporting."

Income Forecasting

The use of certain types of property is more accurately related to the amount of income earned by them, rather than any passage of time or output produced. Such property may be depreciated under the income forecast method.

What Property Can Use This Method?

There are some types of property that are specifically excluded from both ACRS and MACRS, and either the straight-line method of depreciation or the income forecast method are required to be used. Generally, this rule applies to motion picture films, videotapes, and sound recordings placed in service after March 28, 1985.

TIP
If a business can show that a videotape has a useful life of less than 1 year, the tape may be expensed in the year placed in service. For businesses that rent videotapes, this is often the case for the more popular movies.

The Taxpayer Relief Act of 1997 specifically limits the use of the income forecast method of depreciation to the following types of property, placed in service after August 5, 1997: film, video tapes, sound recordings, copyrights, books, and patents. Although the 1997 Tax Act also includes “other property to be specified by regulations,” it clearly states that any forthcoming regulations must restrict the use of the income forecast method to property either whose life cannot be adequately determined by the passage of time or that generates income on such an irregular basis that using any other depreciation method would distort income.

Furthermore, the 1997 Tax Act states that the income forecast method cannot be used to calculate depreciation on consumer durables (i.e., property generally used in the home for personal use such as televisions and furniture) that are subject to rent-to-own contracts. Such property must be depreciated according to MACRS.

How Do I Use This Method?

Under the income forecasting method, the property’s annual depreciation is based on the following two amounts:

- An estimate of the total amount of income the property will earn over its life. (For property placed in service after 9/13/95, the estimate only includes income that the property generates in the first eleven years of its life; see the note below.)
- The percentage of that income actually earned each year.

Note: September 14, 1995 is the effective date for several changes that were made to the income forecasting rules with the passage of the Small Business Job Protection Act of 1996. Another change requires property with an unadjusted basis of more than $100,000 to be subject to the "look-back method." This requires that depreciation be recomputed based on actual income earned by the property and interest paid on any underpayment of tax in the property's third and tenth years of use.

How To:

$$\textit{Depreciable Basis} \times \frac{\textit{Current Year's Net Income* From Asset}}{\textit{Total Estimated Net Income From Asset}} = \textit{Annual Depreciation}$$

* Net income does not include depreciation expense.

Example: XYZ owns a motion picture, costing $50,000, and that is expected to earn $800,000 over the next several years. The film will be depreciated using the income forecast method. Assume there is no salvage value.

Result: The following depreciation is calculated, based on the income earned each year from the film, given below:

Year	Income Earned From Film	Depreciation Calculation		
1	$500,000	$50,000 x (500,000/800,000)	=	$31,250
2	$250,000	$50,000 x (250,000/800,000)	=	$15,626
3	-0-	No depreciation allowed!	=	0
4	$50,000	$50,000 x (50,000/800,000)	=	$ 3,125
		Total Depreciation	=	$50,000

Asset Depreciation Range System

Property placed in service after 1970 and before 1981 that is not recovery property may be depreciated under the Asset Depreciation Range System (ADR). ADR is based on the asset guideline system, which groups assets by industry type and, except for land improvements, gives a range of years (in addition to the "class life") over which the property can be depreciated. Each asset depreciation range has both an upper and lower limit that is about 20% above and below the class life. Land improvements are assigned a class life over which they are depreciated.

ADR was never mandatory. It was elected on an annual basis, but if elected for a particular tax year, all assets placed in service during that year for the business had to use it.

Note: An advantage of ADR is that it gives the taxpayer peace of mind that the useful lives chosen cannot be questioned by the IRS.

ADR Vintage Accounts

When a business elected to use ADR in any particular year, it also needed to decide whether to depreciate its assets in individual item accounts or in multiple asset accounts, grouped by the year placed in service. These accounts are called "vintage accounts," with the "vintage" being the tax year in which the asset or assets are placed in service. If multiple asset vintage accounts are used, each account is set up for assets with an identical class life and that are placed in service during the same year. There is no limit to the number of vintage accounts that may be set up. There may be more than one vintage account for different assets with the same class life.

Note: Certain types of property that may have the same class life are not allowed to be in the same vintage account. Separate vintage accounts are required for personal and real property, new and used property, and assets for which additional first-year depreciation was elected.

ADR Depreciation Methods

Allowable methods of depreciation are straight-line, declining-balance, and sum-of-the-years'-digits. The same depreciation period is used for an entire vintage account.

ADR Early Dispositions

There is a set of rules governing ADR retirements that is much more complex than the rules for dispositions of other types of property (IRS Reg. **1.167(a)-11(d)(3)**). In addition, there are different rules depending on whether the asset is in an individual item account or in a multiple asset account.

ADR distinguishes between two types of retirements: ordinary and extraordinary. By definition, ordinary is any retirement not classified as extraordinary. An extraordinary retirement of ADR property is a retirement of:

- Real property.
- Personal property retired due to a casualty for which the taxpayer consistently treats all similar casualties as extraordinary (such as fire or theft).
- Personal property retired as a direct result of the termination or disposition of a business facility.
- Personal property retired by qualifying as a deductible charitable contribution after 1980.

Every vintage account has a reserve account for depreciation claimed on it in prior years. The reserve account is also adjusted when an asset is retired, but again, the various adjustments are complex. For example, if an ordinary retirement occurs, any proceeds from the retirement are added to the reserve account.

No loss is recognized on an ordinary retirement until the last asset in the account is retired. Gain may be recognized per the limits of IRS Reg. **1.167(a)-11(d)(3)(iii)**.

The treatment of extraordinary ADR retirements is very complicated and will not be handled in this guide. See IRS Reg. **1.167(a)-11(d)(3)(iv)**.

Once the last asset in a vintage account is retired, the vintage account itself is eliminated.

Principles for Calculating Depreciation for Nonrecovery Property

As with all depreciation methods, there are certain principles that must be followed when depreciating nonrecovery property:

Consistency

Although any reasonable method of depreciation is used for nonrecovery property, once used, the chosen method has to be used consistently throughout the property's useful life. The only changes in methods that are allowed without prior approval by the IRS Commissioner are:

- Changing to straight-line when using a declining-balance method.
- Changing to a less accelerated method for residential rental property when the 80% test is not met (see "Limitations on Using Accelerated Methods," page IV-122).
- If using the ADR system, changing from a declining-balance method to the sum-of-the-years'-digits, or from either of these methods to straight-line.

Note: Once chosen, the same depreciation method must be followed for the life of the property, except for the above exceptions, unless the taxpayer applies for a change in accounting method with the IRS. However, the same method of depreciation does *not* have to be used for all assets placed in service the same year or for similar assets placed in service in different years.

Useful Life

Although the depreciation method being used generally cannot be changed, the property's useful life sometimes may be revised. In order for an asset's life to be changed, the change must be significant and there must be a good reason for it. The life originally assigned may simply no longer reflect the property's true life due to such factors as technological change, obsolescence, or inadequate maintenance on the asset.

If an asset's useful life becomes either shorter or longer, future depreciation on the asset will be calculated on its remaining depreciable basis over its newly determined life.

Example: XYZ places in service a $15,000 computer in 1980. It decides to depreciate it over 10 years, using the straight-line method, and estimates no salvage value. In 1983, due to technological improvements, XYZ decides the computer will be used for only 3 more years before it will be replaced.

Result: Using the half-year convention:

Year	Depreciation Calculation		
1980	$\frac{\$15{,}000}{10\ years} \times \frac{1}{2}$	=	\$ 750
1981 and 1982	$\frac{\$15{,}000}{10\ years}$	=	\$1,500 each year
1983-1985	$\frac{\$15{,}000 - \$3{,}750\ (prior\ depreciation)}{3\ years}$	=	\$3,750 each year

Averaging Conventions

Unlike ACRS and MACRS, there are no prescribed averaging conventions for nonrecovery property. Whatever method is used must be reasonable and applied consistently. Generally, depreciation is computed based on the actual period of use, unless the property is being depreciated under the ADR system.

If the ADR system is being used there are two common averaging conventions:

- *Half-Year Convention.* This convention allows a half year of depreciation in the year in which the property is either placed in service or disposed.
- *Modified Half-Year Convention.* This convention treats all property placed in service in the first half of the tax year as if occurring on the first day of the tax year. Any property placed in service during the second half of the tax year is treated as if occurring on the first day of the *next* tax year.

The modified half-year convention results in a full year of depreciation on property placed in service during the first half of the year and no depreciation on property placed in service in the second half of the year. The treatment of dispositions under the modified half-year convention is more complex. Their treatment is based on when the asset was originally placed in service and may best be summarized in the following chart:

If Asset Was Placed in Service in the:	AND Disposed of in the:	Amount of Depreciation in Disposal Year:
First half of year	First half of year	No depreciation
First half of year	Second half of year	50% of full year's depreciation
Second half of year	First half of year	50% of full year's depreciation
Second half of year	Second half of year*	Full year of depreciation

* To earn the full year of depreciation, the disposal must have been in a year *after* the year it was placed in service.

Limitations on Using Accelerated Methods

There are certain limitations as to what property may be depreciated using the accelerated methods of depreciation:

- 200% declining-balance or sum-of-the-years'-digits may be used for:
  - Property with a useful life of 3 years or more.
  - New (versus used) personal property.
  - New residential rental real property.
  - Used residential rental property placed in service *before* July 25, 1969.
- 150% declining-balance may be used for:
  - All of the above.
  - Used personal property.
  - New nonresidential real property.
- 125% declining-balance may be used for:
  - All of the above.
  - Used residential rental property with a life of 20 years or more.
- Straight-line may be used for:
  - All of the above.
  - Used nonresidential real property.
  - Used residential rental property with a life of less than 20 years.

Property for which the business is not the original owner is considered to be "used." Any improvements to used property, however, are considered "new" and may be depreciated using the more accelerated methods.

Residential Rental Property

To qualify as residential rental property, at least 80% of the property's gross rental income must be derived from dwelling units that are not for transient use. In other words, a motel or hotel does not qualify as residential rental property. Also, the 80% test must be met each year. Any year in which new residential property does not qualify as rental property, the depreciation method must be changed to either the 150% declining-balance method or any less accelerated method. Used residential property that no longer qualifies as rental property must use straight-line depreciation.

Note: The above change does not require the approval of the IRS, as long as the property originally qualified for and used the most accelerated method available (either 200% declining-balance or sum-of-the-years'-digits for *new* residential property or 125% declining-balance for *used* residential property) *and* also reverts back to one of those methods as soon as the property once again qualifies under the 80% test.

How To:

The above rule will sometimes result in several changes in depreciation methods over the life of the property:

1. If changing to straight-line:

$$\frac{(\textit{Property's basis} - \textit{Accumulated depreciation}) - \textit{Salvage value}}{\textit{REMAINING useful life in years}}$$

2. If changing to a declining-balance method:

$$\frac{\textit{Property's basis} - \textit{Accumulated depreciation}}{\textit{ORIGINAL useful life}} \times \textit{Applicable percentage}^*$$

* The applicable percentage will be 200%, 150%, or 125%, depending on the facts and circumstances of the particular property.

3. If changing to sum-of-the-years'-digits:

$$(\textit{Property's basis} - \textit{Accum. deprec.}) - \textit{Salvage value} \times \frac{\textit{Useful life remaining}}{\textit{SYD of REMAINING life}}$$

Example: XYZ, a calendar-year corporation, places in service a new residential rental building, costing $100,000, on January 1, 1970. The building has a 40-year useful life and a salvage value of $10,000. The building has the following history of use:

- In 1970, it does not meet the 80% rental income test. XYZ uses 150% declining-balance, the most accelerated method available for new real property that does not qualify as rental property.
- In 1971, it qualifies as rental property by passing the 80% test and XYZ uses the sum-of-the-years'-digits method.
- In 1972, it fails the 80% test once again and XYZ returns to using 150% declining-balance.

Result: Since XYZ always used the most accelerated depreciation method available, the changes do not require the consent of the IRS:

1970 — Using 150% Declining-Balance:

$$\frac{\$100{,}000 \text{ Basis (no accumulated depreciation yet)}}{40\text{-year life}} \times 1.5 \text{ (depreciation rate)} = \$3{,}750$$

1971 — Using Sum-of-the-Years'-Digits:

$$(\$100{,}000 - \$3{,}750 \text{ depreciation}) - \$10{,}000 \text{ salvage} \times \frac{39 \text{ years remaining life}}{780^*} = \$4{,}312.50$$

* The sum-of-the-years'-digits of the remaining life of 39 is 780. As we discussed in the earlier Section III of this guide, Depreciation for Financial Reporting, the formula for computing the sum-of-the-years'-digits, where *n* represents the life in years, is:

$$\frac{n\,(n + 1)}{2}$$

Here we are using the *remaining* life of 39 years:

$$\frac{39\,(39 + 1)}{2} = 780$$

1972 — Using 150% Declining-Balance:

$$\frac{\$100{,}000 - \$8{,}062.50 \text{ Accum. depreciation}}{40 \text{ years (original life)}} \times 1.5 \text{ Depreciation rate} = \$3{,}447.66$$

Additional First-Year Depreciation

For depreciable personal property with a useful life of at least 6 years and placed in service before 1981, additional depreciation, or "additional bonus depreciation," could have been claimed for 20% of its basis, up to $2,000 a year. Such depreciation is handled the same as the present Section 179 expense deduction in that it reduces the asset's basis before computing depreciation.

Basis Reduced by Investment Tax Credit

As explained in the previous chapter on ACRS property, the Investment Tax Credit (ITC) for qualifying property placed in service after 1982 and before 1986 permitted a reduction in the asset's basis. This credit allowed a business to reduce an asset's basis by 50% of the credit claimed in order to take the full amount of the allowable credit. There were several types of nonrecovery property that were placed in service after 1982 but that still qualified for Investment Tax Credit. These included property depreciated by a production or use method, certain property used outside of the U.S., and certain public utility property.

If the full amount of Investment Tax Credit was taken (thereby causing the asset's basis to be reduced), the amount of the credit depended on the useful life of the property:

Useful life of property	Amount of basis on which the credit was taken	Amount of credit
7 or more years	100%	10%
5 or 6 years	66 2/3%	10%
3 or 4 years	33 1/3%	10%

How To:

To determine the amount by which an asset's basis must be reduced if the full amount of Investment Tax Credit (ITC) was taken:

$$\textit{ITC Basis of Property} \times \textit{Applicable \%*} \times \textit{10\% ITC} \times \textit{50\%} = \textit{Basis Reduction}$$

* The "applicable percentage" is the percent of the property's basis on which the ITC is taken; it is based on the property's useful life. As displayed in the previous table, if the property's useful life is seven or more years, the applicable percentage is 100%; if it is five or six years, the applicable percentage is 66 2/3%; and if it is three or four years, the applicable percentage is 33 1/3%.

Note: There were several other factors that could have reduced the amount of Investment Tax Credit and, thus, the amount of the basis reduction. A list of these factors may be found in the previous chapter on ACRS property, in "ACRS Depreciation Methods," page IV-99.

Section IV: Chapter 7: Depreciation and the Alternative Minimum Tax (AMT)

In this section:

Note: The Alternative Minimum Tax (AMT) was repealed by the Tax Cuts and Jobs Act of 2017 for corporations, effective for tax years beginning January 1, 2018 and later. AMT is still in effect for individuals.

The purpose behind the **Alternative Minimum Tax** (AMT) is to ensure that taxpayers with high incomes pay at least a minimum amount of income tax. Frequently, high income taxpayers are able to avail themselves of various tax benefits and income exclusions, which allow them to greatly reduce their tax liabilities. The Alternative Minimum Tax is an attempt to make the tax laws more equitable. It applies to C corporations, individuals, trusts, and estates.

Note: Although S corporations and partnerships are not assessed the AMT at the entity level, the items that are used to compute it are passed through to the shareholders and partners on their K-1s.

The Alternative Minimum Tax computation starts with the entity's taxable income, makes various adjustments to it, subtracts out an exemption amount, and applies a flat tax rate to the result. This is then compared to the regularly computed income tax for the entity. Only if the computed Alternative Minimum Tax is more will the AMT then take precedence over the regular tax. In other words, AMT is not an additional tax, but rather a minimum tax. If the regular income tax is more than AMT, then the AMT calculation is ignored.

While the Alternative Minimum Tax for individuals has been in place for some time, the Alternative Minimum Tax for corporations came later. The Corporation Alternative Minimum Tax, created by the Tax Reform Act of 1986, replaced the former add-on minimum tax for corporations, for tax years starting after 1986. Now, the Taxpayer Relief Act of 1997 has changed the Alternative Minimum Tax rules for corporations once again.

With the passage of the Taxpayer Relief Act of 1997, certain “small business corporations” are exempt from the Alternative Minimum Tax beginning after December 31, 1997. To qualify for the AMT exemption, a corporation must have average gross receipts of less than $5 million for the last three taxable years beginning after December 31, 1993. A qualifying corporation does not have to compute AMT beginning in 1998. However, once a small business corporation has average gross receipts exceeding $7.5 million for a three-year period (not including the first year that the corporation achieves its small business corporation status), it loses its exemption. Although it must once again calculate AMT, the change is prospective. For example, the corporation must begin calculating AMT depreciation on assets placed in service in the year after the loss of small business status.

The objective of the Alternate Minimum Tax is to eliminate the tax advantages, for the higher income taxpayers, of some of the items that receive favorable tax treatment. There is a wide range of tax areas that are affected by the Alternative Minimum Tax, with depreciation being one of the most common. With the appearance of ACRS and MACRS, which allow accelerated depreciation for most assets, depreciation became a major issue when calculating the Alternative Minimum Tax.

Generally, for assets placed in service before 1999, depreciation for the Alternative Minimum Tax is calculated over longer recovery periods than for regular tax purposes, using either less accelerated or straight-line depreciation methods. For assets placed in service after December 31, 1998, AMT depreciation uses the same recovery period for AMT purposes and regular tax purposes, but the depreciation method may be less accelerated. The differences between depreciation used to compute regular taxable income and that used to compute AMT income are of three types:

1. An **“Adjustment”** for depreciation on personal and real property placed in service after 1986.
2. A **“Tax Preference”** affecting:
   - **a.** Accelerated depreciation on real property placed in service before 1987 and
   - **b.** If the entity is either an individual or a personal holding company, accelerated depreciation on leased personal property placed in service before 1987.

> **Note:** Aside from the different types of property affected by AMT Adjustments versus Preferences, the biggest difference between them is that while AMT Adjustments can either increase or decrease AMT income, AMT Tax Preferences can only increase it.

3. An **“Adjusted Current Earnings”** (ACE) adjustment, which affects a broad range of depreciation for property placed in service after 1980 and before 1994. This will be discussed in detail in Section IV: “Chapter 8: Depreciation and Adjusted Current Earnings (ACE).”

How To:

To compute the Alternative Minimum Tax for:

- A Corporation — use IRS Form 4626.
- An Individual — use IRS Form 6251.
- An Estate or Trust — use IRS Form 1041 for 1992 and later; use IRS Form 8656 for 1991 and earlier.

The AMT Adjustment Affecting Depreciation

Although there are many Adjustments to taxable income in order to compute the Alternative Minimum Tax, only one affects depreciation and it involves only MACRS property. In determining the Alternative Minimum Tax, certain MACRS depreciation is recalculated. The difference between the depreciation for AMT purposes and the depreciation for regular tax purposes becomes an Adjustment to income. *An AMT Adjustment may either increase or decrease income.*

To Which MACRS Property Does the AMT Adjustment Apply?

The AMT depreciation Adjustment applies to all pre-1999 MACRS personal and real property that is *not* using straight-line depreciation over the Alternative Depreciation System (ADS) lives. For post-1998 MACRS property, it applies only to personal property using the 200% declining-balance method of depreciation.

The AMT Adjustment applies to any transitional property (placed in service after July 31, 1986) for which MACRS was elected, but it does not apply to property that the business excluded from MACRS, such as property that is being depreciated under a production or use method. Furthermore, the AMT Adjustment does not apply to any property that was expensed under Section 179.

The AMT Adjustment does not apply to property to which the additional first-year depreciation deduction was claimed. The first-year depreciation deduction and all depreciation calculated on the remaining basis are deductible for both regular tax and AMT purposes.

Note: If property was placed in service after 1986 but is being depreciated under ACRS, due to the transitional rules in effect for certain property (usually property subject to earlier contracts), then such property will *not* be subject to an AMT Adjustment. However, this property will be treated as an AMT Tax Preference item. This will be discussed under "AMT Tax Preferences Affecting Depreciation," page IV-134.

Depreciation for Property Subject to the AMT Adjustment

The calculation of depreciation for the Alternative Minimum Tax Adjustment is handled differently for personal and real property. In addition, the Taxpayer Relief Act of 1997 changed the AMT depreciation Adjustment for property placed in service after December 31, 1998. Although any previously owned property must continue to be depreciated for AMT purposes under the pre-97 Tax Act rules, there is now a new set of rules for post-1998 property.

Besides exempting small corporations from the Alternative Minimum Tax, the Taxpayer Relief Act of 1997 made two significant changes to the AMT depreciation Adjustment, effective for property placed in service after December 31, 1998:

- The AMT depreciation Adjustment is eliminated for property that is depreciated for regular tax purposes under the straight-line method.
- The recovery periods for calculating AMT depreciation on all other property will be the same as for regular tax purposes, which will decrease the amount of the AMT depreciation Adjustment.

Personal Property

Under MACRS, there are four alternative methods for depreciating personal property. Depending on the method used and when the asset is placed in service, the depreciation calculation for the Alternative Minimum Tax will be different. If, for regular tax purposes, MACRS property is being depreciated using:

1. *Straight-Line Over the Alternative Depreciation System (ADS) Life:* There is no Adjustment for the Alternative Minimum Tax.
2. Straight-Line *Over the General Depreciation System (GDS) Life:* If the asset is placed in service before 1999, compute AMT depreciation on the asset using straight-line depreciation over its Alternative Depreciation System (ADS) life. If the asset is placed in service after 1998, there is no Adjustment for AMT.
3. 200% *Declining-Balance Over the GDS Life:* If the asset is placed in service before 1999, compute AMT depreciation on the asset using 150% declining-balance, over its Alternative Depreciation System (ADS) life, switching to straight-line depreciation when it results in a larger deduction. If the asset is placed in service after 1998, compute AMT depreciation using 150% declining-balance (with the same rules for switching to straight-line) over the same recovery period as you are using for regular tax purposes.
4. 150% *Declining-Balance Over the Alternative Depreciation System (ADS) Life (if placed in service before 1/1/99) or the GDS life (if placed in service after 12/31/98):* There is no Adjustment for the Alternative Minimum Tax.

How To:

As described above, depending on the type of depreciation used for regular tax purposes, recalculate depreciation using either the ADS method or the 150% declining-balance method. Use the same averaging convention that was used for regular tax purposes (either the half-year or midquarter convention), and do not consider salvage value under either depreciation method. The difference between this and the depreciation used for regular tax purposes is the AMT depreciation Adjustment.

Example: On March 3, 2001, XYZ places in service 3-year MACRS property, costing $1,500, which it depreciates using 200% declining-balance and the half-year convention. The property has a 4-year ADS life.

Result: XYZ computes depreciation as follows:

For Regular Tax Purposes:

$$\frac{\$1,500}{3} \times 2 \times \frac{6}{12} = \$500$$

For AMT Purposes:

$$\frac{\$1,500}{4} \times 1.5 \times \frac{6}{12} = \$281.25$$

Therefore, for the current year, XYZ has a positive Adjustment when determining its AMT of $218.75 ($500 – $281.25).

Note: Remember that a positive AMT Adjustment *increases* income and thus the AMT, and a negative AMT Adjustment *decreases* income and reduces the AMT.

Example: Assume the same facts as above, except that XYZ elected to use the straight-line method over the asset's GDS life of 3 years.

Result: XYZ computes depreciation as follows:

For Regular Tax Purposes:

$$\frac{\$1,500}{3} \times \frac{6}{12} = \$250$$

For AMT Purposes:

$$\frac{\$1,500}{4} \times \frac{6}{12} = \$187.50$$

Therefore, for the current year, XYZ has a positive Adjustment when determining its AMT of $62.50 ($250 – $187.50).

When the 200% declining-balance method is used for regular tax purposes, the regularly computed MACRS depreciation will be greater than that computed for the AMT Adjustment in the early years of an asset's life. However, in later years the AMT depreciation will be greater, and when this occurs, the Adjustment will be a negative amount.

Example: Assume that 7-year MACRS property, costing $10,000, is placed in service prior to 1999. It is being depreciated using 200% declining-balance and the half-year convention. Assume its ADS life is 10 years.

Result: For the AMT Adjustment, 150% declining-balance is used and the following results are computed over the asset's life:

Year	MACRS Depreciation	AMT Depreciation	AMT Adjustment*
1	$ 1,429	$ 750	$ 679
2	2,449	1,388	1,061
3	1,749	1,179	570
4	1,249	1,002	247
5	893	874	19
6	892	874	18
7	893	874	19
8	446	874	(428)
9		874	(874)
10		874	(874)
11		437	(437)
Total	$10,000	$10,000	0

* The AMT Adjustment is the difference between MACRS depreciation and AMT depreciation.

The above example demonstrates several points for MACRS property that is placed in service prior to 1999:

- Starting in the property's later life (the eighth year in this example), the AMT Adjustment becomes a negative amount.
- AMT depreciation can be significantly slower than regular MACRS. In this example, for an asset costing $10,000, during the first 3 years, MACRS depreciation is $5,627, while the AMT depreciation is only $3,317, or a $2,310 difference.
- The difference between regular MACRS depreciation and AMT depreciation becomes even greater if the gap is wider between the asset's life for MACRS and its life for ADS. For example, an airplane, with a 7-year life for MACRS, has a 12-year life for ADS and the AMT calculation.
- Finally, the above example demonstrates that all AMT depreciation Adjustments are simply "timing" differences. In other words, if the property is held for its entire

recovery period, the same amount of depreciation is eventually taken ($10,000 in the above example) for both regular and AMT purposes. An AMT depreciation Adjustment will initially be an increase for computing AMT income, but later in the asset's life, it will actually decrease income.

The AMT Adjustment for excess MACRS depreciation for newer property is netted with the negative AMT Adjustment for older property, and is thereby reduced. It is also possible for the resulting AMT Adjustment to end up being a negative amount. If that occurs, then the taxable income will be reduced.

Example: XYZ has two assets: Property A, which is new, and Property B, which is much older. It has computed the following depreciation for the current year:

	Property A	**Property B**
For regular tax purposes:	$5,000	$3,000
For AMT purposes:	3,000	5,500
Difference:	$2,000	($2,500)

The two amounts are netted and result in a negative Adjustment for AMT of ($500), or ($2,000 – $2,500).

TIP

There are several ways by which the AMT Adjustment for personal property might be avoided, but each technique needs to be thought through and all resulting consequences need to be considered. The following lists the available techniques and suggests *some* of the possible results (remember that the *overall* effect on the business must be considered and each situation will be unique):

1. Expensing qualifying property under Section 179.
   Result: Electing Section 179 expense will greatly speed up depreciation. However, because of the taxable income limitation, it may not be able to be deducted in the current year.
2. Using a production or use method of depreciation where appropriate.
   Result: Depending on the facts and circumstances, this could result in either a quicker or slower rate of depreciation.
3. Electing to use 150% declining-balance for personal property.
   Result: Using 150% declining-balance will reduce the yearly depreciation deductions, as compared to using 200% declining-balance. See also 4. below for other possible effects.
4. Electing to use the ADS method.
   Result: Electing ADS will reduce the yearly depreciation deductions. This may, however, be inconsequential if the business has a large net operating loss either in the current year or being carried forward from prior years. Also, if the business is planning on selling the property or disposing of it some other way before the end of its recovery period, using ADS will either reduce any future gain or increase a future loss.
5. Leasing rather than buying property.
   Result: There are a large number of arguments for and against leasing property, beyond the scope of this guide. There are, however, no AMT Adjustments required for lease payments.

Note: The last two techniques are also available to be used for real property.

Real Property

Under MACRS, real property is depreciated using the straight-line method over either 27.5, 31.5, or 39 years. For AMT purposes, straight-line depreciation will also be used, but if the property is placed in service before 1999, it is depreciated over a 40-year recovery period. By using the longer recovery period, such depreciation will be less for AMT purposes, until the final years. If the property is placed in service after 1998, there will be no AMT depreciation Adjustment.

How To:

For real property placed in service before 1999, use straight-line depreciation over a 40-year life. Use the midmonth convention and do not consider salvage value. The difference between this and the depreciation used for regular tax purposes is the AMT Adjustment.

Example: XYZ is depreciating its factory, which is MACRS property placed in service May 1, 2001, over its recovery period of 39 years. The factory cost $100,000.

Result: Except for the property's first and last recovery years (due to the midmonth convention), XYZ computes depreciation annually as follows:

For Regular Tax Purposes:

$$\frac{\$100{,}000}{39} = \$2{,}564.10$$

For AMT Purposes:

$$\frac{\$100{,}000}{40} = \$2{,}500$$

Therefore, each year there will be a positive Adjustment for AMT of $64.10 ($2,564.10 – $2,500). However, after the 39 years have elapsed, the property will be fully depreciated for regular tax purposes, but not for AMT purposes. When this occurs, there will be a negative Adjustment for AMT of ($2,500) in the next year, assuming the property is still in service.

AMT Tax Preferences Affecting Depreciation

In general, there are fewer AMT Tax Preferences as compared with Adjustments. Two Tax Preferences affect depreciation. For the most part, both of the depreciation Tax Preferences are for property placed in service before 1987. The AMT Tax Preferences are for property being depreciated under either ACRS or the pre-1981 (i.e., nonrecovery) methods.

Unlike the previously described AMT Adjustments, *Tax Preferences may only increase income when computing the Alternative Minimum Tax!* However, like the AMT Adjustments, depreciation on certain property is recalculated, and the difference between the depreciation calculated for AMT purposes and the depreciation calculated for regular tax purposes becomes the Tax Preference amount.

To Which ACRS and Pre-1981 Property Do AMT Tax Preferences Apply?

Tax Preferences apply to property placed in service before 1987 that is either:

- real property using accelerated depreciation, or
- leased personal property using accelerated depreciation, *but only if* the entity is either an individual taxpayer or a personal holding company.

The above description is correct for most property. However, for property that fits either of the above categories, there are three exceptions to the "before 1987" date for being placed in service:

1. Any property being depreciated under MACRS will *not* be treated as a Tax Preference item, even if placed in service before 1987. Such property is, instead, handled as an AMT Adjustment item.
2. Any property being depreciated under ACRS, even if placed in service after 1987, *is* treated as a Tax Preference item.
3. Even if the property is placed in service before 1987, the AMT Tax Preference will not apply if the business was exempt from AMT due to the Taxpayer Relief Act of 1997 and later lost its exemption. In such a case, the business has to calculate AMT depreciation, but only on a prospective basis.

Note: The reason for these exceptions to the date placed in service is due to two types of property: property that, because of earlier construction contracts, qualifies as transitional property and property that falls under the anti-churning rules. Neither of these types of property can be categorized as either MACRS or ACRS property based only on their date placed in service.

As with the AMT Adjustment, property that is being depreciated under the Alternate ACRS method (straight-line depreciation) is excluded from being a Tax Preference item.

Depreciation for Property Subject to an AMT Tax Preference

Depreciation for the Alternative Minimum Tax Preference is calculated on a property-by-property basis for both categories of property (i.e., real and leased personal property). If, at any point, the AMT depreciation calculated for a particular property is *more* than the depreciation calculated on the same property for regular tax purposes, it is ignored and no Tax Preference results. AMT depreciation for the Tax Preference computation is handled differently for real and leased property.

Note: The Tax Preference is not computed for any property in the year in which it is disposed. Therefore, any depreciation allowed in the year of disposition is ignored for AMT purposes. (IRS Reg. **1.57-1(b)(3)** & **1.57-1(c)(3)**)

Real Property

The Tax Preference depreciation for the AMT computation affects two types of real property if they are being depreciated under an accelerated method: ACRS recovery property and pre-1981 nonrecovery property.

Recovery Property

Under ACRS, real property may be depreciated over a 15-, 18-, or 19-year recovery period, based on the date it was first placed in service. For AMT, the property is depreciated using the straight-line method over the same ACRS life that was used to depreciate the property for regular tax purposes and salvage value is not taken into consideration. However, if the property is being depreciated under the Alternate ACRS method (straight-line over a choice of recovery periods) for regular tax purposes, there will be no Tax Preference for AMT.

How To:

Use straight-line depreciation over a 15-, 18-, or 19-year life (i.e., the same life that is used for regular tax purposes). Use the midmonth convention and salvage value is ignored. The difference between this and the depreciation used for regular tax purposes is the AMT Tax Preference.

Note: Depreciation for low-income housing is handled the same way as above for the AMT calculation.

Example: XYZ, a calendar-year corporation, owns real property that was placed in service on January 1, 1986, costing $100,000. It is being depreciated under regular ACRS with a 19-year class life. XYZ needs to compute depreciation for 1992.

Result: XYZ computes depreciation as follows:

For Regular Tax Purposes:

$100,000 x 5.2% (**ACRS Table A 6**) = $5,200

For AMT Purposes:

$100,000 x 5.3% (**ACRS Table A 9**) = $5,300

Since the AMT depreciation is more than the depreciation calculated for regular tax purposes, there is no Tax Preference on the property for 1992.

Nonrecovery Property

For real property that is excluded from ACRS and MACRS, and is therefore considered nonrecovery property, the AMT Tax Preference applies if the property is being depreciated using an accelerated method.

How To:

For AMT, the property is depreciated using the straight-line method over the property's useful life and *salvage value must be deducted* from the property's basis. The difference between this and the depreciation used for regular tax purposes, is the AMT Tax Preference.

Leased Personal Property

If an individual or a personal holding company is depreciating personal property that it is leasing to others, using an accelerated method, such property is subject to the AMT Tax Preference rules. Therefore, the only time a corporation is affected is if it is a personal holding company. The treatment for recovery and nonrecovery property is slightly different.

Recovery Property

For ACRS personal property that is being leased to others and is depreciated using an accelerated method (i.e., straight-line depreciation was not elected), recompute the depreciation for AMT by the straight-line method using the following extended recovery periods:

For:	Use a recovery period of:
3-year property	5 years
5-year property	8 years
10-year property	15 years
15-year public utility property	22 years

How To:

Use straight-line depreciation over the longer recovery period above. Use the half-year convention and do not consider salvage value. The difference between this and the depreciation used for regular tax purposes is the AMT Tax Preference.

There is no Tax Preference if the property is being depreciated over a recovery period longer than that given above.

Nonrecovery Property

If a business owns nonrecovery property that it is leasing to others and that is depreciated using an accelerated method:

How To:

Recompute the depreciation for AMT by the straight-line method over the same useful life used by the taxpayer when computing depreciation for regular tax purposes, *deducting out salvage value*. The difference between this and the depreciation used for regular tax purposes is the AMT Tax Preference.

Note: If you depreciated the property under a method that did not require a useful life or salvage value, then select the useful life and salvage value that would have been correct had the straight-line method been used originally.

AMT Depreciation in General

When computing depreciation for the Alternative Minimum Tax calculation, there are various issues that you need to keep in mind:

Averaging Conventions

When computing the AMT depreciation, use the same averaging convention as used for regular tax purposes:

Property Type		Convention
MACRS	Personal	Half-year or midquarter
	Real	Midmonth
ACRS	Personal	Half-year
	Real	Full-month or midmonth
Nonrecovery	Personal	Convention or actual days*
	Real	

* For nonrecovery property, use whatever was used for regular tax purposes. Nonrecovery property did not always use an averaging convention.

Percentage Tables

Just as there are percentage tables for MACRS depreciation and for ACRS depreciation on real property, there are also percentage tables for calculating the AMT depreciation for all of MACRS property and for ACRS real property. These are included with the tables in the back of this guide. See either "MACRS Percentage Tables," page VI-14, or "ACRS Percentage Tables," page VI-41, preceding the tables, for assistance in locating the appropriate table.

Salvage Value

As in computing MACRS and ACRS depreciation for regular tax purposes, even when using the straight-line method, salvage value is ignored and never deducted from the property's basis when computing depreciation on such property for AMT purposes. However, when computing an AMT Tax Preference **on nonrecovery property, salvage value must be deducted from the property's basis** before the AMT straight-line depreciation is computed.

Miscellaneous AMT Rules Pertaining to Depreciation

The other issues that you need to be aware of are:

1. *Basis of Property.* One effect of having an AMT Adjustment for MACRS property depreciation is that the property will then have a different basis for AMT when computing gain or loss if the property is disposed of before the end of its recovery period. Therefore, yet another AMT Adjustment is created in the year the property is disposed.

Note: Unlike AMT Adjustments, AMT Tax Preferences do NOT create a separate adjusted basis in property for AMT purposes.

Example: In 1995, XYZ places in service an asset costing $1,000. It is 7-year MACRS property, the half-year convention applies, and XYZ is depreciating the asset using 200% declining-balance. The property has a 12-year ADS life. In 1997, the asset is sold for $600.

Result: XYZ makes the following computation:

	For Regular Tax Purposes	For AMT Tax Purposes
Original Cost	$1,000	$1,000
Depreciation (using percentage tables)	(475)	(231)
Adjusted Basis	$ 525	$ 769
Sales Price	$ 600	$ 600
Adjusted Basis	(525)	(769)
Gain on Disposition*	$ 75	
AMT Loss on Disposition*		$ (169)

***How To:**

Enter the difference between the AMT and the regular tax gain or loss as follows:

- If a Corporation: 2013 Form 4626, Line 2e.
- If an Individual: 2013 Form 6251, Line 18.

2. *Luxury Automobile Rules*. Although it has not been clarified in the existing IRS Code or Regulations whether or not the luxury automobile limitations on depreciation apply to the amounts calculated for AMT, it is generally presumed that in fact they do apply. Therefore, when computing the AMT depreciation on luxury automobiles, limit the amount calculated to the luxury auto depreciation allowed for the year. Hence, in most cases, there will be no AMT Adjustment or Tax Preference on luxury automobiles.
3. *Uniform Capitalization Rules*. Depreciation that is capitalized under the uniform capitalization rules of IRS Code Sec. **263A** must be recalculated using the above rules for AMT purposes.
4. *Certified Pollution Control Facilities*. A certified pollution control facility that is being amortized will generate either an AMT Adjustment (if placed in service after

1986, but before 1999) or a Tax Preference (if placed in service before 1987). For more detail, see IRS Code Sec. **56(a)(5)** and IRS Reg. **1.57-1(d)(1)**.

AMT Summary

Except for the ACE Adjustment, which will be discussed in the next chapter, the AMT Adjustments and Tax Preferences are best summarized in chart form:

Type of Property	If Depreciated for Regular Tax Purposes:	Then Depreciate for AMT Purposes:	AMT Recovery Period or Life	AMT Adjustment or Tax Preference
MACRS Personal	200% DB GDS Life	150% DB[1]	ADS Life or GDS Life[2]	Adjustment
Pre-1999 MACRS Personal	Straight-Line GDS Line	Straight-Line	ADS Life	Adjustment
Pre-1999 MACRS Real	Straight-Line 27.5/31.5/39-yr.	Straight-Line	40 years	Adjustment
ACRS Real	Accelerated	Straight-Line	15, 18, 19 Same as Tax	Tax Preference
Pre-81 Real	Accelerated	Straight-Line Deduct Salvage	Useful Life Same as Tax	Tax Preference
ACRS Leased Personal[3]	Accelerated	Straight-Line	Extended Recovery Periods[4]	Tax Preference
Pre-81 Leased Personal[3]	Accelerated	Straight-Line Deduct Salvage	Useful Life Same as Tax	Tax Preference

1 When 150% declining-balance is applicable for computing the AMT depreciation, you must switch to the straight-line method when it results in a larger deduction.

2 If the property is placed in service before 1999, use the ADS life. If it is placed in service after 1998, use the same recovery period as for regular tax purposes.

3 This applies only to personal holding companies and individual taxpayers.

4 These are specific recovery periods. See "Leased Personal Property," page IV-137, for detailed information.

Remember that there is neither an Adjustment nor a Tax Preference for the following:

Type of Property	Depreciation for Regular Tax Purposes
MACRS — Pre-1999 Personal and Real	Straight-Line ADS Life
MACRS — Post-1998 Personal and Real	Straight Line GDS or ADS Life
MACRS — Pre-1999 Personal	150% DB ADS Life
MACRS — Post-1998 Personal	150% DB GDS Life
ACRS — Real and Leased Personal	Straight-Line Alternate ACRS
Pre-81 — Real and Leased Personal	Straight-Line

In addition, if a company qualifies as a small business corporation that is exempt from AMT (according to the Taxpayer Relief Act of 1997), and then loses its AMT exemption, there is neither an Adjustment nor a Tax Preference for any property placed in service through the end of the year in which the corporation loses its exemption.

There is no AMT Adjustment for Indian Reservation property.

Finally, there is no Adjustment for property on which the bonus depreciation was claimed.

AMT Depreciation Worksheet

AMT Adjustment

	Depreciation for regular tax purposes on all MACRS property *not* depreciated under ADS		________
	AMT Depreciation on personal property using 150% declining-balance	________	
	plus		
less	AMT Depreciation on personal property using straight-line over ADS life	________	
	plus		
	AMT Depreciation on real property using straight-line over 40 years	________	
	Subtotal = AMT Depreciation		( )
	AMT Adjustment*		========

* If a Corporation: 2013 IRS Form 4626, Line 2a. If an Individual: 2013 IRS Form 6251, Line 18.

AMT Tax Preference on Real Property

	Depreciation for regular tax purposes on all ACRS and Pre-1981 Real Property using an accelerated method	________
less	AMT Depreciation on real property using straight-line over same ACRS recovery period or Pre-81 property life	( )
	AMT Tax Preference*	========

* If a Corporation: 2013 IRS Form 4626, Line 2o. If an Individual: 2013 IRS Form 6251, Line 27.

AMT Tax Preference on Leased Personal Property

Note: This is only for a personal holding company or an individual taxpayer.

	Depreciation for regular tax purposes on all ACRS and Pre-1981 Leased Personal Property using an accelerated method	________
less	AMT Depreciation on leased personal property using straight-line over either longer ACRS recovery period or same Pre-81 property life	( )
	AMT Tax Preference*	________

* If a Corporation: 2013 IRS Form 4626, Line 2o. If an Individual: 2013 IRS Form 6251, Line 27.

Section IV: Chapter 8: Depreciation and Adjusted Current Earnings (ACE)

In this section:

The Adjusted Current Earnings (ACE) Adjustment is part of the Alternative Minimum Tax (AMT). It is an additional adjustment after making the computations for the other AMT Adjustments and Tax Preferences described in the previous chapter. The Revenue Reconciliation Act of 1989 (IRS Code Sec. **56(g)**) attempted to simplify an earlier AMT adjustment that applied to a corporation's book income. The ACE Adjustment only applies to C corporations and is effective for tax years beginning after 1989.

The purpose of the Adjusted Current Earnings Adjustment is to recapture some of the overall tax savings by corporations that may report large earnings to their shareholders but, due to a variety of tax advantages, avoid paying much tax. Notice that it does *not* apply to S corporations.

Note: The ACE Adjustment also does NOT apply to a Regulated Investment Company (RIC), a Real Estate Investment Trust (REIT), or a Real Estate Mortgage Investment Conduit (REMIC).

Although the ACE Adjustment is still part of the Alternative Minimum Tax calculation, the depreciation component of the ACE Adjustment is being eliminated. The Revenue Reconciliation Act of 1993 eliminates the depreciation adjustment for ACE for property placed in service after December 31, 1993. However, all earlier-owned property that had a depreciation adjustment for computing ACE must continue to be depreciated separately for the ACE Adjustment until the end of its recovery period (or until it is no longer used in the business). The one exception to this is when a corporation is exempt from AMT due to the Taxpayer Relief Act of 1997. When this occurs, the qualifying corporation no longer computes either AMT or ACE, beginning in 1998. Even if the corporation later loses its AMT exemption, it does not need to compute the ACE Adjustment. In such a case, the business only has to calculate AMT depreciation again, on a prospective basis. Therefore, the exemption from the ACE depreciation calculation is a permanent one.

Simply put, when the ACE Adjustment applies, C corporations must recompute current year income (i.e., adjust current earnings, thus "ACE") by adding back certain income that is excluded from regular income tax, as well as adding back the excessive portions of certain deductions. One such "excessive deduction" is accelerated depreciation. Even though the ACE Adjustment was not effective until tax years beginning after 1989, it applies to current depreciation on property that was placed in service after 1980 but before 1994.

The result of the ACE Adjustment is that a C corporation must increase its AMT income by 75% of the excess, if any, of the amount by which its Adjusted Current Earnings exceed its "Pre-Adjustment AMT Income." Pre-Adjustment AMT Income, which is line 4 of the 2008 IRS Form 4626, is AMT income computed before the calculation of any ACE Adjustments or AMT net operating loss.

How To:

Adjusted Current Earnings (ACE) – Pre-Adjustment AMTI = Excess

Excess × 75% = ACE Adjustment

Note: The above is an overview of the "ACE Adjustment," of which the ACE Depreciation Adjustment is a major component.

Example: Suppose that XYZ, a C corporation, has calculated the following:

Adjusted Current Earnings (ACE)	=	$1,500
Pre-Adjustment AMTI	=	$ 500

Result: To determine XYZ's ACE Adjustment:

	$1,500	(ACE)
less	– 500	(Pre-Adjustment AMTI)
	$1,000	(Excess)
times	x 75%	
	$ 750	ACE Adjustment

The $750 ACE Adjustment is added to the Pre-Adjustment AMT Income of $500, to equal $1,250. This amount is then reduced by any AMT net operating loss and any adjustment based on energy preferences, to produce the final Alternative Minimum Taxable Income.

Note: A negative ACE Adjustment is possible to the extent that there was a positive ACE Adjustment in a prior year.

This chapter will explain the ACE Adjustment for depreciation.

ACE Depreciation in General

Of the various items that comprise the ACE Adjustment, depreciation is a major component. In general, for purposes of the ACE computation, depreciation is recalculated for most assets using the MACRS Alternative Depreciation System (ADS). The difference between this and the depreciation recalculated for AMT is the amount of the ACE Depreciation Adjustment.

Note: Understanding the ADS method of depreciation is, therefore, essential to understanding the ACE Depreciation Adjustment. ADS is described in detail in Section IV: "Chapter 2: Modified Accelerated Cost Recovery System (MACRS)." Basically, ADS uses straight-line depreciation, with the same MACRS averaging convention rules, but usually over a longer recovery period.

ACE Depreciation Adjustment Worksheet

	Depreciation for Regular Tax Purposes		______
less	AMT Adjustment Amount (from line 2a*)	______	
	plus		
	AMT Tax Preference on Real Property (line 2o*)	______	
	plus		
	AMT Tax Preference on Personal Property (line 2o*)	______	
	Subtotal = AMT Adjustment and Tax Preferences		( )
equals	Total Depreciation Expense Recomputed for AMT (*before the ACE Adjustment*)**		______
less	Total Depreciation Expense Recomputed for ACE (an additional worksheet (see page IV-160) will be needed to determine this number)		( )
	ACE Depreciation Adjustment* **		______

* Line references are to the 2013 IRS Form 4626, Alternative Minimum Tax – Corporations. Remember that while the Tax Preference amounts can only be positive numbers, the Adjustment amount can be either a positive or a negative number. *A negative AMT Adjustment amount will* ***increase*** *the "Total Depreciation Expense Recomputed for AMT."*

** If you prefer, and have available your worksheet showing what the total depreciation expense recomputed for AMT purposes is, you can skip the above computation and start with this line. However, it is important to remember that *"total depreciation expense recomputed for AMT purposes"* ***includes the regular tax depreciation*** *for any property for which it was NOT necessary to recalculate depreciation for AMT purposes.*

*** This ACE Depreciation Adjustment is then added to "Preadjustment alternative minimum taxable income (AMTI)," line 3 of the 2011 IRS Form 4626, along with the various other ACE Adjustments, to determine the corporation's Adjusted Current Earnings.

The ACE Depreciation Adjustment may be either a positive or a negative amount:

1. If ACE depreciation is *less* than AMT depreciation, a positive amount results, and the difference will *increase* ACE. Remember that the goal of the ACE Adjustment is to increase current earnings in order to increase the amount of tax. Generally, before recomputing depreciation per the prescribed ACE method, the depreciation expense is higher, causing current earnings to be lower. *Thus, the object of the ACE Adjustment is to lower the depreciation expense and cause the current earnings to increase.*

2. If ACE depreciation is *more* than AMT depreciation, a negative amount results, and the difference will *decrease* ACE. This eventually will occur, since ACE depreciation represents a "timing difference." We will demonstrate this later with an example.

Example: XYZ has three assets, two of which are MACRS property, subject to the AMT Adjustment, and a third property, which is being depreciated under Income Forecasting. All three assets were placed in service before 1994. The following depreciation has already been computed:

	Asset A	**Asset B**	**Asset C**	**Total**
Depreciation for regular tax purposes	$6	$8	$9	$23
Depreciation for AMT purposes	5	6	9*	$20
AMT Adjustment Amount	$1	$2	N/A	$ 3
Total Depreciation for ACE purposes	$3	$4	$9*	$16

Determine the ACE Depreciation Adjustment.

Result: Using the above worksheet:

	Depreciation for Regular Tax Purposes		$23
	AMT Adjustment Amount	$3	
	plus		
less	AMT Tax Preference Amount	0	
	Subtotal = AMT Adjustment and Tax Preferences		(3)
equals	Total Depreciation Expense Recomputed for AMT**		$20
less	Total Depreciation Expense Recomputed for ACE		(16)
	ACE Depreciation Adjustment		$ 4

* Notice that both the AMT and ACE depreciation amounts include the regular tax depreciation on Asset C, which was *not* affected by any AMT or ACE adjustments.

** Alternatively, you could have started with this line, completing it by the filling in the $20 amount computed above.

Example: Assume the same example as above, but reverse the depreciation amounts for regular tax and AMT purposes:

	Asset A	**Asset B**	**Asset C**	**Total**
Depreciation for regular tax purposes	$5	$6	$9	$20
Depreciation for AMT purposes	6	8	9	$23
AMT Adjustment Amount	($1)	($2)	N/A	($ 3)
Total Depreciation for ACE purposes	$3	$4	$9	$16

Determine the ACE Depreciation Adjustment.

Result: Again, using our worksheet:

	Depreciation for Regular Tax Purposes		$20
	AMT Adjustment Amount	($3)	
	plus		
less	AMT Tax Preference Amount	0	
	Subtotal = AMT Adjustment and Tax Preferences* * We are subtracting a negative amount.		((3))
equals	Total Depreciation Expense Recomputed for AMT**		$23

less	Total Depreciation Expense Recomputed for ACE	(16)
	ACE Depreciation Adjustment	$ 7

To Which Property Does the ACE Adjustment Apply?

The 75% ACE Adjustment applies to *all* property, since it is applied to the excess of Adjusted Current Earnings over Pre-Adjustment AMTI, both of which include an amount of depreciation expense for every asset that is currently being depreciated.

The question, therefore, is on which property do we need to *recalculate* depreciation by a different method in order to determine the ACE Depreciation Adjustment? The answer is that depreciation for the ACE Adjustment is *recalculated* only on ACRS and pre-1994 MACRS property.

Therefore, for ACE purposes, depreciation does *not* need to be recalculated on:

- Property placed in service after December 31, 1993.
- Nonrecovery property (this includes pre-1981 property and any property not subject to either MACRS or ACRS because of the anti-churning rules).
- Property that the business elected to depreciate over a method that is not based on a life in years, such as a Production or Use Method.
- Films, videotapes, and sound recordings.
- Certain public utility property, unless a normalization method of accounting is used.

In addition to the above, depreciation does not need to be recalculated for ACE purposes on any property if a corporation becomes exempt from AMT due to the Taxpayer Relief Act of 1997 (even if it later loses its exemption).

Note: For purposes of this chapter we will refer to the above-mentioned property as "All Other Property," which, as explained earlier, is included in the 75% ACE Adjustment but is *not* recalculated for ACE.

Property, or any portion thereof, that was expensed under Section 179 is excluded from the ACE depreciation recalculation.

The easiest way to understand ACE depreciation is to divide all MACRS and ACRS depreciable property into three categories, based on the year in which it was placed in service:

1. **Post-1989, Pre-1994 MACRS Property**
2. **Pre-1990 MACRS Property**
3. **Pre-1990 ACRS Property**

Note: In the above categories, you will notice that the key date is 1990. The reason for this is that the ACE Adjustment was created for tax years beginning in 1990 and later.

Because each of these three categories receives a different treatment for computing ACE depreciation, each will be described individually on the following pages. We recommend that you look at each category separately. At the end of this chapter, we will put the separate components together, into one worksheet, to come up with the ACE Depreciation Adjustment.

Basis of Property Being Depreciated for ACE Purposes

Unlike the adjustments for AMT depreciation described in the previous chapter, when computing depreciation for ACE purposes, the basis of the asset sometimes needs to be adjusted. One of the reasons, in fact, for dividing the property into the three categories mentioned above is to keep straight the different treatment given for determining the depreciable basis of property in each category for the ACE computation.

For some assets, there is no special basis adjustment for the ACE calculation, and the same basis as for regular tax purposes is used. However, for other assets, the basis used to compute ACE depreciation may be either the original basis (usually cost) or the AMT basis, either of which is then reduced by the total depreciation claimed on the asset through the close of the last tax year beginning before 1990. (Notice, again, that the key date is 1990.) As you read through the descriptions of the various categories, we will explain what basis must be used for each.

Post-1989, Pre-1994 MACRS Property

MACRS property that is placed in service in tax years beginning after 1989 but before 1994 is depreciated for ACE purposes under the MACRS Alternative Depreciation System (ADS). The property's basis for ACE is the same as that used for regular tax purposes. No special adjustment to basis is required, since no depreciation is claimed on such property before 1990.

Since both of the following classes of property, placed in service after 1989 but before 1994, are depreciated, for both ACE and AMT purposes, using the ADS method and the same basis, the *ACE and AMT depreciation will be the same for*:

- MACRS real property in either the 27.5-, 31.5-, or 39-year class, and
- MACRS personal property that, for regular tax purposes, is depreciated using straight-line depreciation (either over its General Depreciation System—GDS—life or its ADS life).

Example: In 1992, XYZ, a calendar-year business, placed in service an asset costing $1,200, which it is depreciating using 200% declining-balance. The half-year convention applies. For regular tax purposes, it has a 5-year recovery period. For ADS, it has a 6-year recovery period.

Result: XYZ computes depreciation as follows:

For Regular Tax Purposes:*

$$\frac{\$1{,}200}{5} \times 2 \times \frac{6}{12} = \$240$$

For AMT Purposes:*

$$\frac{\$1{,}200}{6} \times 1.5 \times \frac{6}{12} = \$150$$

* When making these calculations, we could have used the percentage from the tables given in the back of this guide, instead of manually making the computation as we have done here.

For ACE Purposes:

$$\frac{\$1{,}200}{6} \times \frac{6}{12} = \$100$$

Therefore, to calculate the ACE Depreciation Adjustment in this example:

	Total Depreciation Expense Recomputed for AMT	$150
less	Total Depreciation Expense Recomputed for ACE	(100)
	ACE Depreciation Adjustment	$50

*Or, if using our worksheet:***

	Depreciation for Regular Tax Purposes	$240
less	AMT Adjustment Amount ($240 – $150)	(90)
	Total Depreciation Expense Recomputed for AMT	$150
less	Total Depreciation Expense Recomputed for ACE	(100)
	ACE Depreciation Adjustment	$ 50

** At this point, the reader might wonder about whether it is really necessary to use the steps in the worksheet. However, remember that in this example we are depreciating only *one* asset and, therefore, it is very over-simplified! The danger of the above shortcut is forgetting to include an asset that required no AMT depreciation adjustment.

Continuing with the same example, a complete summary of the depreciation for this asset is as follows:

Year	Regular	AMT	AMT Adjustment	ACE	ACE Adjustment
1992	$240	$150	$ 90	$100	$ 50
1993	384	262	122	200	62
1994	231	197	34	200	(3)

Year	Regular	AMT	AMT Adjustment	ACE	ACE Adjustment
1995	138	169	(31)	200	(31)
1996	138	169	(31)	200	(31)
1997	69	169	(100)	200	(31)
1998	–	84	(84)	100	(16)
Total	$1,200	$1,200	0	$1,200	0

The above example demonstrates several points:

- The AMT Adjustment is the difference between the depreciation calculated for regular tax purposes and the depreciation calculated for AMT purposes.
- The ACE Depreciation Adjustment is the difference between the depreciation calculated for AMT purposes and the depreciation calculated for ACE purposes.
- Both AMT and ACE depreciation are simply "timing differences," in that the same amount of depreciation (i.e., $1,200) is eventually taken under all three methods of depreciation: regular tax, AMT, and ACE.
- Since both the AMT Adjustment and the ACE Depreciation Adjustment allow for positive or negative amounts, by the end of the asset's recovery period, both have "zeroed out." In other words, by the end of the asset's recovery period, the positive adjustments have equally offset the negative adjustments.
- In this example, since the asset was being depreciated for regular tax purposes by the most accelerated method available (i.e., 200% declining-balance), there *is* a difference between AMT depreciation (150% declining-balance) and ACE depreciation (straight-line), even though both are using the asset's ADS life.

Pre-1990 MACRS Property

MACRS property that is placed in service in tax years beginning *before* 1990 is depreciated for ACE purposes under the MACRS Alternative Depreciation System (ADS) using:

- the basis of the property for AMT purposes as of the close of the last tax year beginning *before 1990*, and
- over the remaining ADS recovery period as of the close of the last tax year beginning *before 1990*.

How To:

To compute ACE depreciation on assets included in this category, it is best to use the following steps:

1. Determine the asset's depreciable basis for calculating ACE depreciation (i.e., the AMT adjusted basis):

	Original Basis of Property When First Placed in Service
less	(Total Depreciation Recalculated on Property for AMT Purposes as of the close of the last tax year beginning before 1990*)
equals	Basis of Property on Which To Calculate ACE Depreciation

* For a calendar-year business, this is the total AMT depreciation claimed through December 31, 1989.

2. Determine the asset's remaining ADS life:

- It *begins* on the first day of the first tax year beginning after 1989.
- It *ends* on the last day of the recovery period that would have applied had the property been depreciated using the ADS method since it was first placed in service and applying the same averaging convention as originally used.

3. To compute the ACE depreciation, the following formula is used:

$$\frac{\textit{AMT Adjusted Basis (Step 1)}}{\textit{Remaining ADS Life (Step 2)}}$$

Example: On January 1, 1988, XYZ, a calendar-year business, placed in service an asset costing $1,200, which it is depreciating using 200% declining-balance. The half-year convention applies. For regular tax purposes, it has a 5-year recovery period. For ADS, it has a 6-year recovery period.

Result: To compute depreciation for ACE purposes, we will follow the steps described above:

1. Determine the asset's AMT adjusted basis:

	Original basis of asset	$1,200
less	AMT Depreciation through 1989 ($150 in 1988 + $262 in 1989)	(412)
	Basis of Property on Which To Calculate ACE Depreciation	$788

2. Determine the asset's remaining ADS life:

- It begins on January 1, 1990, the first day of the first tax year beginning after 1989.
- It ends on June 30, 1994. The asset has a 6-year ADS life and the half-year convention applies. Therefore, as of 12/31/89, 1.5 years of the asset's ADS recov-

ery period had expired, leaving another 4.5 years (6 years less 1.5 years) remaining.

3. Compute the ACE depreciation:

$$\frac{\textit{\$788 (asset's basis as computed for AMT)}}{\textit{4.5 years (remaining ADS life)}} = \textit{\$175}$$

Therefore, since this is straight-line depreciation, XYZ will expense $175 of depreciation for ACE each year for 4 years and $88 in the final half-year. A complete summary of the depreciation for this asset is as follows:

Year	Regular	AMT	AMT Adjustment	ACE	ACE Adjustment
1988	$240	$150	$ 90	N/A*	N/A
1989	384	262	122	N/A*	N/A
1990	231	197	34	175	22
1991	138	169	(31)	175	(6)
1992	138	169	(31)	175	(6)
1993	69	169	(100)	175	(6)
1994	–	84	(84)	88	(4)
Total	$1,200	$1,200	0	$788**	0

* There is no ACE Depreciation Adjustment in either 1988 or 1989, as it was not effective until 1990.

** The $788 was the asset's AMT adjusted basis determined above in Step 1.

Pre-1990 ACRS Property

ACRS property is depreciated for ACE purposes under the MACRS Alternative Depreciation System (ADS) using:

- the regular tax basis computed as of the close of the last tax year beginning *before 1990*, and
- over the remaining ADS recovery period as of the close of the last tax year beginning *before 1990*.

Note: Even though this category is for *ACRS* property, notice that the depreciation method used for ACE purposes is the *MACRS* ADS method, *not* the ACRS Alternate Straight-Line method.

How To:

To compute ACE depreciation on assets included in this category:

1. Determine the asset's depreciable basis for calculating ACE depreciation (i.e., the regular tax basis):

	Original Basis of Property When First Placed in Service
less	(Total Depreciation Calculated on Property for Regular Tax Purposes as of the close of the last tax year beginning *before 1990*)
equals	Basis of Property on Which To Calculate ACE Depreciation

2. Determine the asset's remaining ADS life:

- It *begins* on the first day of the first tax year beginning after 1989.
- It *ends* on the last day of the recovery period that would have applied had the property been depreciated using the ADS method since it was first placed in service and applying the averaging convention that would have been used under MACRS, except that the midquarter convention is not used (IRS Code Reg. **1.56(g)-1(b)(3)(ii)(C)**).

3. To compute the ACE depreciation, the following formula is used:

$$\frac{\textit{Regular Tax Adjusted Basis (Step 1)}}{\textit{Remaining ADS Life (Step 2)}}$$

Note: Since depreciation for ACE purposes is computed over the remaining ADS recovery period, this means that some ACRS property that may be fully depreciated for regular tax purposes is still being depreciated for ACE purposes! (In order for this to apply, the property cannot be fully depreciated for regular tax purposes *prior to* 1/1/90.)

The next two examples will demonstrate how the remaining ADS life affects ACRS property:

Example: Assume that XYZ, a calendar-year business, placed in service on December 31, 1985, ACRS personal property with an ACRS recovery period of 5 years and a MACRS ADS life of 9.5 years.

Result: Since ACRS has built into its percentage tables the half year convention, *as of December 31, 1989,* 5 recovery years will have expired and *the property is fully depreciated.* The property now has a basis of zero. Therefore, even though the full ADS life of the asset has not yet expired, there is no ACE depreciation computed.

Example: Assume the same facts as in the preceding example, except that the property was placed in service on December 31, *1986*, or 1 year later.

Result: Unlike the previous example, as of December 31, 1989, the property is *not* fully depreciated, having been depreciated for only 4 of its 5 recovery years. Since under MACRS the property would have used the half-year convention (remember that the midquarter convention is *not* an option for ACE purposes), as of December 31, 1989, 3.5 years of its ADS life will have expired. Therefore, of its 9.5 ADS life, 6 years (9.5 years less 3.5 years) of depreciation for ACE purposes remain.

The next example demonstrates how to calculate depreciation for ACE purposes:

Example: On January 1, 1986, XYZ, a calendar-year business, placed in service an asset costing $1,000, which it is depreciating using the regular ACRS method of 150% declining-balance. For regular tax purposes, it had 5-year recovery period. For ADS, it has a 9.5-year recovery period.

Result: To compute depreciation for ACE purposes:

1. Determine the asset's regular tax adjusted basis:

	Original basis of asset	$1,000
less	Regular Tax Depreciation through 1989 ($150 in 1986, $220 in 1987, $210 in 1988 and 1989)	(790)
	Basis of Property on Which To Calculate ACE Depreciation	$210

2. Determine the asset's remaining ADS life:
   - It begins on January 1, 1990, the first day of the first tax year beginning after 1989.
   - It ends on December 31, 1995. The asset has a 9.5-year ADS life and the half-year convention applies. Therefore, as of 12/31/89, 3.5 years of the asset's ADS recovery period has expired, leaving another 6 years (9.5 years less 3.5 years) remaining.
3. Compute the ACE depreciation:

$$\frac{\textit{\$210 (asset's basis as computed for regular tax purposes)}}{\textit{6 years (remaining ADS life)}} = \textit{\$35}$$

Therefore, XYZ will expense $35 of depreciation each year for 6 years. A complete summary of the depreciation for this asset is as follows:

Year	Regular	AMT	AMT Adjustment	ACE	ACE Adjustment
1986	$150	$150	N/A	N/A	N/A
1987	220	220	–	N/A	N/A
1988	210	210	–	N/A	N/A
1989	210	210	–	N/A	N/A
1990	210	210	–	35	175

Year	Regular	AMT	AMT Adjustme nt	ACE	ACE Adjustme nt
1991	–	–	–	35	(35)
1992	–	–	–	35	(35)
1993	–	–	–	35	(35)
1994	–	–	–	35	(35)
1994	–	–	–	35	(35)
Total	$1,000	$1,000	0	$210	0

The above example demonstrates several points:

- We are assuming that this is not leased personal property and that XYZ is not a Personal Holding Company. Therefore, AMT depreciation equals regular tax depreciation.
- Since AMT depreciation is the same as regular tax depreciation, there is no Tax Preference adjustment for AMT. (Remember that since this is ACRS property, if an AMT adjustment had been required, it would have been an AMT Tax Preference, not an Adjustment.)
- There is no ACE Depreciation Adjustment until 1990.
- The XYZ Adjusted Current Earnings is increased in 1990 and decreased in later years.

Miscellaneous ACE Rules Pertaining to Depreciation

The other issues that you need to be aware of are:

1. *Basis of Property.* Just as the other AMT Adjustments create a different basis for AMT purposes, so too does the ACE Depreciation Adjustment. Therefore, if during the tax year, a business disposes of property for which it has made an ACE adjustment, then it must recompute the property's adjusted basis for ACE purposes and recalculate the property's gain or loss. (For an example of the required computation, see "Miscellaneous AMT Rules Pertaining to Depreciation," page IV-139.)
2. *Luxury Automobile Rules.* The luxury automobile rules of IRS Code Sect. **280F** for listed property, which limit the amount of allowable depreciation, apply to ACE depreciation, the same as they do for regular and AMT depreciation purposes.
3. *Uniform Capitalization Rules.* Depreciation that is capitalized under the uniform capitalization rules of IRS Code Sec. **263A** must be recalculated using the above rules for ACE purposes.
4. *Separate Set of Records.* A separate set of records to record ACE depreciation must be kept *even if the corporation is not in an AMT situation in a given year*. It is still

necessary to compute ACE depreciation in order to keep track of both the corporation's Adjusted Current Earnings and the property's basis for ACE purposes.

5. Although property placed in service after December 31, 1993, has no depreciation adjustment for ACE, the depreciation adjustment for such property for the Alternative Minimum Tax still applies.

ACE Summary

The ACE Adjustment for depreciation on property placed in service before 1994 is best summarized in chart form:

Property Type	Year Property Placed in Service	Basis of Property To Be Used for ACE Depreciation	ACE Depreciatio n Method	ACE Recovery Period
MACRS	Post-1989, Pre-1994	Original Basis	Straight-Line	ADS Recovery Period
MACRS	Pre-1990	AMT Adjusted Basis[1]	Straight-Line	Remaining ADS Recovery Period[2]
ACRS	Pre-1990	Regular Tax Adjusted Basis[1]	Straight-Line	Remaining ADS Recovery Period[2]
All Other Property	ACE Depreciation Will Be the Same as for Regular Tax Purposes			

1 Adjusted basis as of the close of the last tax year beginning before 1990.

2 Remaining ADS recovery period as of the close of the last tax year beginning before 1990.

In addition to the above, remember that depreciation does not need to be recalculated for ACE purposes on any property if a corporation becomes exempt from AMT due to the Taxpayer Relief Act of 1997 (even if it later loses its exemption).

ACE Depreciation Worksheet

Total Depreciation Expense Recomputed for AMT
(see the worksheet on page IV-147) ____________

Depreciation Expense Recomputed for ACE Purposes:

Post-1989, Pre-1994 MACRS Property: ____________

$$\frac{\textit{Original Basis}}{\textit{ADS Recovery Period}}$$

plus

Pre-1900 MACRS Property: ____________

$$\frac{\textit{AMT Adjusted Basis*}}{\textit{Remaining ADS Recovery Period*}}$$

less *plus*

Pre-1990 ACRS Property: ____________

$$\frac{\textit{Regular Tax Adjusted Basis*}}{\textit{Remaining ADS Recovery Period*}}$$

plus

All Other Property: ____________

Use same depreciation method as for
Regular Tax Purposes

Subtotal = Total Depreciation Expense Recomputed for ACE ( )

ACE Depreciation Adjustment** ____________

* As of the close of the last tax year beginning before 1990.

** The ACE Depreciation Adjustment may be either a positive or negative amount!

Section IV: Chapter 9: Depreciation and IRS Tax Form 4562

In this section:

IRS Form 4562, Depreciation and Amortization, is used by all types of entities and has several purposes:

- To claim a deduction for depreciation and amortization expense.
- To elect Section 179 expense.
- To provide detailed information on the use of vehicles.
- To provide general information on listed property other than vehicles.

Whether or not a business that is claiming depreciation* must file Form 4562 depends first on the type of entity it is. A regular C corporation (i.e., any corporation other than an S corporation) must file Form 4562 with its federal tax return every year that it is claiming any depreciation. Other types of businesses (partnerships, S corporations, etc.) only need to file Form 4562 if they have depreciation expense for property placed in service in the current year, any Section 179 amount (including any Section 179 carryover amount being expensed in the current year), or are depreciating any listed property. In other words, a business that is claiming depreciation expense does not have to file Form 4562 if it is not operating as a C corporation, has no listed property, is not claiming any Section 179 expense, and does not place any depreciable property in service in the current year.

Note: *For the purpose of this discussion, the term *depreciation* will include regular depreciation, amortization, and Section 179 expense.

Although IRS requires detailed information on current-year depreciation, it does not require any detail on depreciable assets that were placed in service in earlier years. However, all such information (depreciable basis, depreciation method, recovery period, etc.) must be kept in your permanent records.

Form 4562 consists of six parts; each is designed to capture specific information. Before we discuss each part in detail below, see the Form 4562, Depreciation and Amortization page on the IRS web site to view (or download) the latest version of the form. All line references refer to the 2015 version but should apply to most other years since significant changes are rare.

Part I: Section 179 Election

Completion of Part 1 of Form 4562 for new property constitutes an election to claim Section 179 expense. In addition, Part 1 is designed to limit the amount of Section 179 expense by the three principal parameters:

- Dollar limit - The maximum dollar limitation is entered on Line 1.
- Investment limit - The investment limit is entered on Line 3.
- Taxable income limit - The taxable income limitation, if applicable, is entered on Line 11.

Completing Part I

Prepare a listing of property, other than listed property, on which you claimed Section 179 expense this year. Also, look at line 13 of your prior year Form 4562 to see if there is a carryover amount of disallowed Section 179 expense from last year.

Line 1:

Generally, this is $500,000 for the current year. However, if the entity is located in a special zone, this amount is increased by a specified amount described in "Miscellaneous Section 179 Rules," page IV-19.

Line 2:

This is the total cost of qualifying Section 179 property placed in service in the current year. For an enterprise zone, only include 50% of any qualified zone property.

Line 3:

Generally, this is the investment limit of $2,000,000 for the current year. However, if the entity is located in a special zone, this amount is increased by a specified amount described in "Miscellaneous Section 179 Rules," page IV-19.

Lines 4 - 6:

Self-explanatory.

Line 7:

All information on listed property is entered in Part V of Form 4562, page two. If Section 179 expense is claimed on such property, it is entered both in Part V and here on Line 7. If the property is a luxury vehicle, the combined amount of Section 179 and depreciation expense claimed on it cannot exceed the annual limit.

Line 8 and 9:

Self-explanatory.

Line 10:

Enter any carryover of Section 179 expense that was disallowed in previous years. This is the amount on line 13 of your prior year Form 4562.

Line 11:

Enter the smaller of:

- Line 5 (the amount of allowable Section 179 expense after the previous two limitations are applied), or
- The entity's taxable income. Taxable income is calculated without regard to the Section 179 expense deduction or any net operating loss carryforward or carryback.

Line 12:

This is the amount of Section 179 expense allowed for the current year.

Line 13:

This is the unallowable amount of Section 179 expense, which may be carried forward indefinitely.

Part II: Special Depreciation Allowance and Other Depreciation

Part II of Form 4562 is where the 168 first-year depreciation allowance, ACRS, and other depreciation is entered.

Completing Part II

Prepare a listing of all qualified special zone properties for which you are taking the 168 first-year depreciation allowance and all non-MACRS property placed in service in an earlier year that is still being depreciated. Exclude listed property. Although it is important to keep detailed records, no attachment is required for this part of the form.

Line 14:

Enter the special Depreciation Allowance taken on all qualified special zone assets placed in service in the current year.

Line 15:

This is a separate line for property that you elect to depreciate under a method not based in terms of years, such as the units-of-production method. You must attach a statement showing the property's:

- Description
- Depreciation method
- Depreciable basis

Line 16:

This line includes the following:

- ACRS property
- Nonrecovery property
- Property subject to the anti-churning rules. See "Anti-Churning Rules," page IV-66, and "Anti-Churning Rules," page IV-110, for a detailed explanation.
- Videotapes, sound recordings, and motion picture films (income forecasting)
- Intangible property that is not Section 197 property. An example is computer software that is depreciated over 36 months.
- Property depreciated under ADR.

Part III: MACRS Depreciation

Part III of Form 4562 is where property *other than listed property* is entered if it is depreciated under MACRS. For record-keeping purposes, this is the most important section of the form. It identifies all of the essential information for depreciating these assets in future years.

Part III is divided into three sections:

1. Section A: MACRS depreciation for assets placed in service in a prior year, and the election to use general asset accounts.
2. Section B: Property depreciated under the General Depreciation System (GDS).
3. Section C: Property depreciated under the Alternative Depreciation System (ADS).

Completing Part III

Prepare a listing of your MACRS assets, but exclude all listed property. Distinguish between those assets depreciated under the General Depreciation System (GDS) and those depreciated under the Alternative Depreciation System (ADS). Next, group the assets by their recovery-period classification.

Section A

Enter MACRS depreciation for assets placed in service in a prior year.

Check the box on the following line to make the general asset account election. This is sometimes referred to as mass-asset or multiple-asset accounting. Under this system, you can depreciate a large number of similar assets in one account, rather than depreciating each asset individually. This election is irrevocable and applies to the current year and all future years.

Section B

This is where you enter current year acquisitions that are depreciated under MACRS and for which you have not elected the Alternative Depreciation System (ADS). It includes property that you have elected to depreciate using 150% declining-balance, but over their longer ADS recovery periods. Each line represents a property classification* based on the asset's class life, assigned under the Asset Depreciation Range (ADR) System. For a detailed listing of property classifications, see "IRS ADR Class Life Table," page VI-4.

Note: **Notice that the term "classification" is not the same as an asset's class life!* For example, a desk has a 7-year recovery period based on a 10-year ADR class life. A desk belongs on the line for 7-year property. If you elect to depreciate an asset using the 150% declining-balance method over its ADS life, the classification of the asset does not change. Therefore, the line on which it is reported does not change. Whether a desk is depreciated using 200% declining-balance over its GDS life of 7 years or by 150% declining-balance using its ADS life of 10 years, it is entered on the line for 7-year property.

For each classification of property, which is preprinted in Column (a), enter:

- **Column (b)** - Month and year placed in service, but only if it is residential rental or nonresidential real property.
- **Column (c)** - Basis for depreciation: For an explanation of how to compute depreciable basis, see "Basis Used for Depreciation," page I-12. Remember to deduct out any Section 179 expense.
- **Column (d)** - Recovery period: Note that the recovery periods for 25-, 27.5-, and 39-year property are preprinted on the form.
- **Column (e)** - Averaging convention: For personal property enter either "HY" (half-year) or "MQ" (midquarter). For residential rental and nonresidential real property, the averaging convention ("MM" for midmonth) is preprinted on the form.
- **Column (f)** - Depreciation method: This is where you elect to use 150% declining-balance (enter "150 DB") or straight-line (enter "S/L") for personal property. If neither of these elections is made, enter "200 DB" for 200% declining-balance.
- **Column (g)** - Depreciation expense: Enter the amount calculated for the current year.

Section C

The election to use the Alternative Depreciation System (ADS) is made by completing Section C. The instructions to complete this section are the same as for Section B except that for Column (f) the depreciation method is preprinted as "S/L."

Part IV: Summary

Part IV of Form 4562 is a summary of the total depreciation expense. It does not include amortization expense. It does include the depreciation for listed property from the second page of the form and totals it along with the depreciation and Section 179 expense amounts entered in Parts I, II, and III. However, it does *not* include any Section 179 expense if the entity completing the form is either a partnership or S corporation. This is because Section 179 expense for such entities is passed through to the individual partners or shareholders.

This summary section also asks for the amount of any increase in the basis of assets subject to the uniform capitalization rules of IRS Section 263A. Generally, manufacturers are the ones most likely to be affected by this code section.

Part V: Listed Property

Part V pertains to all types of listed property, whether or not it actually has any personal use and whether or not it was placed in service in the current year. For a complete discussion of the definition of listed property, see "Definition of Listed Property," page IV-73. Now that Section 179 expense has been limited to $25,000 for sport utility vehicles purchased after October 22, 2004, SUV detailed information will appear under listed property, even though an SUV is not considered to be listed property.

Part V is divided into three sections:

1. Section A: Lists all listed property and includes depreciation and other important information about each asset.
2. Section B: Requests information on the use of business vehicles.
3. Section C: Contains questions for employers who provide vehicles for use by their employees.

Depreciation deductions for listed property are allowed only for the percentage of the property's basis used for business and investment purposes. There are substantiation requirements for proving such use. For an explanation, see "Record-Keeping Requirements for Listed Property," page IV-96. There are also two types of written policy statements that will satisfy these substantiation requirements. These are described in "Completing Part V," in the explanation for "Section C," page IV-167.

Completing Part V

Prepare a listing of all listed property regardless of the tax year the property was placed in service. Include all relevant information about each property's depreciation. Divide the property into two groups: property used more than 50% in qualified business use and property used 50% or less in qualified business use. For a detailed explanation, see "Qualified Business Use," page IV-75.

Section A

List any automobiles first, followed by all other listed property. If there are more than five vehicles and they are all used 100% for business purposes, you may group them by tax year. If employees reimburse the company for their personal use of a vehicle or the value of the personal use is included in the employees' gross income, the vehicle is treated as being used 100% for business purposes.

Note: Remember that:

- The ceiling limitations for vehicles are the maximum amounts of depreciation *and* Section 179 expense that may be claimed. Also, such limitations must be reduced if the tax year is a short year or if the business use is less than 100%.
- If listed property is not used more than 50% of the time for qualified business use, no Section 179 expense may be claimed and straight-line depreciation must be used.
- If business use of listed property falls to 50% or less in a subsequent year, it may be necessary to recapture depreciation and Section 179 expense. This is done on the IRS Form 4797.

Section B

First answer the questions in Section C, the next section. For each vehicle identified in Section A, information about its mileage and its specific use must be provided here unless:

- Any of the questions in Section C are answered "Yes," or
- A vehicle is only used by employees who are <u>not</u> more than 5% owners.

Section C

If any of the questions in this section are answered "Yes," Section B above does not have to be completed.

If the employer keeps one of the two types of <u>written</u> policy statements described below, the employee who uses a company vehicle does not need to keep a separate set of records and the company will have also satisfied its substantiation requirements as well:

1. <u>A policy statement that prohibits all personal use, including commuting</u>, of the company vehicles by employees and <u>all</u> of the following conditions are met:
    - *The employer owns or leases the vehicle and provides the vehicle to one or more employees for use in the employer's business.
    - The vehicle is kept on the employer's business premises when not in use.
    - No employee who uses the vehicle lives at the employer's place of business.
    - *An employee may only use the vehicle personally if that use is *de minimis* in nature (such as the employee stopping for lunch between two business calls).
    - *The employer reasonably believes that his employees are not using the vehicles for personal use.
    - The employer can provide evidence to support all of the preceding five conditions.
1. <u>A policy statement that prohibits all personal use, except commuting</u>, of the company vehicles by employees and <u>all</u> of the following conditions are met:

- *All of the same preceding three conditions with an asterisk in front of them, except add the words "other than commuting" to the last two.
- The employer requires that the employee commutes to work in the vehicle for legitimate noncompensatory business reasons.
- The employee is not an officer, director, or a 1% or more owner of the employer's business.
- The employer includes the commuting value in the employee's gross income.
- The employer can provide evidence to support all of the preceding six conditions.

As an alternative to the above, an employer can treat all use of a vehicle by an employee as personal use. In other words, the employer can include the value of the availability of the vehicle in the employee's gross income, without any exclusion for a working condition fringe benefit to the employee, and withhold the required taxes. This would constitute sufficient evidence and would satisfy the substantiation requirements for the employer (per IRS Reg. **1.274-6T(c)**). The employee, however, would then have to substantiate any deduction.

Part VI: Amortization

Each year, you may elect to amortize certain qualifying property over a prescribed number of years. The election to amortize any newly acquired property is made by completing Part VI. You only provide detailed information for amortizable property acquired in the current year. IRS does not require detail on amortizable property that was placed in service in earlier years.

For current year property, you must provide the IRS code section under which it is being amortized. Most intangible property is amortized over 15 years, under Code Section 197. For a detailed explanation, see Section II: "Amortization." Other types of amortizable property and their appropriate IRS code sections are:

- Pollution control facilities: Sec. 169
- Certain bond premiums: Sec. 171
- Cost of acquiring a lease: Sec. 178
- Reforestation expenses: Sec. 194
- Start-up expenses: Sec. 195
- Organization costs for a corporation: Sec. 248
- Organization costs for a partnership: Sec. 709

Tips on Completing Form 4562

- If a tax return (generally an individual return) has more than one business activity, prepare a separate Form 4562 for each activity. However, prepare only one Part I when computing the allowable amount of Section 179 expense.
- Since the Form 4562 only shows detail for current year acquisitions, you must maintain detailed records for property depreciated and/or amortized from previous years.
- The Form 4562 must be filed with any C corporation income tax return that is claiming a depreciation expense. However, an S corporation, partnership, or an individual filing a Schedule C (Profit or Loss from Business) only needs to file it if depreciable property is placed in service during the current year or the entity is claiming any depreciation on any listed property. In addition, an individual filing a Schedule C must file the Form 4562 if claiming any Section 179 expense, either from the current year or as a carryover amount from a previous year.
- Rounding off to whole dollars is acceptable to IRS. Eliminate any amount less than fifty cents and increase any amount from fifty cents to ninety-nine cents to the next higher dollar.

Section V: Conclusion

In this section:

We have covered a wide range of depreciation issues in this guide, both from a financial reporting perspective and according to IRS rules. We started with the basic concepts and then went on to specifics. There are two principal goals when calculating depreciation:

- To accurately match depreciation expense with business income.
- To correctly follow both GAAP and IRS rules.

Initially, the myriad of rules surrounding depreciation may have seemed overwhelming. However, as you have learned, if taken one step at a time, depreciation is not difficult.

A key to correctly calculating depreciation is simply remembering to ask yourself all of the necessary questions. Most depreciation errors are either errors of omission or errors caused by not fully understanding one's options. For example:

- *"Do you need to keep an ACE book?"*
- *"Do you start depreciating an asset as soon as you purchase it?"*

The list goes on. Obviously, before you even begin wondering if you know all of the correct answers, you need to be sure you know all of the questions. The "Depreciation Questions," page V-5, is intended as a checklist to insure that nothing is forgotten.

The Fundamentals of Depreciation

By starting with the fundamentals in Section I, you have been able to see that the depreciation rules are built upon certain basic concepts:

- Property type
- Depreciable basis
- Date placed in service
- Property's useful life or recovery period
- Depreciation method

Having read through this guide, it should also be apparent that most depreciation methods are based on either the straight-line method or a declining-balance method. Each method has several variations, some of which are optional, while others are required to be used at certain times.

Depreciation for Financial Versus Tax Reporting Purposes

In distinguishing between depreciation used for financial reporting versus tax reporting, although the same basic fundamentals are used, the intent behind the choice of depreciation method is quite different.

Financial reporting attempts to find which depreciation method, approved by GAAP, most realistically reflects the business's use of the property. Tax reporting, on the other hand, attempts to find which depreciation method, approved by the IRS, will allow the business to pay the least amount of income tax, as late as possible, within the law.

Allowed or Allowable Depreciation

A concept that is unique to depreciation for tax reporting purposes is "allowed or allowable." If an income tax return is filed and accepted by the IRS, the amount of depreciation expensed on that return has been technically "allowed." However, because of any number of reasons, the amount of depreciation claimed may not be correct. In other words, it may not equal the amount "allowable" by the IRS. When this occurs, the amount claimed may be either too much or not enough.

When an incorrect amount of depreciation is claimed on a tax return, there are two possible methods for rectifying this:

- File an amended return if the statute of limitations has not expired.

How To:

An amended tax return may be filed within three years from the date the original return was filed, or two years after the tax was paid, whichever is later. A return that is filed early is considered to have been filed on the due date of the return.

- File a Form 3115, Application for Change in Accounting Method.

What happens if you discover that an incorrect amount of depreciation was claimed, it is too late to file an amended return, you did not file Form 3115, and you are now disposing of the property and need to determine the property's basis to compute the amount of gain or loss? The answer is that the *property's basis must be reduced by the greater of the allowed or allowable depreciation:*

When the allowed amount is greater:	If too much depreciation was claimed, the business must reduce the property's basis by the amount deducted on the tax return, to the extent of any tax benefit received from the excess deduction.
or	
When the allowable amount is greater:	If too little depreciation was claimed, the business must reduce the property's basis by the correct amount of depreciation to which it was entitled, even though no tax benefit was ever derived!

Multiple Depreciation Calculations

As stated earlier, different depreciation methods are used for different types of reporting (i.e., financial vs. tax). In addition, different depreciation methods may be used within any one income tax return.

A C corporation will, in many instances, be required to keep at least four separate sets of depreciation records:

1. Financial statement depreciation.
2. Regular income tax depreciation.
3. AMT depreciation*.
4. ACE depreciation*.

* Beginning in 1998, if a corporation qualifies as a "small business corporation" under the Taxpayer Relief Act of 1997, it does not have to compute either AMT or ACE depreciation. Furthermore, corporation that began business in 1994 or later will not be subject to the ACE Depreciation Adjustment.

In addition to the above, the business may also need to keep a separate set of records for state depreciation. This will occur if you are filing a state income tax return for a state that has its own set of depreciation rules.

TIP
To simplify your record-keeping requirements:

Electing to use the MACRS Alternative Depreciation System (ADS), whenever possible, will eliminate the depreciation adjustment for AMT, as well as eliminating any recalculation of depreciation for the computation of Earnings and Profits. (For assets placed in service prior to 1994, electing ADS also eliminated the depreciation adjustment for ACE.)

Note: You need to be aware, however, that the above is only appropriate when the business does not need to reduce its taxable income to avoid paying more tax, such as when it is in a loss situation.

Section V: Depreciation Questions

Decisions, decisions . . .

The key to correctly calculating depreciation is simply remembering to ask yourself all of the necessary questions. None of the questions are difficult. However, they are *all* important, and missing even one of them may give you an incorrect calculation.

Here are the questions, all very simple. In case you forget any of the terminology or need a "How To" reminder, we have included subtitles and page references so you can quickly turn to the appropriate discussion of what may be involved in the decision-making process and find a quick clarification:

No.	Question	Where to find the answer
1.	Are you the entity that may claim the depreciation on this particular property?	*Who May Claim Depreciation?* (Section I: page I-2)
A.	If you cannot claim depreciation, but you are leasing the property (note that some lessees are entitled to depreciation), is it listed property?	*Leased Listed Property* (Section IV: Chapter 3: page IV-90)
2.	Is the property depreciable?	*What Property May Be Depreciated?* (Section I: page I-2)
3.	What type of property is it? Is it tangible or intangible property? Is it personal or real property?	*Elements of Depreciation, Type of Property* (Section I: page I-10)
A.	Is it amortizable?	Section II: Amortization
B.	Is it listed property?	Section IV: Chapter 4: Passenger Automobiles and Other Listed Property
C.	Is it Low-Income Housing that was placed in service after 1980 but before 1987?	Section IV: Chapter 4: page IV-98
4.	What date was the property first placed in service?	*Elements of Depreciation, The Date Placed in Service* (Section I: page I-11)
5.	What is the property's depreciable basis? (Remember to ask if the property was used for personal purposes.)	*Basis Used for Depreciation* (Section I: page I-12)
6.	Are you depreciating the property for financial statement purposes[1] or for tax reporting purposes?[2] (You may be depreciating the property for both types of reporting.)	[1]Section III: Depreciation for Financial Reporting [2]Section IV: Depreciation for Income Tax Reporting
Questions 7–10 Are For Financial Reporting Purposes:		

No.	Question	Where to find the answer
7.	Does the property have a salvage value?	Section III: page III-1
8.	What is the property's useful life?	Section III: page III-1
9.	What depreciation method will you use?	Section III: page III-1 and *Depreciation Methods for Financial Reporting* (Section III: page III-2) and:
A.	If using the straight-line method:	*Straight-Line Method* (Section III: page III-2)
B.	If using an accelerated method:	*Accelerated Methods* (Section III: page III-2)
C.	If using a production or use method:	*Production or Use Methods* (Section III: page III-6)
D.	If using income forecasting:	*Depreciation Methods, Income Forecasting* (Section IV: Chapter 5: page IV-117)
10.	Was the property in service for less than 12 months during the current tax year?	*Depreciation for Partial Periods* (Section III: page III-9)
	Questions 11–21 Are for Tax Reporting Purposes:	
11.	What date was the property placed in service? (You will, in most cases, need to know the month as well as the year.) Based on the chart in Section IV, page IV-2, you will be able to determine which chapter of this guide will give you a detailed explanation for the type of property you are depreciating.	Section IV: chart on page IV-2
	For MACRS Property Only:	
12.	If the property qualifies, are you expensing the property under the Section 179 expense deduction?	Section IV: Chapter 1: First-Year Expensing
13.	What is the property's recovery period?	*MACRS Recovery Periods* (Section IV: Chapter 2: page IV-42)
14.	What averaging convention must be applied?	*MACRS Averaging Conventions* (Section IV: Chapter 2: page IV-44)
15.	What depreciation methods may you use?	*MACRS Depreciation Methods* (Section IV: Chapter 2: page IV-49)
16.	How is the depreciation method that you have chosen calculated?	Section IV: Chapter 2: Modified Accelerated Cost Recovery System (MACRS)
A.	Can you use the percentage tables?	*Calculating MACRS Depreciation, Percentage Tables* (Section IV: Chapter 2: page IV-51)

No.	Question	Where to find the answer
B.	If you are not using the percentage tables, do you need to understand the manual calculation?	*Calculating MACRS Depreciation, Manual Calculation* (Section IV: Chapter 2: page IV-52)
C.	Are you using the Alternative Depreciation System (ADS)?	*ADS* (Section IV: Chapter 2: page IV-56)
	For All Types of Property:	
17.	Is the current tax year less than 12 months? *If yes:*	
A.	Is it MACRS property?	*Short Tax Years* (Section IV: Chapter 2: page IV-57), and
1.	Was the property placed in service this year?	*Property Placed in Service in a Short Year* (Section IV: Chapter 2: page IV-58)
2.	Was the property placed in service during an earlier year?	*Short Year After the Property Is Placed in Service* (Section IV: Chapter 2: page IV-62)
B.	Is it ACRS property?	*Short Tax Years* (Section IV: Chapter 4: page IV-106)
C.	Is it nonrecovery property (pre-1981)?	*Principles for Calculating Depreciation for Nonrecovery Property, Averaging Conventions* (Section IV: Chapter 5: page IV-121) and *Depreciation for Partial Periods* (Section III: page III-9)
18.	Is the property subject to the anti-churning rules?	*Property Excluded From MACRS, Anti-Churning Rules* (Section IV: Chapter 2: page IV-66)
19.	Was the property disposed of this year while its recovery period has not yet expired? *If yes:*	
A.	Is it MACRS property?	*Early Dispositions* (Section IV: Chapter 2: page IV-63)
B.	Is it ACRS property?	*Early Dispositions* (Section IV: Chapter 4: page IV-108)
C.	Is it nonrecovery property (pre-1981)?	*Principles for Calculating Depreciation for Nonrecovery Property, Averaging Conventions* (Section IV: Chapter 5: page IV-121)
20.	Was there a change in the type of use of the property? *If yes:*	
A.	Is it listed property (either MACRS or ACRS)?	*Depreciation Limitations on Listed Property, Predominant Use Test Failed in Subsequent Tax Year* (Section IV: Chapter 3: page IV-80)

No.	Question	Where to find the answer
B.	Is it ACRS property?	*Changes in How Property Is Used* (Section IV: Chapter 4: page IV-110)
C.	Is it both nonrecovery property (pre-1981) *and* residential rental property that either passes or fails the “80% rental test” in the current year?	*Principles for Calculating Depreciation for Nonrecovery Property, Limitations on Using Accelerated Methods, Residential Rental Property* (Section IV: Chapter 5: page IV-122)
21.	Has the business used *any* form of accelerated depreciation for *any* property?	Section IV: Chapter 7: Depreciation and the Alternative Minimum Tax (AMT), and, if a C corporation with pre-1994 property, Section IV: Chapter 8: Depreciation and Adjusted Current Earnings (ACE)

Section VI: Tables

In this section:

Guide To Using the Tables

We have organized the necessary tables by labeling each with both a letter(s) and number as follows:

1. **T #** — These are the three tables that are based on the ADR Class Life system. See page VI-2.
2. **M #** — These are the 18 **M**ACRS Percentage Tables. See page VI-14.
3. **A #** — These are the 15 **A**CRS Percentage Tables. See page VI-41.
4. **ALP #** — These are the two tables for **A**CRS **L**isted **P**roperty. See page VI-49.
5. **ALL #** — These are the two tables for **A**CRS **L**eased **L**isted Property. See page VI-50.
6. **MLL #** — These are the two tables for **M**ACRS **L**eased **L**isted Property. See page VI-51.

Note: The tables for MACRS Listed Property that is *not* leased are located with the MACRS Percentage Tables described in **2.** above, since such property uses the ADS method.

Tables 1–3

All three of the following tables may be used to determine the proper classification of MACRS property. These tables will simplify the IRS ADR Class Life Table, which is also included here. You should use these tables when determining the MACRS recovery period (i.e., the GDS life) for any depreciable property newly acquired, as well as for determining either the class life or the ADS life of MACRS property. Remember that the ADS life is also used for Alternative Minimum Tax (AMT) calculations on MACRS property.

Table 1

This is an alphabetical listing for determining the recovery periods for *commonly used assets*.

Table 2

This table is for determining the recovery periods for property used in a *manufacturing* business. It is alphabetized according to the particular type of manufacturing industry.

You will notice that the first column in this table shows the "asset class number." Once you have located the correct industry, you may need further detail. If that is the case, turn to the IRS ADR Class Life Table, located just behind these tables, and refer to the asset class number, which in the IRS table is found in numerical order.

For correctly classifying *tools* used in the manufacture of a particular type of product, look at **Table 2** under the type of product being manufactured, and then look for "special tools." For example, special tools used in manufacturing rubber products may be found in **Table 2** under the listing: "rubber products–special tools."

Table 3

This table is for determining the recovery periods for property according to the type of *business* in which it is used. The different types of businesses are sorted alphabetically.

As in **Table 2**, we have included the "asset class number" from the IRS ADR Class Life Table. It is a good idea to reference the IRS table as well, since there are various exceptions for specific assets, too numerous to include in our table.

Which table should you use?

- If it is an asset most likely being used in many different types of businesses, use **Table 1**.
- If it is an asset used in a manufacturing business, use **Table 2**.
- If it is an asset fairly unique to a particular type of business, use **Table 3**.

Remember that under MACRS, any personal property without a class is automatically *7-year property* for regular MACRS depreciation, with a *12-year recovery period for ADS.*

Help: Enter “IRS table” on the Index tab of the Sage Fixed Assets Depreciation online Help to review the information in Tables 1-3.

IRS ADR Class Life Table

Table B-1. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
	SPECIFIC DEPRECIABLE ASSETS USED IN ALL BUSINESS ACTIVITIES, EXCEPT AS NOTED:			
00.11	**Office Furniture, Fixtures, and Equipment:** Includes furniture and fixtures that are not a structural component of a building. Includes such assets as desks, files, safes, and communications equipment. Does not include communications equipment that is included in other classes.	10	7	10
00.12	**Information Systems:** Includes computers and their peripheral equipment used in administering normal business transactions and the maintenance of business records, their retrieval and analysis. Information systems are defined as: 1) Computers: A computer is a programmable electronically activated device capable of accepting information, applying prescribed processes to the information, and supplying the results of these processes with or without human intervention. It usually consists of a central processing unit containing extensive storage, logic, arithmetic, and control capabilities. Excluded from this category are adding machines, electronic desk calculators, etc., and other equipment described in class 00.13. 2) Peripheral equipment consists of the auxiliary machines which are designed to be placed under control of the central processing unit. Nonlimiting examples are: Card readers, card punches, magnetic tape feeds, high speed printers, optical character readers, tape cassettes, mass storage units, paper tape equipment, keypunches, data entry devices, teleprinters, terminals, tape drives, disc drives, disc files, disc packs, visual image projector tubes, card sorters, plotters, and collators. Peripheral equipment may be used on-line or off-line. Does not incude equipment that is an integral part of other capital equipment that is included in other classes of economic activity, i.e., computers used primarily for process or production control, switching, channeling, and automating distributive trades and services such as point of sale (POS) computer systems. Also, does not include equipment of a kind used primarily for amusement or entertainment of the user.	6	5	5
00.13	**Data Handling Equipment; except Computers:** Includes only typewriters, calculators, adding and accounting machines, copiers, and duplicating equipment.	6	5	6
00.21	**Airplanes (airframes and engines), except those used in commercial or contract carrying of passengers or freight, and all helicopters (airframes and engines)**	6	5	6
00.22	**Automobiles, Taxis**	3	5	5
00.23	**Buses**	9	5	9
00.241	**Light General Purpose Trucks:** Includes trucks for use over the road (actual weight less than 13,000 pounds)	4	5	5
00.242	**Heavy General Purpose Trucks:** Includes heavy general purpose trucks, concrete ready mix-trucks, and ore trucks, for use over the road (actual unloaded weight 13,000 pounds or more)	6	5	6
00.25	**Railroad Cars and Locomotives, except those owned by railroad transportation companies**	15	7	15
00.26	**Tractor Units for Use Over-The-Road**	4	3	4
00.27	**Trailers and Trailer-Mounted Containers**	6	5	6
00.28	**Vessels, Barges, Tugs, and Similar Water Transportation Equipment, except those used in marine construction**	18	10	18
00.3	**Land Improvements:** Includes improvements directly to or added to land, whether such improvements are section 1245 property or section 1250 property, provided such improvements are depreciable. Examples of such assets might include sidewalks, roads, canals, waterways, drainage facilities, sewers (not including municipal sewers in Class 51), wharves and docks, bridges, fences, landscaping shrubbery, or radio and television transmitting towers. Does not include land improvements that are explicitly included in any other class, and buildings and structural components as defined in section 1.48-1(e) of the regulations. Excludes public utility initial clearing and grading land improvements as specified in Rev. Rul. 72-403, 1972-2 C.B. 102.	20	15	20
00.4	**Industrial Steam and Electric Generation and/or Distribution Systems:** Includes assets, whether such assets are section 1245 property or 1250 property, providing such assets are depreciable, used in the production and/or distribution of electricity with rated total capacity in excess of 500 Kilowatts and/or assets used in the production and/or distribution of steam with rated total capacity in excess of 12,500 pounds per hour for use by the taxpayer in its industrial manufacturing process or plant activity and not ordinarily available for sale to others. Does not include buildings and structural components as defined in section 1.48-1(e) of the regulations. Assets used to generate and/or distribute electricity or steam of the type described above, but of lesser rated capacity, are not included, but are included in the appropriate manufacturing equipment classes elsewhere specified. Also includes electric generating and steam distribution assets, which may utilize steam produced by a waste reduction and resource recovery plant, used by the taxpayer in its industrial manufacturing process or plant activity. Steam and chemical recovery boiler systems used for the recovery and regeneration of chemicals used in manufacturing, with rated capacity in excess of that described above, with specifically related distribution and return systems are not included but are included in appropriate manufacturing equipment classes elsewhere specified. An example of an excluded steam and chemical recovery boiler system is that used in the pulp and paper manufacturing equipment classes elsewhere specified. An example of an excluded steam and chemical recovery boiler system is that used in the pulp and paper manufacturing industry.	22	15	22

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
	DEPRECIABLE ASSETS USED IN THE FOLLOWING ACTIVITIES:			
01.1	**Agriculture:** Includes machinery and equipment, grain bins, and fences but no other land improvements, that are used in the production of crops or plants, vines, and trees; livestock; the operation of farm dairies, nurseries, greenhouses, sod farms, mushroom cellars, cranberry bogs, apiaries, and fur farms; the performance of agriculture, animal husbandry, and horticultural services.	10	7	10
01.11	**Cotton Ginning Assets**	12	7	12
01.21	**Cattle, Breeding or Dairy**	7	5	7
01.221	**Any breeding or work horse that is 12 years old or less at the time it is placed in service****	10	7	10
01.222	**Any breeding or work horse that is more than 12 years old at the time it is placed in service****	10	3	10
01.223	**Any race horse that is more than 2 years old at the time it is placed in service****	*	3	12
01.224	**Any horse that is more than 12 years old at the time it is placed in service and that is neither a race horse nor a horse described in class 01.222****	*	3	12
01.225	**Any horse not described in classes 01.221, 01.222, 01.223, or 01.224**	*	7	12
01.23	**Hogs, Breeding**	3	3	3
01.24	**Sheep and Goats, Breeding**	5	5	5
01.3	**Farm buildings except structures included in Class 01.4**	25	20	25
01.4	**Single purpose agricultural or horticultural structures (within the meaning of section 168(i)(13) of the Code)**	15	10***	15
10.0	**Mining:** Includes assets used in the mining and quarrying of metallic and nonmetallic minerals (including sand, gravel, stone, and clay) and the milling, beneficiation and other primary preparation of such materials.	10	7	10
13.0	**Offshore Drilling:** Includes assets used in offshore drilling for oil and gas such as floating, self-propelled and other drilling vessels, barges, platforms, and drilling equipment and support vessels such as tenders, barges, towboats and crewboats. Excludes oil and gas production assets.	7.5	5	7.5
13.1	**Drilling of Oil and Gas Wells:** Includes assets used in the drilling of onshore oil and gas wells and the provision of geophysical and other exploration services; and the provision of such oil and gas field services as chemical treatment, plugging and abandoning of wells and cementing or perforating well casings. Does not include assets used in the performance of any of these activities and services by integrated petroleum and natural gas producers for their own account.	6	5	6
13.2	**Exploration for and Production of Petroleum and Natural Gas Deposits:** Includes assets used by petroleum and natural gas producers for drilling of wells and production of petroleum and natural gas, including gathering pipelines and related storage facilities. Also includes petroleum and natural gas offshore transportation facilities used by producers and others consisting of platforms (other than drilling platforms classified in Class 13.0), compression or pumping equipment, and gathering and transmission lines to the first onshore transshipment facility. The assets used in the first onshore transshipment facility are also included and consist of separation equipment (used for separation of natural gas, liquids, and in Class 49.23), and liquid holding or storage facilities (other than those classified in Class 49.25). Does not include support vessels.	14	7	14
13.3	**Petroleum Refining:** Includes assets used for the distillation, fractionation, and catalytic cracking of crude petroleum into gasoline and its other components.	16	10	16
15.0	**Construction:** Includes assets used in construction by general building, special trade, heavy and marine construction contractors, operative and investment builders, real estate subdividers and developers, and others except railroads.	6	5	6
20.1	**Manufacture of Grain and Grain Mill Products:** Includes assets used in the production of flours, cereals, livestock feeds, and other grain and grain mill products.	17	10	17
20.2	**Manufacture of Sugar and Sugar Products:** Includes assets used in the production of raw sugar, syrup, or finished sugar from sugar cane or sugar beets.	18	10	18
20.3	**Manufacture of Vegetable Oils and Vegetable Oil Products:** Includes assets used in the production of oil from vegetable materials and the manufacture of related vegetable oil products.	18	10	18
20.4	**Manufacture of Other Food and Kindred Products:** Includes assets used in the production of foods and beverages not included in classes 20.1, 20.2 and 20.3.	12	7	12
20.5	**Manufacture of Food and Beverages—Special Handling Devices:** Includes assets defined as specialized materials handling devices such as returnable pallets, palletized containers, and fish processing equipment including boxes, baskets, carts, and flaking trays used in activities as defined in classes 20.1, 20.2, 20.3 and 20.4. Does not include general purpose small tools such as wrenches and drills, both hand and power-driven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices.	4	3	4

* Property described in asset classes 01.223, 01.224, and 01.225 are assigned recovery periods but have no class lives.
** A horse is more than 2 (or 12) years old after the day that is 24 (or 144) months after its actual birthdate.
*** 7 if property was placed in service before 1989.

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
21.0	**Manufacture of Tobacco and Tobacco Products:** Includes assets used in the production of cigarettes, cigars, smoking and chewing tobacco, snuff, and other tobacco products.	15	7	15
22.1	**Manufacture of Knitted Goods:** Includes assets used in the production of knitted and netted fabrics and lace. Assets used in yarn preparation, bleaching, dyeing, printing, and other similar finishing processes, texturing, and packaging, are elsewhere classified.	7.5	5	7.5
22.2	**Manufacture of Yarn, Thread, and Woven Fabric:** Includes assets used in the production of spun yarns including the preparing, blending, spinning, and twisting of fibers into yarns and threads, the preparation of yarns such as twisting, warping, and winding, the production of covered elastic yarn and thread, cordage, woven fabric, tire fabric, braided fabric, twisted jute for packaging, mattresses, pads, sheets, and industrial belts, and the processing of textile mill waste to recover fibers, flocks, and shoddies. Assets used to manufacture carpets, man-made fibers, and nonwovens, and assets used in texturing, bleaching, dyeing, printing, and other similar finishing processes, are elsewhere classified.	11	7	11
22.3	**Manufacture of Carpets and Dyeing, Finishing, and Packaging of Textile Products and Manufacture of Medical and Dental Supplies:** Includes assets used in the production of carpets, rugs, mats, woven carpet backing, chenille, and other tufted products, and assets used in the joining together of backing with carpet yarn or fabric. Includes assets used in washing, scouring, bleaching, dyeing, printing, drying, and similar finishing processes applied to textile fabrics, yarns, threads, and other textile goods. Includes assets used in the production and packaging of textile products, other than apparel, by creasing, forming, trimming, cutting, and sewing, such as the preparation of carpet and fabric samples, or similar joining together processes (other than the production of scrim reinforced paper products and laminated paper products) such as the sewing and folding of hosiery and panty hose, and the creasing, folding, trimming, and cutting of fabrics to produce nonwoven products, such as disposable diapers and sanitary products. Also includes assets used in the production of medical and dental supplies other than drugs and medicines. Assets used in the manufacture of nonwoven carpet backing, and hard surface floor covering such as tile, rubber, and cork, are elsewhere classified.	9	5	9
22.4	**Manufacture of Textile Yarns:** Includes assets used in the processing of yarns to impart bulk and/or stretch properties to the yarn. The principal machines involved are falsetwist, draw, beam-to-beam, and stuffer box texturing equipment and related highspeed twisters and winders. Assets, as described above, which are used to further process man-made fibers are elsewhere classified when located in the same plant in an integrated operation with man-made fiber producing assets. Assets used to manufacture man-made fibers and assets used in bleaching, dyeing, printing, and other similar finishing processes, are elsewhere classified.	8	5	8
22.5	**Manufacture of Nonwoven Fabrics:** Includes assets used in the production of nonwoven fabrics, felt goods including felt hats, padding, batting, wadding, oakum, and fillings, from new materials and from textile mill waste. Nonwoven fabrics are defined as fabrics (other than reinforced and laminated composites consisting of nonwovens and other products) manufactured by bonding natural and/or synthetic fibers and/or filaments by means of induced mechanical interlocking, fluid entanglement, chemical adhesion, thermal or solvent reaction, or by combination thereof other than natural hydration bonding as ocurs with natural cellulose fibers. Such means include resin bonding, web bonding, and melt bonding. Specifically includes assets used to make flocked and needle punched products other than carpets and rugs. Assets, as described above, which are used to manufacture nonwovens are elsewhere classified when located in the same plant in an integrated operation with man-made fiber producing assets. Assets used to manufacture man-made fibers and assets used in bleaching, dyeing, printing, and other similar finishing processes, are elsewhere classified.	10	7	10
23.0	**Manufacture of Apparel and Other Finished Products:** Includes assets used in the production of clothing and fabricated textile products by the cutting and sewing of woven fabrics, other textile products, and furs; but does not include assets used in the manufacture of apparel from rubber and leather.	9	5	9
24.1	**Cutting of Timber:** Includes logging machinery and equipment and roadbuilding equipment used by logging and sawmill operators and pulp manufacturers for their own account.	6	5	6
24.2	**Sawing of Dimensional Stock from Logs:** Includes machinery and equipment installed in permanent or well established sawmills.	10	7	10
24.3	**Sawing of Dimensional Stock from Logs:** Includes machinery and equipment in sawmills characterized by temporary foundations and a lack, or minimum amount, of lumberhandling, drying, and residue disposal equipment and facilities.	6	5	6
24.4	**Manufacture of Wood Products, and Furniture:** Includes assets used in the production of plywood, hardboard, flooring, veneers, furniture, and other wood products, including the treatment of poles and timber.	10	7	10
26.1	**Manufacture of Pulp and Paper:** Includes assets for pulp materials handling and storage, pulp mill processing, bleach processing, paper and paperboard manufacturing, and on-line finishing. Includes pollution control assets and all land improvements associated with the factory site or production process such as effluent ponds and canals, provided such improvements are depreciable but does not include buildings and structural components as defined in section 1.48-1(e)(1) of the regulations. Includes steam and chemical recovery boiler systems, with any rated capacity, used for the recovery and regeneration of chemicals used in manufacturing. Does not include assets used either in pulpwood logging, or in the manufacture of hardboard.	13	7	13

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
26.2	**Manufacture of Converted Paper, Paperboard, and Pulp Products:** Includes assets used for modification, or remanufacture of paper and pulp into converted products, such as paper coated off the paper machine, paper bags, paper boxes, cartons and envelopes. Does not include assets used for manufacture of nonwovens that are elsewhere classified.	10	7	10
27.0	**Printing, Publishing, and Allied Industries:** Includes assets used in printing by one or more processes, such as letter-press, lithography, gravure, or screen; the performance of services for the printing trade, such as bookbinding, typesetting, engraving, photo-engraving, and electrotyping; and the publication of newspapers, books, and periodicals.	11	7	11
28.0	**Manufacture of Chemicals and Allied Products:** Includes assets used to manufacture basic organic and inorganic chemicals; chemical products to be used in further manufacture, such as synthetic fibers and plastics materials; and finished chemical products. Includes assets used to further process man-made fibers, to manufacture plastic film, and to manufacture nonwoven fabrics, when such assets are located in the same plant in an integrated operation with chemical products producing assets. Also includes assets used to manufacture photographic supplies, such as film, photographic paper, sensitized photographic paper, and developing chemicals. Includes all land improvements associated with plant site or production processes, such as effluent ponds and canals, provided such land improvements are depreciable but does not include buildings and structural components as defined in section 1.48-1(e) of the regulations. Does not include assets used in the manufacture of finished rubber and plastic products or in the production of natural gas products, butane, propane, and by-products of natural gas production plants.	9.5	5	9.5
30.1	**Manufacture of Rubber Products:** Includes assets used for the production of products from natural, synthetic, or reclaimed rubber, gutta percha, balata, or gutta siak, such as tires, tubes, rubber footwear, mechanical rubber goods, heels and soles, flooring, and rubber sundries; and in the recapping, retreading, and rebuilding of tires.	14	7	14
30.11	**Manufacture of Rubber Products—Special Tools and Devices:** Includes assets defined as special tools, such as jigs, dies, mandrels, molds, lasts, patterns, specialty containers, pallets, shells; and tire molds, and accessory parts such as rings and insert plates used in activities as defined in class 30.1. Does not include tire building drums and accessory parts and general purpose small tools such as wrenches and drills, both power and hand-driven, and other general purpose equipment such as conveyors and transfer equipment.	4	3	4
30.2	**Manufacture of Finished Plastic Products:** Includes assets used in the manufacture of plastics products and the molding of primary plastics for the trade. Does not include assets used in the manufacture of basic plastics materials nor the manufacture of phonograph records.	11	7	11
30.21	**Manufacture of Finished Plastic Products—Special Tools:** Includes assets defined as special tools, such as jigs, dies, fixtures, molds, patterns, gauges, and specialty transfer and shipping devices, used in activities as defined in class 30.2. Special tools are specifically designed for the production or processing of particular parts and have no significant utilitarian value and cannot be adapted to further or different use after changes or improvements are made in the model design of the particular part produced by the special tools. Does not include general purpose small tools such as wrenches and drills, both hand and power-driven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices.	3.5	3	3.5
31.0	**Manufacture of Leather and Leather Products:** Includes assets used in the tanning, currying, and finishing of hides and skins; the processing of fur pelts; and the manufacture of finished leather products, such as footwear, belting, apparel, and luggage.	11	7	11
32.1	**Manufacture of Glass Products:** Includes assets used in the production of flat, blown, or pressed products of glass, such as float and window glass, glass containers, glassware and fiberglass. Does not include assets used in the manufacture of lenses.	14	7	14
32.11	**Manufacture of Glass Products—Special Tools:** Includes assets defined as special tools such as molds, patterns, pallets, and specialty transfer and shipping devices such as steel racks to transport automotive glass, used in activities as defined in class 32.1. Special tools are specifically designed for the production or processing of particular parts and have no significant utilitarian value and cannot be adapted to further or different use after changes or improvements are made in the model design of the particular part produced by the special tools. Does not include general purpose small tools such as wrenches and drills, both hand and power-driven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices.	2.5	3	2.5
32.2	**Manufacture of Cement:** Includes assets used in the production of cement, but does not include assets used in the manufacture of concrete and concrete products nor in any mining or extraction process.	20	15	20
32.3	**Manufacture of Other Stone and Clay Products:** Includes assets used in the manufacture of products from materials in the form of clay and stone, such as brick, tile, and pipe; pottery and related products, such as vitreous-china, plumbing fixtures, earthenware and ceramic insulating materials; and also includes assets used in manufacture of concrete and concrete products. Does not include assets used in any mining or extraction processes.	15	7	15

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
33.2	**Manufacture of Primary Nonferrous Metals:** Includes assets used in the smelting, refining, and electrolysis of nonferrous metals from ore, pig, or scrap, the rolling, drawing, and alloying of nonferrous metals; the manufacture of castings, forgings, and other basic products of nonferrous metals; and the manufacture of nails, spikes, structural shapes, tubing, wire, and cable.	14	7	14
33.21	**Manufacture of Primary Nonferrous Metals—Special Tools:** Includes assets defined as special tools such as dies, jigs, molds, patterns, fixtures, gauges, and drawings concerning such special tools used in the activities as defined in class 33.2, Manufacture of Primary Nonferrous Metals. Special tools are specifically designed for the production or processing of particular products or parts and have no significant utilitarian value and cannot be adapted to further or different use after changes or improvements are made in the model design of the particular part produced by the special tools. Does not include general purpose small tools such as wrenches and drills, both hand and power-driven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices. Rolls, mandrels and refractories are not included in class 33.21 but are included in class 33.2.	6.5	5	6.5
33.3	**Manufacture of Foundry Products:** Includes assets used in the casting of iron and steel, including related operations such as molding and coremaking. Also includes assets used in the finishing of castings and patternmaking when performed at the foundry, all special tools and related land improvements.	14	7	14
33.4	**Manufacture of Primary Steel Mill Products:** Includes assets used in the smelting, reduction, and refining of iron and steel from ore, pig, or scrap; the rolling, drawing and alloying of steel; the manufacture of nails, spikes, structural shapes, tubing, wire, and cable. Includes assets used by steel service centers, ferrous metal forges, and assets used in coke production, regardless of ownership. Also includes related land improvements and all special tools used in the above activities.	15	7	15
34.0	**Manufacture of Fabricated Metal Products:** Includes assets used in the production of metal cans, tinware, fabricated structural metal products, metal stampings, and other ferrous and nonferrous metal and wire products not elsewhere classified. Does not include assets used to manufacture non-electric heating apparatus.	12	7	12
34.01	**Manufacture of Fabricated Metal Products—Special Tools:** Includes assets defined as special tools such as dies, jigs, molds, patterns, fixtures, gauges, and returnable containers and drawings concerning such special tools used in the activities as defined in class 34.0. Special tools are specifically designed for the production or processing of particular machine components, products, or parts, and have no significant utilitarian value and cannot be adapted to further or different use after changes or improvements are made in the model design of the particular part produced by the special tools. Does not include general small tools such as wrenches and drills, both hand and power-driven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices.	3	3	3
35.0	**Manufacture of Electrical and Non-Electrical Machinery and Other Mechanical Products:** Includes assets used to manufacture or rebuild finished machinery and equipment and replacement parts thereof such as machine tools, general industrial and special industry machinery, electrical power generation, transmission, and distribution systems, space heating, cooling, and refrigeration systems, commercial and home appliances, farm and garden machinery, construction machinery, mining and oil field machinery, internal combustion engines (except those elsewhere classified), turbines (except those that power airborne vehicles), batteries, lamps and lighting fixtures, carbon and graphite products, and electromechanical and mechanical products including business machines, instruments, watches and clocks, vending and amusement machines, photographic equipment, medical and dental equipment and appliances, and ophthalmic goods. Includes assets used by manufacturers or rebuilders of such finished machinery and equipment in activities elsewhere classified such as the manufacture of castings, forgings, rubber and plastic products, electronic subassemblies or other manufacturing activities if the interim products are used by the same manufacturer primarily in the manufacture, assembly, or rebuilding of such finished machinery and equipment. Does not include assets used in mining, assets used in the manufacture of primary ferrous and nonferrous metals, assets included in class 00.11 through 00.4 and assets elsewhere classified.	10	7	10
36.0	**Manufacture of Electronic Components, Products, and Systems:** Includes assets used in the manufacture of electronic communication, computation, instrumentation and control system, including airborne applications; also includes assets used in the manufacture of electronic products such as frequency and amplitude modulated transmitters and receivers, electronic switching stations, television cameras, video recorders, record players and tape recorders, computers and computer peripheral machines, and electronic instruments, watches, and clocks; also includes assets used in the manufacture of components, provided their primary use is products and systems defined above such as electron tubes, capacitors, coils, resistors, printed circuit substrates, switches, harness cables, lasers, fiber optic devices, and magnetic media devices. Specifically excludes assets used to manufacture electronic products and components, photocopiers, typewriters, postage meters and other electromechanical and mechanical business machines and instruments that are elsewhere classified. Does not include semiconductor manufacturing equipment included in class 36.1.	6	5	6
36.1	**Any Semiconductor Manufacturing Equipment**	5	5	5

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
37.11	**Manufacture of Motor Vehicles:** Includes assets used in the manufacture and assembly of finished automobiles, trucks, trailers, motor homes, and buses. Does not include assets used in mining, printing and publishing, production of primary metals, electricity, or steam, or the manufacture of glass, industrial chemicals, batteries, or rubber products, which are classified elsewhere. Includes assets used in manufacturing activities elsewhere classified other than those excluded above, where such activities are incidental to and an integral part of the manufacture and assembly of finished motor vehicles such as the manufacture of parts and subassemblies of fabricated metal products, electrical equipment, textiles, plastics, leather, and foundry and forging operations. Does not include any assets not classified in manufacturing activity classes, e.g., does not include any assets classified in asset guideline classes 00.11 through 00.4. Activities will be considered incidental to the manufacture and assembly of finished motor vehicles only if 75 percent or more of the value of the products produced under one roof are used for the manufacture and assembly of finished motor vehicles. Parts that are produced as a normal replacement stock complement in connection with the manufacture and assembly of finished motor vehicles are considered used for the manufacture assembly of finished motor vehicles. Does not include assets used in the manufacture of component parts if these assets are used by taxpayers not engaged in the assembly of finished motor vehicles.	12	7	12
37.12	**Manufacture of Motor Vehicles—Special Tools:** Includes assets defined as special tools, such as jigs, dies, fixtures, molds, patterns, gauges, and specialty transfer and shipping devices, owned by manufacturers of finished motor vehicles and used in qualified activities as defined in class 37.11. Special tools are specifically designed for the production or processing of particular motor vehicle components and have no significant utilitarian value, and cannot be adapted to further or different use, after changes or improvements are made in the model design of the particular part produced by the special tools. Does not include general purpose small tools such as wrenches and drills, both hand and powerdriven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices.	3	3	3
37.2	**Manufacture of Aerospace Products:** Includes assets used in the manufacture and assembly of airborne vehicles and their component parts including hydraulic, pneumatic, electrical, and mechanical systems. Does not include assets used in the production of electronic airborne detection, guidance, control, radiation, computation, test, navigation, and communication equipment or the components thereof.	10	7	10
37.31	**Ship and Boat Building Machinery and Equipment:** Includes assets used in the manufacture and repair of ships, boats, caissons, marine drilling rigs, and special fabrications not included in asset classes 37.32 and 37.33. Specifically includes all manufacturing and repairing machinery and equipment, including machinery and equipment used in the operation of assets included in asset class 37.32. Excludes buildings and their structural components.	12	7	12
37.32	**Ship and Boat Building Dry Docks and Land Improvements:** Includes assets used in the manufacture and repair of ships, boats, caissons, marine drilling rigs, and special fabrications not included in asset classes 37.31 and 37.33. Specifically includes floating and fixed dry docks, ship basins, graving docks, shipways, piers, and all other land improvements such as water, sewer, and electric systems. Excludes buildings and their structural components.	16	10	16
37.33	**Ship and Boat Building—Special Tools:** Includes assets defined as special tools such as dies, jigs, molds, patterns, fixtures, gauges, and drawings concerning such special tools used in the activities defined in classes 37.31 and 37.32. Special tools are specifically designed for the production or processing of particular machine components, products, or parts, and have no significant utilitarian value and cannot be adapted to further or different use after changes or improvements are made in the model design of the particular part produced by the special tools. Does not include general purpose small tools such as wrenches and drills, both hand and power-driven, and other general purpose equipment such as conveyors, transfer equipment, and materials handling devices.	6.5	5	6.5
37.41	**Manufacture of Locomotives:** Includes assets used in building or rebuilding railroad locomotives (including mining and industrial locomotives). Does not include assets of railroad transportation companies or assets of companies which manufacture components of locomotives but do not manufacture finished locomotives.	11.5	7	11.5
37.42	**Manufacture of Railroad Cars:** Includes assets used in building or rebuilding railroad freight or passenger cars (including rail transit cars). Does not include assets of railroad transportation companies or assets of companies which manufacture components of railroad cars but do not manufacture finished railroad cars.	12	7	12
39.0	**Manufacture of Athletic, Jewelry, and Other Goods:** Includes assets used in the production of jewelry; musical instruments; toys and sporting goods; motion picture and television films and tapes; and pens, pencils, office and art supplies, brooms, brushes, caskets, etc. **Railroad Transportation:** Classes with the prefix 40 include the assets identified below that are used in the commercial and contract carrying of passengers and freight by rail. Assets of electrified railroads will be classified in a manner corresponding to that set forth below for railroads not independently operated as electric lines. Excludes the assets included in classes with the prefix beginning 00.1 and 00.2 above, and also excludes any non-depreciable assets included in Interstate Commerce Commission accounts enumerated for this class.	12	7	12

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
40.1	**Railroad Machinery and Equipment:** Includes assets classified in the following Interstate Commerce Commission accounts: **Roadway accounts:** (16) Station and office buildings (freight handling machinery and equipment only) (25) TOFC/COFC terminals (freight handling machinery and equipment only) (26) Communication systems (27) Signals and interlockers (37) Roadway machines (44) Shop machinery **Equipment accounts:** (52) Locomotives (53) Freight train cars (54) Passenger train cars (57) Work equipment	14	7	14
40.2	**Railroad Structures and Similar Improvements:** Includes assets classified in the following Interstate Commerce Commission road accounts: (6) Bridges, trestles, and culverts (7) Elevated structures (13) Fences, snowsheds, and signs (16) Station and office buildings (stations and other operating structures only) (17) Roadway buildings (18) Water stations (19) Fuel stations (20) Shops and enginehouses (25) TOFC/COFC terminals (operating structures only) (31) Power transmission systems (35) Miscellaneous structures (39) Public improvements construction	30	20	30
40.3	**Railroad Wharves and Docks:** Includes assets classified in the following Interstate Commission Commerce accounts: (23) Wharves and docks (24) Coal and ore wharves	20	15	20
40.4	**Railroad Track**	10	7	10
40.51	**Railroad Hydraulic Electric Generating Equipment**	50	20	50
40.52	**Railroad Nuclear Electric Generating Equipment**	20	15	20
40.53	**Railroad Steam Electric Generating Equipment**	28	20	28
40.54	**Railroad Steam, Compressed Air, and Other Power Plan Equipment**	28	20	28
41.0	**Motor Transport—Passengers:** Includes assets used in the urban and interurban commercial and contract carrying of passengers by road, except the transportation assets included in classes with the prefix 00.2.	8	5	8
42.0	**Motor Transport—Freight:** Includes assets used in the commercial and contract carrying of freight by road, except the transportation assets included in classes with the prefix 00.2.	8	5	8
44.0	**Water Transportation:** Includes assets used in the commercial and contract carrying of freight and passengers by water except the transportation assets included in classes with the prefix 00.2. Includes all related land improvements.	20	15	20
45.0	**Air Transport:** Includes assets (except helicopters) used in commercial and contract carrying of passengers and freight by air. For purposes of section 1.167(a)-11(d)(2)(iv)(a) of the regulations, expenditures for "repair, maintenance, rehabilitation, or improvement," shall consist of direct maintenance expenses (irrespective of airworthiness provisions or charges) as defined by Civil Aeronautics Board uniform accounts 5200, maintenance burden (exclusive of expenses pertaining to maintenance buildings and improvements) as defined by Civil Aeronautics Board accounts 5300, and expenditures which are not "excluded additions" as defined in section 1.167(a)-11(d)(2)(vi) of the regulations and which would be charged to property and equipment accounts in the Civil Aeronautics Board uniform system of accounts.	12	7	12
45.1	**Air Transport (restricted):** Includes each asset described in the description of class 45.0 which was held by the taxpayer on April 15, 1976, or is acquired by the taxpayer pursuant to a contract which was, on April 15, 1976, and at all times thereafter, binding on the taxpayer. This criterion of classification based on binding contract concept is to be applied in the same manner as under the general rules expressed in section 49(b)(1), (4), (5) and (8) of the Code (as in effect prior to its repeal by the Revenue Act of 1978, section 312(c)(1), (d), 1978-3 C.B. 1, 60).	6	5	6
46.0	**Pipeline Transportation:** Includes assets used in the private, commercial, and contract carrying of petroleum, gas and other products by means of pipes and conveyors. The trunk lines and related storage facilities of integrated petroleum and natural gas producers are included in this class. Excludes initial clearing and grading land improvements as specified in Rev. Rul. 72-403, 1972-2; C.B. 102, but includes all other related land improvements.	22	15	22

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
	Telephone Communications: Includes the assets classified below and that are used in the provision of commercial and contract telephonic services such as:			
48.11	**Telephone Central Office Buildings:** Includes assets intended to house central office equipment, as defined in Federal Communications Commission Part 31 Account No. 212 whether section 1245 or section 1250 property.	45	20	45
48.12	**Telephone Central Office Equipment:** Includes central office switching and related equipment as defined in Federal Communications Commission Part 31 Account No. 221. Does not include computer-based telephone central office switching equipment included in class 48.121. Does not include private branch exchange (PBX) equipment.	18	10	18
48.121	**Computer-based Telephone Central Office Switching Equipment:** Includes equipment whose functions are those of a computer or peripheral equipment (as defined in section 168(i)(2)(B) of the Code) used in its capacity as telephone central office equipment. Does not include private exchange (PBX) equipment.	9.5	5	9.5
48.13	**Telephone Station Equipment:** Includes such station apparatus and connections as teletypewriters, telephones, booths, private exchanges, and comparable equipment as defined in Federal Communications Commission Part 31 Account Nos. 231, 232, and 234.	10	7*	10*
48.14	**Telephone Distribution Plant:** Includes such assets as pole lines, cable, aerial wire, underground conduits, and comparable equipment, and related land improvements as defined in Federal Communications Commission Part 31 Account Nos. 241, 242.1, 242.2, 242.3, 242.4, 243, and 244.	24	15	24
48.2	**Radio and Television Broadcastings:** Includes assets used in radio and television broadcasting, except transmitting towers. **Telegraph, Ocean Cable, and Satellite Communications (TOCSC)** includes communications-related assets used to provide domestic and international radio-telegraph, wire-telegraph, ocean-cable, and satellite communications services; also includes related land improvements. If property described in Classes 48.31–48.45 is comparable to telephone distribution plant described in Class 48.14 and used for 2-way exchange of voice and data communication which is the equivalent of telephone communication, such property is assigned a class life of 24 years under this revenue procedure. Comparable equipment does not include cable television equipment used primarily for 1-way communication.	6	5	6
48.31	**TOCSC—Electric Power Generating and Distribution Systems:** Includes assets used in the provision of electric power by generation, modulation, rectification, channelization, control, and distribution. Does not include these assets when they are installed on customers premises.	19	10	19
48.32	**TOCSC—High Frequency Radio and Microwave Systems:** Includes assets such as transmitters and receivers, antenna supporting structures, antennas, transmission lines from equipment to antenna, transmitter cooling systems, and control and amplification equipment. Does not include cable and long-line systems.	13	7	13
48.33	**TOCSC—Cable and Long-line Systems:** Includes assets such as transmission lines, pole lines, ocean cables, buried cable and conduit, repeaters, repeater stations, and other related assets. Does not include high frequency radio or microwave systems.	26.5	20	26.5
48.34	**TOCSC—Central Office Control Equipment:** Includes assets for general control, switching, and monitoring of communications signals including electromechanical switching and channeling apparatus, multiplexing equipment patching and monitoring facilities, in-house cabling, teleprinter equipment, and associated site improvements.	16.5	10	16.5
48.35	**TOCSC—Computerized Switching, Channeling, and Associated Control Equipment:** Includes central office switching computers, interfacing computers, other associated specialized control equipment, and site improvements.	10.5	7	10.5
48.36	**TOCSC—Satellite Ground Segment Property:** Includes assets such as fixed earth station equipment, antennas, satellite communications equipment, and interface equipment used in satellite communications. Does not include general purpose equipment or equipment used in satellite space segment property.	10	7	10
48.37	**TOCSC—Satellite Space Segment Property:** Includes satellites and equipment used for telemetry, tracking, control, and monitoring when used in satellite communications.	8	5	8
48.38	**TOCSC—Equipment Installed on Customer's Premises:** Includes assets installed on customer's premises, such as computers, terminal equipment, power generation and distribution systems, private switching center, teleprinters, facsimile equipment and other associated and related equipment.	10	7	10
48.39	**TOCSC—Support and Service Equipment:** Includes assets used to support but not engage in communications. Includes store, warehouse and shop tools, and test and laboratory assets. **Cable Television (CATV):** Includes communications-related assets used to provide cable television community antenna television services. Does not include assets used to provide subscribers with two-way communications services.	13.5	7	13.5

* Property described in asset guideline class 48.13 which is qualified technological equipment as defined in section 168(i)(2) is assigned a 5-year recovery period.

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
48.41	**CATV—Headend:** Includes assets such as towers, antennas, preamplifiers, converters, modulation equipment, and program non-duplication systems. Does not include headend buildings and program origination assets.	11	7	11
48.42	**CATV—Subscriber Connection and Distribution Systems:** Includes assets such as trunk and feeder cable, connecting hardware, amplifiers, power equipment, passive devices, directional taps, pedestals, pressure taps, drop cables, matching transformers, multiple set connector equipment, and convertors.	10	7	10
48.43	**CATV—Program Origination:** Includes assets such as cameras, film chains, video tape recorders, lighting, and remote location equipment excluding vehicles. Does not include buildings and their structural components.	9	5	9
48.44	**CATV—Service and Test:** Includes assets such as oscilloscopes, field strength meters, spectrum analyzers, and cable testing equipment, but does not include vehicles.	8.5	5	8.5
48.45	**CATV—Microwave Systems:** Inlcudes assets such as towers, antennas, transmitting and receiving equipment, and broad band microwave assets is used in the provision of cable television services. Does not include assets used in the provision of common carrier services.	9.5	5	9.5
49.11	**Electric, Gas, Water and Steam, Utility Services:** Includes assets used in the production, transmission and distribution of electricity, gas, steam, or water for sale including related land improvements. **Electric Utility Hydraulic Production Plant:** Includes assets used in the hydraulic power production of electricity for sale, including related land improvements, such as dams, flumes, canals, and waterways.	50	20	50
49.12	**Electric Utility Nuclear Production Plant:** Includes assets used in the nuclear power production and electricity for sale and related land improvements. Does not include nuclear fuel assemblies.	20	15	20
49.121	**Electric Utility Nuclear Fuel Assemblies:** Includes initial core and replacement core nuclear fuel assemblies (i.e., the composite of fabricated nuclear fuel and container) when used in a boiling water, pressurized water, or high temperature gas reactor used in the production of electricity. Does not include nuclear fuel assemblies used in breader reactors.	5	5	5
49.13	**Electric Utility Steam Production Plant:** Includes assets used in the steam power production of electricity for sale, combusion turbines operated in a combined cycle with a conventional steam unit and related land improvements. Also includes package boilers, electric generators and related assets such as electricity and steam distribution systems as used by a waste reduction and resource recovery plant if the steam or electricity is normally for sale to others.	28	20	28
49.14	**Electric Utility Transmission and Distribution Plant:** Includes assets used in the transmission and distribution of electricity for sale and related land improvements. Excludes initial clearing and grading land improvements as specified in Rev. Rul. 72-403, 1972-2 C.B. 102.	30	20	30
49.15	**Electric Utility Combustion Turbine Production Plant:** Includes assets used in the production of electricity for sale by the use of such prime movers as jet engines, combustion turbines, diesel engines, gasoline engines, and other internal combustion engines, their associated power turbines and/or generators, and related land improvements. Does not include combustion turbines operated in a combined cycle with a conventional steam unit.	20	15	20
49.21	**Gas Utility Distribution Facilities:** Includes gas water heaters and gas conversion equipment installed by utility on customers' premises on a rental basis.	35	20	35
49.221	**Gas Utility Manufactured Gas Production Plants:** Includes assets used in the manufacture of gas having chemical and/or physical properties which do not permit complete interchangeability with domestic natural gas. Does not include gas-producing systems and related systems used in waste reduction and resource recovery plants which are elsewhere classified.	30	20	30
49.222	**Gas Utility Substitute Natural Gas (SNG) Production Plant (naphtha or lighter hydrocarbon feedstocks):** Includes assets used in the catalytic conversion of feedstocks or naphtha or lighter hydrocarbons to a gaseous fuel which is completely interchangeable with domestic natural gas.	14	7	14
49.223	**Substitute Natural Gas—Coal Gasification:** Includes assets used in the manufacture and production of pipeline quality gas from coal using the basic Lurgi process with advanced methanation. Includes all process plant equipment and structures used in this coal gasification process and all utility assets such as cooling systems, water supply and treatment facilities, and assets used in the production and distribution of electricity and steam for use by the taxpayer in a gasification plant and attendant coal mining site processes but not for assets used in the production and distribution of electricity and steam for sale to others. Also includes all other related land improvements. Does not include assets used in the direct mining and treatment of coal prior to the gasification process itself.	18	10	18
49.23	**Natural Gas Production Plant**	14	7	14
49.24	**Gas Utility Trunk Pipelines and Related Storage Facilities:** Excluding initial clearing and grading land improvements as specified in Rev. Rul. 72-40.	22	15	22
49.25	**Liquefied Natural Gas Plant:** Includes assets used in the liquefaction, storage, and regasification of natural gas including loading and unloading connections, instrumentation equipment and controls, pumps, vaporizers and odorizers, tanks, and related land improvements. Also includes pipeline interconnections with gas transmission lines and distribution systems and marine terminal facilities.	22	15	22

Publication 946

Table B-2. **Table of Class Lives and Recovery Periods**

Asset class	Description of assets included	Class Life (in years)	Recovery Periods (in years) GDS (MACRS)	ADS
49.3	**Water Utilities:** Includes assets used in the gathering, treatment, and commercial distribution of water.	50	20***	50
49.4	**Central Steam Utility Production and Distribution:** Includes assets used in the production and distribution of steam for sale. Does not include assets used in waste reduction and resource recovery plants which are elsewhere classified.	28	20	28
49.5	**Waste Reduction and Resource Recovery Plants:** Includes assets used in the conversion of refuse or other solid waste or biomass to heat or to a solid, liquid, or gaseous fuel. Also includes all process plant equipment and structures at the site used to receive, handle, collect, and process refuse or other solid waste or biomass in a waterwall, combustion system, oil or gas pyrolysis system, or refuse derived fuel system to create hot water, gas, steam and electricity. Includes material recovery and support assets used in refuse or solid refuse or solid waste receiving, collecting, handling, sorting, shredding, classifying, and separation systems. Does not include any package boilers, or electric generators and related assets such as electricity, hot water, steam and manufactured gas production plants classified in classes 00.4, 49.13, 49.221, and 49.4. Does include, however, all other utilities such as water supply and treatment facilities, ash handling and other related land improvements of a waste reduction and resource recovery plant.	10	7	10
50.	**Municipal Wastewater Treatment Plant**	24	15	24
51.	**Municipal Sewer**	50	20***	50
57.0	**Distributive Trades and Services:** Includes assets used in wholesale and retail trade, and personal and professional services. Includes section 1245 assets used in marketing petroleum and petroleum products.	9	5	9*
57.1	**Distributive Trades and Services—Billboard, Service Station Buildings and Petroleum Marketing Land Improvements:** Includes section 1250 assets, including service station buildings and depreciable land improvements, whether section 1245 property or section 1250 property, used in the marketing of petroleum and petroleum products, but not including any of these facilities related to petroleum and natural gas trunk pipelines. Includes car wash buildings and related land improvements. Includes billboards, whether such assets are section 1245 property or section 1250 property. Excludes all other land improvements, buildings and structural components as defined in section 1.48-1(e) of the regulations. See *Gas station convenience stores* in chapter 3.	20	15	20
79.0	**Recreation:** Includes assets used in the provision of entertainment services on payment of a fee or admission charge, as in the operation of bowling alleys, billiard and pool establishments, theaters, concert halls, and miniature golf courses. Does not include amusement and theme parks and assets which consist primarily of specialized land improvements or structures, such as golf courses, sports stadia, race tracks, ski slopes, and buildings which house the assets used in entertainment services.	10	7	10
80.0	**Theme and Amusement Parks:** Includes assets used in the provision of rides, attractions, and amusements in activities defined as theme and amusement parks, and includes appurtenances associated with a ride, attraction, amusement or theme setting within the park such as ticket booths, facades, shop interiors, and props, special purpose structures, and buildings other than warehouses, administration buildings, hotels, and motels. Includes all land improvements for or in support of park activities (e.g., parking lots, sidewalks, waterways, bridges, fences, landscaping, etc.), and support functions (e.g., food and beverage retailing, souvenir vending and other nonlodging accommodations) if owned by the park and provided exclusively for the benefit of park patrons. Theme and amusement parks are defined as combinations of amusements, rides, and attractions which are permanently situated on park land and open to the public for the price of admission. This guideline class is a composite of all assets used in this industry except transportation equipment (general purpose trucks, cars, airplanes, etc., which are included in asset guideline classes with the prefix 00.2), assets used in the provision of administrative services (asset classes with the prefix 00.1) and warehouses, administration buildings, hotels and motels.	12.5	7	12.5
	Certain Property for Which Recovery Periods Assigned			
	A. Personal Property With No Class Life		7	12
	Section 1245 Real Property With No Class Life		7	40
	B. Qualified Technological Equipment, as defined in section 168(i)(2).	**	5	5
	C. Property Used in Connection with Research and Experimentation referred to in section 168(e)(3)(B).	**	5	class life if no class life—12
	D. Alternative energy property described in sections 48(l)(3)(A)(ix) (as in effect on the day before the date of enactment (11/5/90) of the Revenue Reconciliation Act of 1990).	**	5	class life if no class life—12
	E. Biomass property described in section 48(l)(15) (as in effect on the day before the date of enactment (11/5/90) of the Revenue Reconciliation Act of 1990) and is a qualifying small production facility within the meaning of section 3(17)(c) of the Federal Power Act (16 U.S.C. 796(17)(C)), as in effect on September 1, 1986.	**	5	class life if no class life—12
	F. Energy property described in section 48(a)(3)(A) (or would be described if "solar or wind energy" were substituted for "solar energy" in section 48(a)(3)(A)(i)).	**	5	class life if no class life—12

* Any high technology medical equipment as defined in section 168(i)(2)(C) which is described in asset guideline class 57.0 is assigned a 5-year recovery period for the alternate MACRS method.

** The class life (if any) of property described in classes B, C, D, E, or F is determined by reference to the asset guideline classes. If an item of property described in paragraphs B, C, D, E, or F is not described in any asset guideline class, such item of property has no class life.

*** Use straight line over 25 years if placed in service after June 12, 1996, unless placed in service under a binding contract in effect before June 10, 1996, and at all times until placed in service.

Publication 946

MACRS Percentage Tables

MACRS 3-, 5-, 7-, 10-, 15-, 20-Year Property Using GDS* Life 200%/150% Declining-Balance		
Convention	**Table**	**Page**
Half-Year	M 1	page VI-17
Midquarter 1st Quarter**	M 2	page VI-17
Midquarter 2nd Quarter**	M 3	page VI-18
Midquarter 3rd Quarter**	M 4	page VI-18
Midquarter 4th Quarter**	M 5	page VI-19

* General Depreciation System.

** Denotes which quarter the property was first placed in service.

Note: This table may not be used for 3-, 5-, 7-, or 10-year property that is farm property placed in service after 1988, since such property cannot be depreciated under the double-declining method. Such property may be depreciated using any other method. All other tables are, therefore, applicable. The Tax Cuts and Jobs Act Rule requiring use of the 150-percent-declining balance method on property used in a farming business has been eliminated as of 12/31/2017. Therefore after 12/31/2017, these tables can be used for property used in a farming business.

MACRS 3-, 5-, 7-, 10-, 15-, 20-Year Property Using ADS* or GDS** Life 2.5 Years – 50 Years Straight-Line		
Convention	**Table**	**Page**
Half-Year	M 8	page VI-21
Midquarter 1st Quarter***	M 9	page VI-23
Midquarter 2nd Quarter***	M 10	page VI-25
Midquarter 3rd Quarter***	M 11	page VI-27
Midquarter 4th Quarter***	M 12	page VI-29

MACRS 3-, 5-, 7-, 10-, 15-, 20-Year Property Using ADS* or GDS** Life 2.5 Years – 50 Years Straight-Line		
Convention	**Table**	**Page**

* MACRS Alternative Depreciation System.

** General Depreciation System.

*** Denotes which quarter the property was first placed in service.

MACRS Residential and Nonresidential Real Property Using GDS* Life Straight-Line			
Recovery Period	**Convention**	**Table**	**Page**
27.5	Midmonth	M 6	page VI-19
31.5	Midmonth	M 7	page VI-20
39	Midmonth	M 7(a)	page VI-20

* General Depreciation System.

MACRS Residential and Nonresidential Real Property Using ADS* Life Straight-Line			
Recovery Period	**Convention**	**Table**	**Page**
40	Midmonth	M 13	page VI-31

* MACRS Alternative Depreciation System.

MACRS 3-, 5-, 7-, 10-, 15-, 20-Year Property Alternative Minimum Tax 2.5 Years – 50 Years 150% Declining-Balance		
Convention	**Table**	**Page**
Half-Year	M 14	page VI-31
Midquarter 1st Quarter*	M 15	page VI-33
Midquarter 2nd Quarter*	M 16	page VI-35
Midquarter 3rd Quarter*	M 17	page VI-37

MACRS 3-, 5-, 7-, 10-, 15-, 20-Year Property Alternative Minimum Tax 2.5 Years – 50 Years 150% Declining-Balance		
Convention	**Table**	**Page**
Midquarter 4th Quarter*	M 18	page VI-39

* Denotes which quarter the property was first placed in service.

Note: Tables **M 14 – 18** are to be used for any property using 150% declining-balance over the ADS life and for 3-, 5-, 7-, and 10-year farm property using 150% declining-balance over the GDS life before 12/31/2017. The Tax Cuts and Jobs Act Rule requiring use of the 150-percent-declining balance method on property used in a farming business has been eliminated as of 12/31/2017.

Table M 1:
3-, 5-, 7-, 10-, 15-, and 20-Year Property
Half-Year Convention

Year	Depreciation rate for recovery period					
	3-year	5-year	7-year	10-year	15-year	20-year
1	33.33%	20.00%	14.29%	10.00%	5.00%	3.750%
2	44.45	32.00	24.49	18.00	9.50	7.219
3	14.81	19.20	17.49	14.40	8.55	6.677
4	7.41	11.52	12.49	11.52	7.70	6.177
5		11.52	8.93	9.22	6.93	5.713
6		5.76	8.92	7.37	6.23	5.285
7			8.93	6.55	5.90	4.888
8			4.46	6.55	5.90	4.522
9				6.56	5.91	4.462
10				6.55	5.90	4.461
11				3.28	5.91	4.462
12					5.90	4.461
13					5.91	4.462
14					5.90	4.461
15					5.91	4.462
16					2.95	4.461
17						4.462
18						4.461
19						4.462
20						4.461
21						2.231

Table M 2:
3-, 5-, 7-, 10-, 15-, and 20-Year Property
Midquarter Convention
Placed in Service in First Quarter

Year	Depreciation rate for recovery period					
	3-year	5-year	7-year	10-year	15-year	20-year
1	58.33%	35.00%	25.00%	17.50%	8.75%	6.563%
2	27.78	26.00	21.43	16.50	9.13	7.000
3	12.35	15.60	15.31	13.20	8.21	6.482
4	1.54	11.01	10.93	10.56	7.39	5.996
5		11.01	8.75	8.45	6.65	5.546
6		1.38	8.74	6.76	5.99	5.130
7			8.75	6.55	5.90	4.746
8			1.09	6.55	5.91	4.459
9				6.56	5.90	4.459
10				6.55	5.91	4.459
11				0.82	5.90	4.459
12					5.91	4.460
13					5.90	4.459
14					5.91	4.460
15					5.90	4.459
16					0.74	4.460
17						4.459
18						4.460
19						4.459
20						4.460
21						0.557

Table M 3:
3-, 5-, 7-, 10-, 15-, and 20-Year Property
Midquarter Convention
Placed in Service in Second Quarter

Year	Depreciation rate for recovery period					
	3-year	5-year	7-year	10-year	15-year	20-year
1	41.67%	25.00%	17.85%	12.50%	6.25%	4.688%
2	38.89	30.00	23.47	17.50	9.38	7.148
3	14.14	18.00	16.76	14.00	8.44	6.612
4	5.30	11.37	11.97	11.20	7.59	6.116
5		11.37	8.87	8.96	6.83	5.658
6		4.26	8.87	7.17	6.15	5.233
7			8.87	6.55	5.91	4.841
8			3.33	6.55	5.90	4.478
9				6.56	5.91	4.463
10				6.55	5.90	4.463
11				2.46	5.91	4.463
12					5.90	4.463
13					5.91	4.463
14					5.90	4.463
15					5.91	4.462
16					2.21	4.463
17						4.462
18						4.463
19						4.462
20						4.463
21						1.673

Table M 4:
3-, 5-, 7-, 10-, 15-, and 20-Year Property
Midquarter Convention
Placed in Service in Third Quarter

Year	Depreciation rate for recovery period					
	3-year	5-year	7-year	10-year	15-year	20-year
1	25.00%	15.00%	10.71%	7.50%	3.75%	2.813%
2	50.00	34.00	25.51	18.50	9.63	7.289
3	16.67	20.40	18.22	14.80	8.66	6.742
4	8.33	12.24	13.02	11.84	7.80	6.237
5		11.30	9.30	9.47	7.02	5.769
6		7.06	8.85	7.58	6.31	5.336
7			8.86	6.55	5.90	4.936
8			5.53	6.55	5.90	4.566
9				6.56	5.91	4.460
10				6.55	5.90	4.460
11				4.10	5.91	4.460
12					5.90	4.460
13					5.91	4.461
14					5.90	4.460
15					5.91	4.461
16					3.69	4.460
17						4.461
18						4.460
19						4.461
20						4.460
21						2.788

Table M 5:
3-, 5-, 7-, 10-, 15-, and 20-Year Property
Midquarter Convention
Placed in Service in Fourth Quarter

Year	Depreciation rate for recovery period					
	3-year	5-year	7-year	10-year	15-year	20-year
1	8.33%	5.00%	3.57%	2.50%	1.25%	0.938%
2	61.11	38.00	27.55	19.50	9.88	7.430
3	20.37	22.80	19.68	15.60	8.89	6.872
4	10.19	13.68	14.06	12.48	8.00	6.357
5		10.94	10.04	9.98	7.20	5.880
6		9.58	8.73	7.99	6.48	5.439
7			8.73	6.55	5.90	5.031
8			7.64	6.55	5.90	4.654
9				6.56	5.90	4.458
10				6.55	5.91	4.458
11				5.74	5.90	4.458
12					5.91	4.458
13					5.90	4.458
14					5.91	4.458
15					5.90	4.458
16					5.17	4.458
17						4.458
18						4.459
19						4.458
20						4.459
21						3.901

Table M 6:
Residential Rental Property
Midmonth Convention
Straight-Line—27.5 Years

Year	Month property placed in service											
	1	2	3	4	5	6	7	8	9	10	11	12
1	3.485%	3.182%	2.879%	2.576%	2.273%	1.970%	1.667%	1.364%	1.061%	0.758%	0.455%	0.152%
2-9	3.636	3.636	3.636	3.636	3.636	3.636	3.636	3.636	3.636	3.636	3.636	3.636
10	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
11	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
12	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
13	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
14	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
15	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
16	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
17	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
18	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
19	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
20	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
21	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
22	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
23	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
24	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
25	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
26	3.637	3.637	3.637	3.637	3.637	3.637	3.636	3.636	3.636	3.636	3.636	3.636
27	3.636	3.636	3.636	3.636	3.636	3.636	3.637	3.637	3.637	3.637	3.637	3.637
28	1.97	2.273	2.576	2.879	3.182	3.485	3.636	3.636	3.636	3.636	3.636	3.636
29							0.152	0.455	0.758	1.061	1.364	1.667

Table M 7:
Nonresidential Rental Property
Midmonth Convention
Straight-Line—31.5 Years

Year	Month property placed in service											
	1	2	3	4	5	6	7	8	9	10	11	12
1	3.042%	2.778%	2.513%	2.249%	1.984%	1.720%	1.455%	1.190%	0.926%	0.661%	0.397%	0.132%
2-7	3.175	3.175	3.175	3.175	3.175	3.175	3.175	3.175	3.175	3.175	3.175	3.175
8	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.175	3.175	3.175	3.175	3.175
9	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
10	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
11	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
12	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
13	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
14	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
15	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
16	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
17	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
18	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
19	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
20	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
21	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
22	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
23	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
24	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
25	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
26	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
27	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
28	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
29	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
30	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174
31	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175	3.174	3.175
32	1.720	1.984	2.249	2.513	2.778	3.042	3.175	3.174	3.175	3.174	3.175	3.174
33							0.132	0.397	0.661	0.926	1.190	1.455

Table M 7(a):
Nonresidential Rental Property
Midmonth Convention
Straight-Line—39 Years

Year	Month property placed in service											
	1	2	3	4	5	6	7	8	9	10	11	12
1	2.461%	2.247%	2.033%	1.819%	1.605%	1.391%	1.177%	0.963%	0.749%	0.535%	0.321%	0.107%
2-39	2.564	2.564	2.564	2.564	2.564	2.564	2.564	2.564	2.564	2.564	2.564	2.564
40	0.107	0.321	0.535	0.749	0.963	1.177	1.391	1.605	1.819	2.033	2.247	2.461

Table M 8:
Straight-Line Method
Half-Year Convention

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	20.0%	16.67%	14.29%	12.5%	10.0%	8.33%	7.69%	7.14%	6.67%	6.25%	5.88%	5.56%	5.26%
2	40.0	33.33	28.57	25.0	20.0	16.67	15.39	14.29	13.33	12.50	11.77	11.11	10.53
3	40.0	33.33	28.57	25.0	20.0	16.67	15.38	14.29	13.33	12.50	11.76	11.11	10.53
4		16.67	28.57	25.0	20.0	16.67	15.39	14.28	13.33	12.50	11.77	11.11	10.53
5				12.5	20.0	16.66	15.38	14.29	13.34	12.50	11.76	11.11	10.52
6					10.0	16.67	15.39	14.28	13.33	12.50	11.77	11.11	10.53
7						8.33	15.38	14.29	13.34	12.50	11.76	11.11	10.52
8								7.14	13.33	12.50	11.77	11.11	10.53
9										6.25	11.76	11.11	10.52
10												5.56	10.53

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	5.0%	4.76%	4.55%	4.35%	4.17%	4.0%	3.85%	3.70%	3.57%	3.33%	3.13%	3.03%	2.94%
2	10.0	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
3	10.0	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
4	10.0	9.53	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
5	10.0	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
6	10.0	9.53	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
7	10.0	9.52	9.09	8.70	8.34	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
8	10.0	9.53	9.09	8.69	8.33	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
9	10.0	9.52	9.09	8.70	8.34	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
10	10.0	9.53	9.09	8.69	8.33	8.0	7.70	7.40	7.15	6.66	6.25	6.06	5.88
11	5.0	9.52	9.09	8.70	8.34	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.89
12			4.55	8.69	8.33	8.0	7.70	7.40	7.15	6.66	6.25	6.06	5.88
13					4.17	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.89
14							3.85	7.40	7.15	6.66	6.25	6.06	5.88
15									3.57	6.67	6.25	6.06	5.89
16										3.33	6.25	6.06	5.88
17											3.12	6.07	5.89
18													2.94

Table M 8 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	2.78%	2.63%	2.5%	2.273%	2.083%	2.0%	1.887%	1.786%	1.667%	1.429%	1.25%	1.111%	1.0%
2	5.56	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
3	5.56	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
4	5.55	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
5	5.56	5.26	5.0	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
6	5.55	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
7	5.56	5.26	5.0	4.546	4.167	4.0	3.773	3.572	3.333	2.857	2.50	2.222	2.0
8	5.55	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
9	5.56	5.27	5.0	4.546	4.167	4.0	3.773	3.572	3.333	2.857	2.50	2.222	2.0
10	5.55	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
11	5.56	5.27	5.0	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.50	2.222	2.0
12	5.55	5.26	5.0	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.50	2.222	2.0
13	5.56	5.27	5.0	4.546	4.166	4.0	3.773	3.572	3.334	2.857	2.50	2.222	2.0
14	5.55	5.26	5.0	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
15	5.56	5.27	5.0	4.546	4.166	4.0	3.774	3.572	3.334	2.857	2.50	2.222	2.0
16	5.55	5.26	5.0	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
17	5.56	5.27	5.0	4.546	4.166	4.0	3.774	3.572	3.334	2.857	2.50	2.222	2.0
18	5.55	5.26	5.0	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
19	2.78	5.27	5.0	4.546	4.166	4.0	3.774	3.572	3.334	2.857	2.50	2.222	2.0
20		2.63	5.0	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
21			2.5	4.546	4.166	4.0	3.774	3.572	3.334	2.857	2.50	2.222	2.0
22				4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
23				2.273	4.166	4.0	3.774	3.572	3.334	2.857	2.50	2.222	2.0
24					4.167	4.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
25					2.083	4.0	3.774	3.572	3.334	2.857	2.50	2.222	2.0
26						2.0	3.773	3.571	3.333	2.857	2.50	2.222	2.0
27							3.774	3.572	3.334	2.857	2.50	2.223	2.0
28								3.571	3.333	2.858	2.50	2.222	2.0
29								1.786	3.334	2.857	2.50	2.223	2.0
30									3.333	2.858	2.50	2.222	2.0
31									1.667	2.857	2.50	2.223	2.0
32										2.858	2.50	2.222	2.0
33										2.857	2.50	2.223	2.0
34										2.858	2.50	2.222	2.0
35										2.857	2.50	2.223	2.0
36										1.429	2.50	2.222	2.0
37											2.50	2.223	2.0
38											2.50	2.222	2.0
39											2.50	2.223	2.0
40											2.50	2.222	2.0
41											1.25	2.223	2.0
42												2.222	2.0
43												2.223	2.0
44												2.222	2.0
45												2.223	2.0
46												1.111	2.0
47-50													2.0
51													1.0

Table M 9:
Straight-Line Method
Midquarter Convention
Placed in Service in First Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	35.0%	29.17%	25.00%	21.88%	17.5%	14.58%	13.46%	12.50%	11.67%	10.94%	10.29%	9.72%	9.21%
2	40.0	33.33	28.57	25.00	20.0	16.67	15.38	14.29	13.33	12.50	11.77	11.11	10.53
3	25.0	33.33	28.57	25.00	20.0	16.67	15.39	14.28	13.33	12.50	11.76	11.11	10.53
4		4.17	17.86	25.00	20.0	16.67	15.38	14.29	13.33	12.50	11.77	11.11	10.53
5				3.12	20.0	16.66	15.39	14.28	13.34	12.50	11.76	11.11	10.52
6					2.5	16.67	15.38	14.29	13.33	12.50	11.77	11.11	10.53
7						2.08	9.62	14.28	13.34	12.50	11.76	11.11	10.52
8								1.79	8.33	12.50	11.77	11.12	10.53
9										1.56	7.35	11.11	10.52
10												1.39	6.58

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	8.75%	8.33%	7.95%	7.61%	7.29%	7.0%	6.73%	6.48%	6.25%	5.83%	5.47%	5.30%	5.15%
2	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
3	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
4	10.00	9.53	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
5	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
6	10.00	9.53	9.09	8.69	8.34	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
7	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
8	10.00	9.53	9.09	8.69	8.34	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
9	10.00	9.52	9.09	8.70	8.33	8.0	7.70	7.40	7.14	6.67	6.25	6.06	5.88
10	10.00	9.53	9.10	8.69	8.34	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
11	1.25	5.95	9.09	8.70	8.33	8.0	7.70	7.40	7.14	6.67	6.25	6.06	5.88
12			1.14	5.43	8.34	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.89
13					1.04	5.0	7.70	7.40	7.14	6.67	6.25	6.06	5.88
14							0.96	4.63	7.15	6.66	6.25	6.06	5.89
15									0.89	6.67	6.25	6.06	5.88
16										0.83	6.25	6.07	5.89
17											0.78	3.79	5.88
18													0.74

Table M 9 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	4.86%	4.61%	4.375%	3.977%	3.646%	3.5%	3.302%	3.125%	2.917%	2.500%	2.188%	1.944%	1.75%
2	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
3	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
4	5.56	5.26	5.000	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
5	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
6	5.56	5.26	5.000	4.546	4.167	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
7	5.55	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
8	5.56	5.26	5.000	4.546	4.167	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
9	5.55	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
10	5.56	5.27	5.000	4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
11	5.55	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
12	5.56	5.27	5.000	4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
13	5.55	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
14	5.56	5.27	5.000	4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
15	5.55	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
16	5.56	5.27	5.000	4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
17	5.55	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
18	5.56	5.27	5.000	4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
19	0.69	5.26	5.000	4.545	4.167	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
20		0.66	5.000	4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
21			0.625	4.545	4.167	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
22				4.546	4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
23				0.568	4.167	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
24					4.166	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
25					0.521	4.0	3.773	3.571	3.334	2.857	2.500	2.222	2.00
26						0.5	3.774	3.572	3.333	2.857	2.500	2.223	2.00
27							2.358	3.571	3.334	2.858	2.500	2.222	2.00
28								3.572	3.333	2.857	2.500	2.223	2.00
29								0.446	3.334	2.858	2.500	2.222	2.00
30									3.333	2.857	2.500	2.223	2.00
31									0.417	2.858	2.500	2.222	2.00
32										2.857	2.500	2.223	2.00
33										2.858	2.500	2.222	2.00
34										2.857	2.500	2.223	2.00
35										2.858	2.500	2.222	2.00
36										0.357	2.500	2.223	2.00
37											2.500	2.222	2.00
38											2.500	2.223	2.00
39											2.500	2.222	2.00
40											2.500	2.223	2.00
41											0.312	2.222	2.00
42												2.223	2.00
43												2.222	2.00
44												2.223	2.00
45												2.222	2.00
46												0.278	2.00
47-50													2.00
51													0.25

Table M 10:
Straight-Line Method
Midquarter Convention
Placed in Service in Second Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	25.0%	20.83%	17.86%	15.63%	12.5%	10.42%	9.62%	8.93%	8.33%	7.81%	7.35%	6.94%	6.58%
2	40.0	33.33	28.57	25.00	20.0	16.67	15.38	14.29	13.33	12.50	11.77	11.11	10.53
3	35.0	33.34	28.57	25.00	20.0	16.67	15.38	14.28	13.33	12.50	11.76	11.11	10.53
4		12.50	25.00	25.00	20.0	16.66	15.39	14.29	13.34	12.50	11.77	11.11	10.53
5				9.37	20.0	16.67	15.38	14.28	13.33	12.50	11.76	11.11	10.52
6					7.5	16.66	15.39	14.29	13.34	12.50	11.77	11.11	10.53
7						6.25	13.46	14.28	13.33	12.50	11.76	11.11	10.52
8								5.36	11.67	12.50	11.77	11.12	10.53
9										4.69	10.29	11.11	10.52
10												4.17	9.21

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	6.25%	5.95%	5.68%	5.43%	5.21%	5.0%	4.81%	4.63%	4.46%	4.17%	3.91%	3.79%	3.68%
2	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
3	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
4	10.00	9.53	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
5	10.00	9.52	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
6	10.00	9.53	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
7	10.00	9.52	9.09	8.69	8.34	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
8	10.00	9.53	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
9	10.00	9.52	9.09	8.69	8.34	8.0	7.69	7.40	7.15	6.66	6.25	6.06	5.88
10	10.00	9.53	9.09	8.70	8.33	8.0	7.70	7.41	7.14	6.67	6.25	6.06	5.88
11	3.75	8.33	9.10	8.69	8.34	8.0	7.69	7.40	7.15	6.66	6.25	6.06	5.88
12			3.41	7.61	8.33	8.0	7.70	7.41	7.14	6.67	6.25	6.06	5.89
13					3.13	7.0	7.69	7.40	7.15	6.66	6.25	6.06	5.88
14							2.89	6.48	7.14	6.67	6.25	6.06	5.89
15									2.68	6.66	6.25	6.06	5.88
16										2.50	6.25	6.06	5.89
17											2.34	5.31	5.88
18													2.21

Table M 10 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	3.47%	3.29%	3.125%	2.841%	2.604%	2.5%	2.358%	2.232%	2.083%	1.786%	1.563%	1.389%	1.25%
2	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
3	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
4	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
5	5.55	5.26	5.000	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
6	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
7	5.55	5.26	5.000	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
8	5.56	5.26	5.000	4.545	4.167	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
9	5.55	5.27	5.000	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
10	5.56	5.26	5.000	4.545	4.167	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
11	5.55	5.27	5.000	4.546	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
12	5.56	5.26	5.000	4.545	4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
13	5.55	5.27	5.000	4.546	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
14	5.56	5.26	5.000	4.545	4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
15	5.55	5.27	5.000	4.546	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
16	5.56	5.26	5.000	4.545	4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
17	5.55	5.27	5.000	4.546	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
18	5.56	5.26	5.000	4.545	4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
19	2.08	5.27	5.000	4.546	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
20		1.97	5.000	4.545	4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
21			1.875	4.546	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
22				4.545	4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
23				1.705	4.166	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
24					4.167	4.0	3.773	3.572	3.334	2.857	2.500	2.222	2.00
25					1.562	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
26						1.5	3.773	3.572	3.334	2.857	2.500	2.222	2.00
27							3.302	3.571	3.333	2.857	2.500	2.223	2.00
28								3.572	3.334	2.858	2.500	2.222	2.00
29								1.339	3.333	2.857	2.500	2.223	2.00
30									3.334	2.858	2.500	2.222	2.00
31									1.250	2.857	2.500	2.223	2.00
32										2.858	2.500	2.222	2.00
33										2.857	2.500	2.223	2.00
34										2.858	2.500	2.222	2.00
35										2.857	2.500	2.223	2.00
36										1.072	2.500	2.222	2.00
37											2.500	2.223	2.00
38											2.500	2.222	2.00
39											2.500	2.223	2.00
40											2.500	2.222	2.00
41											0.937	2.223	2.00
42												2.222	2.00
43												2.223	2.00
44												2.222	2.00
45												2.223	2.00
46												0.833	2.00
47-50													2.00
51													0.75

Table M 11:
Straight-Line Method
Midquarter Convention
Placed in Service in Third Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	15.0%	12.50%	10.71%	9.38%	7.5%	6.25%	5.77%	5.36%	5.00%	4.69%	4.41%	4.17%	3.95%
2	40.0	33.33	28.57	25.00	20.0	16.67	15.38	14.29	13.33	12.50	11.76	11.11	10.53
3	40.0	33.34	28.57	25.00	20.0	16.67	15.39	14.28	13.33	12.50	11.77	11.11	10.53
4	5.0	20.83	28.58	25.00	20.0	16.66	15.38	14.29	13.33	12.50	11.76	11.11	10.52
5			3.57	15.62	20.0	16.67	15.39	14.28	13.34	12.50	11.77	11.11	10.53
6					12.5	16.66	15.38	14.29	13.33	12.50	11.76	11.11	10.52
7						10.42	15.39	14.28	13.34	12.50	11.77	11.11	10.53
8							1.92	8.93	13.33	12.50	11.76	11.11	10.52
9									1.67	7.81	11.77	11.11	10.53
10											1.47	6.95	10.52
11													1.32

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	3.75%	3.57%	3.41%	3.26%	3.13%	3.0%	2.88%	2.78%	2.68%	2.50%	2.34%	2.27%	2.21%
2	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
3	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
4	10.00	9.52	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
5	10.00	9.53	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
6	10.00	9.52	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
7	10.00	9.53	9.09	8.70	8.34	8.0	7.69	7.41	7.14	6.66	6.25	6.06	5.88
8	10.00	9.52	9.09	8.69	8.33	8.0	7.70	7.40	7.14	6.67	6.25	6.06	5.88
9	10.00	9.53	9.09	8.70	8.34	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
10	10.00	9.52	9.09	8.69	8.33	8.0	7.70	7.40	7.14	6.67	6.25	6.06	5.88
11	6.25	9.53	9.10	8.70	8.34	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
12		1.19	5.68	8.69	8.33	8.0	7.70	7.40	7.14	6.67	6.25	6.06	5.89
13				1.09	5.21	8.0	7.69	7.41	7.15	6.66	6.25	6.06	5.88
14						1.0	4.81	7.40	7.14	6.67	6.25	6.06	5.89
15								0.93	4.47	6.66	6.25	6.06	5.88
16										4.17	6.25	6.07	5.89
17											3.91	6.06	5.88
18												0.76	3.68

Table M 11 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	2.08%	1.97%	1.875%	1.705%	1.563%	1.5%	1.415%	1.339%	1.250%	1.071%	0.938%	0.833%	0.75%
2	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
3	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
4	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
5	5.55	5.26	5.000	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
6	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
7	5.55	5.26	5.000	4.546	4.167	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
8	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
9	5.55	5.27	5.000	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
10	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.333	2.857	2.500	2.222	2.00
11	5.55	5.27	5.000	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
12	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
13	5.55	5.27	5.000	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
14	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
15	5.55	5.27	5.000	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
16	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
17	5.55	5.27	5.000	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
18	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
19	3.47	5.27	5.000	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
20		3.29	5.000	4.545	4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
21			3.125	4.546	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
22				4.545	4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
23				2.841	4.166	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
24					4.167	4.0	3.774	3.572	3.334	2.857	2.500	2.222	2.00
25					2.604	4.0	3.773	3.571	3.333	2.857	2.500	2.222	2.00
26						2.5	3.774	3.572	3.334	2.858	2.500	2.222	2.00
27							3.773	3.571	3.333	2.857	2.500	2.223	2.00
28							0.472	3.572	3.334	2.858	2.500	2.222	2.00
29								2.232	3.333	2.857	2.500	2.223	2.00
30									3.334	2.858	2.500	2.222	2.00
31									2.083	2.857	2.500	2.223	2.00
32										2.858	2.500	2.222	2.00
33										2.857	2.500	2.223	2.00
34										2.858	2.500	2.222	2.00
35										2.857	2.500	2.223	2.00
36										1.786	2.500	2.222	2.00
37											2.500	2.223	2.00
38											2.500	2.222	2.00
39											2.500	2.223	2.00
40											2.500	2.222	2.00
41											1.562	2.223	2.00
42												2.222	2.00
43												2.223	2.00
44												2.222	2.00
45												2.223	2.00
46												1.389	2.00
47-50													2.00
51													1.25

Table M 12:
Straight-Line Method
Midquarter Convention
Placed in Service in Fourth Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	5.0%	4.17%	3.57%	3.13%	2.5%	2.08%	1.92%	1.79%	1.67%	1.56%	1.47%	1.39%	1.32%
2	40.0	33.33	28.57	25.00	20.0	16.67	15.39	14.29	13.33	12.50	11.76	11.11	10.53
3	40.0	33.33	28.57	25.00	20.0	16.67	15.38	14.28	13.33	12.50	11.77	11.11	10.53
4	15.0	29.17	28.57	25.00	20.0	16.67	15.39	14.29	13.33	12.50	11.76	11.11	10.52
5			10.72	21.87	20.0	16.66	15.38	14.28	13.33	12.50	11.77	11.11	10.53
6					17.5	16.67	15.39	14.29	13.34	12.50	11.76	11.11	10.52
7						14.58	15.38	14.28	13.33	12.50	11.77	11.11	10.53
8							5.77	12.50	13.34	12.50	11.76	11.11	10.52
9									5.00	10.94	11.77	11.11	10.53
10											4.41	9.73	10.52
11													3.95

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	1.25%	1.19%	1.14%	1.09%	1.04%	1.0%	0.96%	0.93%	0.89%	0.83%	0.78%	0.76%	0.74%
2	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
3	10.00	9.52	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
4	10.00	9.52	9.09	8.70	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
5	10.00	9.53	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
6	10.00	9.52	9.09	8.70	8.34	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
7	10.00	9.53	9.09	8.69	8.33	8.0	7.69	7.41	7.14	6.67	6.25	6.06	5.88
8	10.00	9.52	9.09	8.70	8.34	8.0	7.69	7.40	7.15	6.66	6.25	6.06	5.88
9	10.00	9.53	9.09	8.69	8.33	8.0	7.70	7.41	7.14	6.67	6.25	6.06	5.88
10	10.00	9.52	9.09	8.70	8.34	8.0	7.69	7.40	7.15	6.66	6.25	6.06	5.88
11	8.75	9.53	9.09	8.69	8.33	8.0	7.70	7.41	7.14	6.67	6.25	6.06	5.88
12		3.57	7.96	8.70	8.34	8.0	7.69	7.40	7.15	6.66	6.25	6.06	5.89
13				3.26	7.29	8.0	7.70	7.41	7.14	6.67	6.25	6.06	5.88
14						3.0	6.73	7.40	7.15	6.66	6.25	6.06	5.89
15								2.78	6.25	6.67	6.25	6.06	5.88
16										5.83	6.25	6.06	5.89
17											5.47	6.07	5.88
18												2.27	5.15

Table M 12 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	0.69%	0.66%	0.625%	0.568%	0.521%	0.5%	0.472%	0.446%	0.417%	0.357%	0.313%	0.278%	0.25%
2	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
3	5.56	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
4	5.56	5.26	5.000	4.546	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
5	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
6	5.56	5.26	5.000	4.546	4.167	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
7	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
8	5.56	5.26	5.000	4.546	4.167	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
9	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
10	5.56	5.27	5.000	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
11	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.333	2.857	2.500	2.222	2.00
12	5.56	5.27	5.000	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
13	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
14	5.56	5.27	5.000	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
15	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
16	5.56	5.27	5.000	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
17	5.55	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
18	5.56	5.27	5.000	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
19	4.86	5.26	5.000	4.545	4.167	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
20		4.61	5.000	4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
21			4.375	4.545	4.167	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
22				4.546	4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
23				3.977	4.167	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
24					4.166	4.0	3.773	3.572	3.333	2.857	2.500	2.222	2.00
25					3.646	4.0	3.774	3.571	3.334	2.857	2.500	2.222	2.00
26						3.5	3.773	3.572	3.333	2.857	2.500	2.222	2.00
27							3.774	3.571	3.334	2.858	2.500	2.222	2.00
28							1.415	3.572	3.333	2.857	2.500	2.223	2.00
29								3.125	3.334	2.858	2.500	2.222	2.00
30									3.333	2.857	2.500	2.223	2.00
31									2.917	2.858	2.500	2.222	2.00
32										2.857	2.500	2.223	2.00
33										2.858	2.500	2.222	2.00
34										2.857	2.500	2.223	2.00
35										2.858	2.500	2.222	2.00
36										2.500	2.500	2.223	2.00
37											2.500	2.222	2.00
38											2.500	2.223	2.00
39											2.500	2.222	2.00
40											2.500	2.223	2.00
41											2.187	2.222	2.00
42												2.223	2.00
43												2.222	2.00
44												2.223	2.00
45												2.222	2.00
46												1.945	2.00
47-50													2.00
51													1.75

Table M 13:
Straight-Line Method
Midmonth Convention

Year	Month property placed in service											
	1	2	3	4	5	6	7	8	9	10	11	12
1	2.396%	2.188%	1.979%	1.771%	1.563%	1.354%	1.146%	0.938%	0.729%	0.521%	0.313%	0.104%
2-40	2.500	2.500	2.500	2.500	2.500	2.500	2.500	2.500	2.500	2.500	2.500	2.500
41	0.104	0.312	0.521	0.729	0.937	1.146	1.354	1.562	1.771	1.979	2.187	2.396

Table M 14:
150% Declining-Balance Method
Half-Year Convention

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	30.0%	25.0%	21.43%	18.75%	15.00%	12.50%	11.54%	10.71%	10.00%	9.38%	8.82%	8.33%	7.89%
2	42.0	37.5	33.67	30.47	25.50	21.88	20.41	19.13	18.00	16.99	16.09	15.28	14.54
3	28.0	25.0	22.45	20.31	17.85	16.41	15.70	15.03	14.40	13.81	13.25	12.73	12.25
4		12.5	22.45	20.31	16.66	14.06	13.09	12.25	11.52	11.22	10.91	10.61	10.31
5				10.16	16.66	14.06	13.09	12.25	11.52	10.80	10.19	9.65	9.17
6					8.33	14.06	13.09	12.25	11.52	10.80	10.19	9.64	9.17
7						7.03	13.08	12.25	11.52	10.80	10.18	9.65	9.17
8								6.13	11.52	10.80	10.19	9.64	9.17
9										5.40	10.18	9.65	9.17
10												4.82	9.16

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	7.50%	7.14%	6.82%	6.52%	6.25%	6.00%	5.77%	5.56%	5.36%	5.00%	4.69%	4.55%	4.41%
2	13.88	13.27	12.71	12.19	11.72	11.28	10.87	10.49	10.14	9.50	8.94	8.68	8.43
3	11.79	11.37	10.97	10.60	10.25	9.93	9.62	9.33	9.05	8.55	8.10	7.89	7.69
4	10.02	9.75	9.48	9.22	8.97	8.73	8.51	8.29	8.08	7.70	7.34	7.17	7.01
5	8.74	8.35	8.18	8.02	7.85	7.69	7.53	7.37	7.22	6.93	6.65	6.52	6.39
6	8.74	8.35	7.98	7.64	7.33	7.05	6.79	6.55	6.44	6.23	6.03	5.93	5.83
7	8.74	8.35	7.97	7.64	7.33	7.05	6.79	6.55	6.32	5.90	5.55	5.39	5.32
8	8.74	8.35	7.98	7.63	7.33	7.05	6.79	6.55	6.32	5.90	5.55	5.39	5.23
9	8.74	8.36	7.97	7.64	7.33	7.04	6.79	6.55	6.32	5.91	5.55	5.39	5.23
10	8.74	8.35	7.98	7.63	7.33	7.05	6.79	6.55	6.32	5.90	5.55	5.39	5.23
11	4.37	8.36	7.97	7.64	7.32	7.04	6.79	6.55	6.32	5.91	5.55	5.39	5.23
12			3.99	7.63	7.33	7.05	6.78	6.55	6.32	5.90	5.55	5.39	5.23
13					3.66	7.04	6.79	6.56	6.32	5.91	5.54	5.38	5.23
14							3.39	6.55	6.31	5.90	5.55	5.39	5.23
15									3.16	5.91	5.54	5.38	5.23
16										2.95	5.55	5.39	5.23
17											2.77	5.38	5.23
18													2.62

Table M 14 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	4.17%	3.95%	3.750%	3.409%	3.125%	3.000%	2.830%	2.679%	2.500%	2.143%	1.875%	1.667%	1.500%
2	7.99	7.58	7.219	6.586	6.055	5.820	5.500	5.214	4.875	4.194	3.680	3.278	2.955
3	7.32	6.98	6.677	6.137	5.676	5.471	5.189	4.934	4.631	4.014	3.542	3.169	2.866
4	6.71	6.43	6.177	5.718	5.322	5.143	4.895	4.670	4.400	3.842	3.409	3.063	2.780
5	6.15	5.93	5.713	5.328	4.989	4.834	4.618	4.420	4.180	3.677	3.281	2.961	2.697
6	5.64	5.46	5.285	4.965	4.677	4.544	4.357	4.183	3.971	3.520	3.158	2.862	2.616
7	5.17	5.03	4.888	4.627	4.385	4.271	4.110	3.959	3.772	3.369	3.040	2.767	2.538
8	4.94	4.69	4.522	4.311	4.111	4.015	3.877	3.747	3.584	3.225	2.926	2.674	2.461
9	4.94	4.69	4.462	4.063	3.854	3.774	3.658	3.546	3.404	3.086	2.816	2.585	2.388
10	4.94	4.69	4.461	4.063	3.729	3.584	3.451	3.356	3.234	2.954	2.710	2.499	2.316
11	4.94	4.69	4.462	4.063	3.729	3.583	3.383	3.205	3.072	2.828	2.609	2.416	2.246
12	4.95	4.69	4.461	4.063	3.729	3.584	3.383	3.205	2.994	2.706	2.511	2.335	2.179
13	4.94	4.69	4.462	4.064	3.730	3.583	3.383	3.205	2.994	2.590	2.417	2.257	2.114
14	4.95	4.69	4.461	4.063	3.729	3.584	3.383	3.205	2.994	2.571	2.326	2.182	2.050
15	4.94	4.69	4.462	4.064	3.730	3.583	3.383	3.205	2.994	2.571	2.253	2.110	1.989
16	4.95	4.69	4.461	4.063	3.729	3.584	3.383	3.205	2.994	2.571	2.253	2.039	1.929
17	4.94	4.69	4.462	4.064	3.730	3.583	3.383	3.205	2.994	2.571	2.253	2.005	1.871
18	4.95	4.70	4.461	4.063	3.729	3.584	3.383	3.205	2.994	2.571	2.253	2.005	1.815
19	2.47	4.69	4.462	4.064	3.730	3.583	3.383	3.205	2.994	2.571	2.253	2.005	1.806
20		2.35	4.461	4.463	3.729	3.584	3.384	3.205	2.993	2.571	2.253	2.005	1.806
21			2.231	4.064	3.730	3.583	3.383	3.205	2.994	2.571	2.253	2.005	1.806
22				4.063	3.729	3.584	3.384	3.205	2.993	2.571	2.253	2.005	1.806
23				2.032	3.730	3.583	3.383	3.205	2.994	2.571	2.253	2.005	1.806
24					3.729	3.584	3.384	3.205	2.993	2.571	2.253	2.004	1.806
25					1.865	3.583	3.383	3.205	2.994	2.571	2.253	2.005	1.806
26						1.792	3.384	3.205	2.993	2.571	2.253	2.004	1.806
27							3.383	3.205	2.994	2.571	2.253	2.005	1.806
28								3.205	2.993	2.572	2.253	2.004	1.806
29								1.602	2.994	2.571	2.253	2.005	1.806
30									2.993	2.572	2.253	2.004	1.806
31									1.497	2.571	2.253	2.005	1.806
32										2.572	2.253	2.004	1.806
33										2.571	2.252	2.005	1.806
34										2.572	2.253	2.004	1.806
35										2.571	2.252	2.005	1.806
36										1.286	2.253	2.004	1.806
37											2.252	2.005	1.806
38											2.253	2.004	1.806
39											2.252	2.005	1.806
40											2.253	2.004	1.806
41											1.126	2.005	1.806
42												2.004	1.805
43												2.005	1.806
44												2.004	1.805
45												2.005	1.806
46												1.002	1.805
47													1.806
48													1.805
49													1.806
50													1.805
51													0.903

Table M 15:
150% Declining-Balance Method
Midquarter Convention
Property Placed in Service in First Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	52.50%	43.75%	37.50%	32.81%	26.25%	21.88%	20.19%	18.75%	17.50%	16.41%	15.44%	14.58%	13.82%
2	29.23	28.13	26.79	25.20	22.13	19.53	18.42	17.41	16.50	15.67	14.92	14.24	13.61
3	18.27	25.00	21.98	19.76	16.52	14.65	14.17	13.68	13.20	12.74	12.29	11.86	11.46
4		3.12	13.73	19.76	16.52	14.06	13.03	12.16	11.42	10.77	10.20	9.89	9.65
5				2.47	16.52	14.06	13.02	12.16	11.42	10.77	10.19	9.64	9.15
6					2.06	14.06	13.03	12.16	11.41	10.76	10.20	9.65	9.15
7						1.76	8.14	12.16	11.42	10.77	10.19	9.64	9.15
8								1.52	7.13	10.76	10.20	9.65	9.15
9										1.35	6.37	9.64	9.14
10												1.21	5.72

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	13.13%	12.50%	11.93%	11.41%	10.94%	10.50%	10.10%	9.72%	9.38%	8.75%	8.20%	7.95%	7.72%
2	13.03	12.50	12.01	11.56	11.13	10.74	10.37	10.03	9.71	9.13	8.61	8.37	8.14
3	11.08	10.71	10.37	10.05	9.74	9.45	9.18	8.92	8.67	8.21	7.80	7.61	7.42
4	9.41	9.18	8.96	8.74	8.52	8.32	8.12	7.93	7.74	7.39	7.07	6.92	6.77
5	8.71	8.32	7.96	7.64	7.46	7.32	7.18	7.04	6.91	6.65	6.41	6.29	6.17
6	8.71	8.32	7.96	7.64	7.33	7.04	6.78	6.53	6.31	5.99	5.80	5.71	5.63
7	8.71	8.32	7.96	7.64	7.33	7.04	6.77	6.54	6.31	5.90	5.54	5.38	5.23
8	8.71	8.32	7.96	7.64	7.33	7.04	6.78	6.53	6.31	5.91	5.54	5.38	5.23
9	8.71	8.32	7.96	7.64	7.33	7.04	6.77	6.54	6.31	5.90	5.54	5.38	5.23
10	8.71	8.31	7.97	7.63	7.32	7.04	6.78	6.53	6.31	5.91	5.54	5.38	5.23
11	1.09	5.20	7.96	7.64	7.33	7.04	6.77	6.54	6.31	5.90	5.54	5.38	5.23
12			1.00	4.77	7.32	7.03	6.78	6.53	6.31	5.91	5.54	5.38	5.22
13					0.92	4.40	6.77	6.54	6.32	5.90	5.54	5.38	5.23
14							0.85	4.08	6.31	5.91	5.55	5.38	5.22
15									0.79	5.90	5.54	5.38	5.23
16										0.74	5.55	5.37	5.22
17											0.69	3.36	5.23
18													0.65

Table M 15 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	7.29%	6.91%	6.563%	5.966%	5.469%	5.250%	4.953%	4.688%	4.375%	3.750%	3.281%	2.917%	2.625%
2	7.73	7.35	7.008	6.411	5.908	5.685	5.380	5.106	4.781	4.125	3.627	3.236	2.921
3	7.08	6.77	6.482	5.974	5.539	5.344	5.075	4.832	4.542	3.948	3.491	3.128	2.834
4	6.49	6.23	5.996	5.567	5.193	5.023	4.788	4.574	4.315	3.779	3.360	3.024	2.749
5	5.95	5.74	5.546	5.187	4.868	4.722	4.517	4.329	4.099	3.617	3.234	2.923	2.666
6	5.45	5.29	5.130	4.834	4.564	4.439	4.262	4.097	3.894	3.462	3.113	2.826	2.586
7	5.00	4.87	4.746	4.504	4.279	4.172	4.020	3.877	3.700	3.314	2.996	2.732	2.509
8	4.94	4.69	4.459	4.197	4.011	3.922	3.793	3.669	3.515	3.172	2.884	2.640	2.433
9	4.95	4.69	4.459	4.061	3.761	3.687	3.578	3.473	3.339	3.036	2.776	2.552	2.360
10	4.94	4.69	4.459	4.061	3.729	3.582	3.383	3.287	3.172	2.906	2.671	2.467	2.290
11	4.95	4.69	4.459	4.061	3.729	3.582	3.384	3.204	3.013	2.781	2.571	2.385	2.221
12	4.94	4.69	4.460	4.061	3.730	3.582	3.383	3.204	2.994	2.662	2.475	2.306	2.154
13	4.95	4.69	4.459	4.061	3.729	3.582	3.384	3.204	2.994	2.571	2.382	2.229	2.090
14	4.94	4.69	4.460	4.061	3.730	3.582	3.383	3.204	2.994	2.571	2.293	2.154	2.027
15	4.95	4.68	4.459	4.061	3.729	3.582	3.384	3.204	2.994	2.571	2.252	2.083	1.966
16	4.94	4.69	4.460	4.061	3.730	3.582	3.383	3.204	2.994	2.571	2.252	2.013	1.907
17	4.95	4.68	4.459	4.061	3.729	3.582	3.384	3.204	2.994	2.571	2.253	2.005	1.850
18	4.94	4.69	4.460	4.061	3.730	3.582	3.383	3.204	2.994	2.571	2.252	2.005	1.806
19	0.62	4.68	4.459	4.061	3.729	3.581	3.384	3.204	2.994	2.571	2.253	2.005	1.806
20		0.59	4.460	4.060	3.730	3.582	3.383	3.204	2.994	2.571	2.252	2.005	1.806
21			0.557	4.061	3.729	3.581	3.384	3.203	2.993	2.571	2.253	2.005	1.806
22				4.060	3.730	3.582	3.383	3.204	2.994	2.571	2.252	2.005	1.806
23				0.508	3.729	3.581	3.384	3.203	2.993	2.571	2.253	2.005	1.806
24					3.730	3.582	3.383	3.204	2.994	2.570	2.252	2.005	1.806
25					0.466	3.581	3.384	3.203	2.993	2.571	2.253	2.004	1.806
26						0.448	3.383	3.204	2.994	2.570	2.252	2.005	1.806
27							2.115	3.203	2.993	2.571	2.253	2.004	1.806
28								3.204	2.994	2.570	2.252	2.005	1.805
29								0.400	2.993	2.571	2.253	2.004	1.806
30									2.994	2.570	2.252	2.005	1.805
31									0.374	2.571	2.253	2.004	1.806
32										2.570	2.252	2.005	1.805
33										2.571	2.253	2.004	1.806
34										2.570	2.252	2.005	1.805
35										2.571	2.253	2.004	1.806
36										0.321	2.252	2.005	1.805
37											2.253	2.004	1.806
38											2.252	2.005	1.805
39											2.253	2.004	1.806
40											2.252	2.005	1.805
41											0.282	2.004	1.806
42												2.005	1.805
43												2.004	1.806
44												2.005	1.805
45												2.004	1.806
46												0.251	1.805
47													1.806
48													1.805
49													1.806
50													1.805
51													0.226

Table M 16:
150% Declining-Balance Method
Midquarter Convention
Property Placed in Service in Second Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	37.50%	31.25%	26.79%	23.44%	18.75%	15.63%	14.42%	13.39%	12.50%	11.72%	11.03%	10.42%	9.87%
2	37.50	34.38	31.38	28.71	24.38	21.09	19.75	18.56	17.50	16.55	15.70	14.93	14.23
3	25.00	25.00	22.31	20.15	17.06	15.82	15.19	14.58	14.00	13.45	12.93	12.44	11.98
4		9.37	19.52	20.15	16.76	14.06	13.07	12.22	11.49	10.93	10.65	10.37	10.09
5				7.55	16.76	14.06	13.07	12.22	11.49	10.82	10.19	9.64	9.16
6					6.29	14.07	13.07	12.22	11.49	10.82	10.19	9.65	9.16
7						5.27	11.43	12.23	11.48	10.83	10.19	9.64	9.16
8								4.58	10.05	10.82	10.20	9.65	9.17
9										4.06	8.92	9.64	9.16
10												3.62	8.02

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	9.38%	8.93%	8.52%	8.15%	7.81%	7.50%	7.21%	6.94%	6.70%	6.25%	5.86%	5.68%	5.51%
2	13.59	13.01	12.47	11.98	11.52	11.10	10.71	10.34	10.00	9.38	8.83	8.57	8.34
3	11.55	11.15	10.77	10.42	10.08	9.77	9.47	9.19	8.92	8.44	8.00	7.80	7.60
4	9.82	9.56	9.31	9.06	8.82	8.60	8.38	8.17	7.97	7.59	7.25	7.09	6.93
5	8.73	8.34	8.04	7.88	7.72	7.56	7.41	7.26	7.12	6.83	6.57	6.44	6.32
6	8.73	8.34	7.98	7.64	7.33	7.04	6.78	6.55	6.35	6.15	5.95	5.86	5.76
7	8.73	8.34	7.98	7.64	7.33	7.04	6.79	6.55	6.32	5.91	5.55	5.38	5.25
8	8.73	8.34	7.98	7.64	7.33	7.05	6.78	6.55	6.32	5.90	5.55	5.39	5.23
9	8.73	8.34	7.99	7.64	7.33	7.04	6.79	6.54	6.32	5.91	5.55	5.38	5.23
10	8.73	8.35	7.98	7.63	7.33	7.05	6.78	6.55	6.32	5.90	5.54	5.39	5.23
11	3.28	7.30	7.99	7.64	7.33	7.04	6.79	6.54	6.32	5.91	5.55	5.38	5.23
12			2.99	6.68	7.32	7.05	6.78	6.55	6.32	5.90	5.54	5.39	5.23
13					2.75	6.16	6.79	6.54	6.32	5.91	5.55	5.38	5.24
14							2.54	5.73	6.33	5.90	5.54	5.39	5.23
15									2.37	5.91	5.55	5.38	5.24
16										2.21	5.54	5.39	5.23
17											2.08	4.71	5.24
18													1.96

Table M 16 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	5.21%	4.93%	4.688%	4.261%	3.906%	3.750%	3.538%	3.348%	3.125%	2.679%	2.344%	2.083%	1.875%
2	7.90	7.51	7.148	6.528	6.006	5.775	5.460	5.178	4.844	4.171	3.662	3.264	2.944
3	7.24	6.91	6.612	6.083	5.631	5.429	5.151	4.900	4.602	3.992	3.525	3.155	2.855
4	6.64	6.37	6.116	5.668	5.279	5.103	4.859	4.638	4.371	3.821	3.393	3.050	2.770
5	6.08	5.86	5.658	5.281	4.949	4.797	4.584	4.389	4.153	3.657	3.265	2.948	2.687
6	5.58	5.40	5.233	4.921	4.639	4.509	4.325	4.154	3.945	3.501	3.143	2.850	2.606
7	5.11	4.98	4.841	4.586	4.349	4.238	4.080	3.932	3.748	3.351	3.025	2.755	2.528
8	4.94	4.69	4.478	4.273	4.078	3.984	3.849	3.721	3.561	3.207	2.912	2.663	2.452
9	4.94	4.69	4.463	4.063	3.823	3.745	3.631	3.522	3.383	3.069	2.802	2.574	2.378
10	4.95	4.69	4.463	4.063	3.729	3.583	3.426	3.333	3.213	2.938	2.697	2.489	2.307
11	4.94	4.69	4.463	4.062	3.729	3.583	3.384	3.205	3.053	2.812	2.596	2.406	2.238
12	4.95	4.69	4.463	4.063	3.729	3.583	3.383	3.205	2.994	2.692	2.499	2.325	2.171
13	4.94	4.69	4.463	4.062	3.730	3.583	3.384	3.205	2.994	2.576	2.405	2.248	2.106
14	4.95	4.69	4.463	4.063	3.729	3.583	3.383	3.205	2.994	2.571	2.315	2.173	2.042
15	4.94	4.69	4.462	4.062	3.730	3.583	3.384	3.205	2.994	2.571	2.253	2.101	1.981
16	4.95	4.69	4.463	4.063	3.729	3.583	3.383	3.204	2.994	2.571	2.253	2.031	1.922
17	4.94	4.69	4.462	4.062	3.730	3.583	3.384	3.205	2.994	2.571	2.253	2.005	1.864
18	4.95	4.69	4.463	4.063	3.729	3.583	3.383	3.204	2.993	2.571	2.253	2.005	1.808
19	1.85	4.69	4.462	4.062	3.730	3.583	3.384	3.205	2.994	2.571	2.253	2.005	1.806
20		1.76	4.463	4.063	3.729	3.583	3.383	3.204	2.993	2.571	2.253	2.005	1.806
21			1.673	4.062	3.730	3.583	3.384	3.205	2.994	2.572	2.253	2.005	1.806
22				4.063	3.729	3.583	3.383	3.204	2.993	2.571	2.253	2.005	1.806
23				1.523	3.730	3.583	3.384	3.205	2.994	2.572	2.253	2.004	1.806
24					3.729	3.582	3.383	3.204	2.993	2.571	2.253	2.005	1.806
25					1.399	3.583	3.384	3.205	2.994	2.572	2.253	2.004	1.806
26						1.343	3.383	3.204	2.993	2.571	2.253	2.005	1.806
27							2.961	3.205	2.994	2.572	2.253	2.004	1.806
28								3.204	2.993	2.571	2.253	2.005	1.806
29								1.202	2.994	2.572	2.253	2.004	1.806
30									2.993	2.571	2.252	2.005	1.806
31									1.123	2.572	2.253	2.004	1.806
32										2.571	2.252	2.005	1.806
33										2.572	2.253	2.004	1.806
34										2.571	2.252	2.005	1.806
35										2.572	2.253	2.004	1.806
36										0.964	2.252	2.005	1.806
37											2.253	2.004	1.806
38											2.252	2.005	1.806
39											2.253	2.004	1.806
40											2.252	2.005	1.806
41											0.845	2.004	1.806
42												2.005	1.806
43												2.004	1.806
44												2.005	1.806
45												2.004	1.805
46												0.752	1.806
47													1.805
48													1.806
49													1.805
50													1.806
51													0.677

Table M 17:
150% Declining-Balance Method
Midquarter Convention
Property Placed in Service in Third Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	22.50%	18.75%	16.07%	14.06%	11.25%	9.38%	8.65%	8.04%	7.50%	7.03%	6.62%	6.25%	5.92%
2	46.50	40.63	35.97	32.23	26.63	22.66	21.08	19.71	18.50	17.43	16.48	15.63	14.85
3	27.56	25.00	22.57	20.46	18.64	16.99	16.22	15.48	14.80	14.16	13.57	13.02	12.51
4	3.44	15.62	22.57	20.46	16.56	14.06	13.10	12.27	11.84	11.51	11.18	10.85	10.53
5			2.82	12.79	16.57	14.06	13.10	12.28	11.48	10.78	10.18	9.64	9.17
6					10.35	14.06	13.11	12.27	11.48	10.78	10.17	9.65	9.17
7						8.79	13.10	12.28	11.48	10.78	10.18	9.64	9.18
8							1.64	7.67	11.48	10.79	10.17	9.65	9.17
9									1.44	6.74	10.18	9.64	9.18
10											1.27	6.03	9.17
11													1.15

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	5.63%	5.36%	5.11%	4.89%	4.69%	4.50%	4.33%	4.17%	4.02%	3.75%	3.52%	3.41%	3.31%
2	14.16	13.52	12.94	12.41	11.91	11.46	11.04	10.65	10.28	9.63	9.05	8.78	8.53
3	12.03	11.59	11.18	10.79	10.43	10.08	9.77	9.46	9.18	8.66	8.20	7.98	7.78
4	10.23	9.93	9.65	9.38	9.12	8.88	8.64	8.41	8.20	7.80	7.43	7.26	7.09
5	8.75	8.51	8.33	8.16	7.98	7.81	7.64	7.48	7.32	7.02	6.73	6.60	6.47
6	8.75	8.34	7.97	7.63	7.33	7.05	6.79	6.65	6.54	6.31	6.10	6.00	5.90
7	8.75	8.34	7.97	7.63	7.33	7.05	6.79	6.55	6.31	5.90	5.55	5.45	5.38
8	8.74	8.34	7.97	7.63	7.33	7.05	6.79	6.54	6.31	5.90	5.55	5.38	5.23
9	8.75	8.34	7.97	7.63	7.33	7.05	6.79	6.55	6.32	5.91	5.55	5.39	5.23
10	8.74	8.34	7.97	7.63	7.32	7.05	6.79	6.54	6.31	5.90	5.55	5.38	5.23
11	5.47	8.35	7.96	7.63	7.33	7.05	6.79	6.55	6.32	5.91	5.55	5.39	5.23
12		1.04	4.98	7.64	7.32	7.04	6.80	6.54	6.31	5.90	5.55	5.38	5.23
13				0.95	4.58	7.05	6.79	6.55	6.32	5.91	5.55	5.39	5.22
14						0.88	4.25	6.54	6.31	5.90	5.55	5.38	5.23
15								0.82	3.95	5.91	5.55	5.39	5.22
16										3.69	5.55	5.38	5.23
17											3.47	5.39	5.22
18												0.67	3.27

Table M 17 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	3.13%	2.96%	2.813%	2.557%	2.344%	2.250%	2.123%	2.009%	1.875%	1.607%	1.406%	1.250%	1.125%
2	8.07	7.66	7.289	6.644	6.104	5.865	5.540	5.250	4.906	4.217	3.697	3.292	2.966
3	7.40	7.06	6.742	6.191	5.722	5.513	5.227	4.968	4.661	4.036	3.559	3.182	2.877
4	6.78	6.50	6.237	5.769	5.364	5.182	4.931	4.702	4.428	3.863	3.425	3.076	2.791
5	6.22	5.99	5.769	5.375	5.029	4.871	4.652	4.450	4.207	3.698	3.297	2.973	2.707
6	5.70	5.51	5.336	5.009	4.715	4.579	4.388	4.212	3.996	3.539	3.173	2.874	2.626
7	5.23	5.08	4.936	4.667	4.420	4.304	4.140	3.986	3.796	3.387	3.054	2.778	2.547
8	4.94	4.69	4.566	4.349	4.144	4.046	3.906	3.773	3.607	3.242	2.940	2.686	2.471
9	4.94	4.69	4.460	4.064	3.885	3.803	3.685	3.571	3.426	3.103	2.829	2.596	2.397
10	4.94	4.69	4.460	4.064	3.729	3.584	3.476	3.379	3.255	2.970	2.723	2.510	2.325
11	4.94	4.69	4.460	4.064	3.730	3.584	3.383	3.205	3.092	2.843	2.621	2.426	2.255
12	4.95	4.69	4.460	4.064	3.729	3.584	3.383	3.205	2.994	2.721	2.523	2.345	2.187
13	4.94	4.69	4.461	4.064	3.730	3.584	3.383	3.205	2.994	2.605	2.428	2.267	2.122
14	4.95	4.69	4.460	4.064	3.729	3.584	3.383	3.205	2.994	2.571	2.337	2.192	2.058
15	4.94	4.70	4.461	4.064	3.730	3.584	3.383	3.205	2.994	2.571	2.253	2.118	1.996
16	4.95	4.69	4.460	4.064	3.729	3.584	3.383	3.206	2.994	2.571	2.253	2.048	1.937
17	4.94	4.70	4.461	4.064	3.730	3.584	3.383	3.205	2.994	2.571	2.253	2.005	1.878
18	4.95	4.69	4.460	4.065	3.729	3.584	3.383	3.206	2.994	2.571	2.253	2.005	1.822
19	3.09	4.70	4.461	4.064	3.730	3.584	3.383	3.205	2.994	2.571	2.253	2.005	1.806
20		2.93	4.460	4.065	3.729	3.584	3.383	3.206	2.993	2.571	2.253	2.005	1.806
21			2.788	4.064	3.730	3.585	3.383	3.205	2.994	2.571	2.253	2.005	1.806
22				4.065	3.729	3.584	3.383	3.206	2.993	2.571	2.253	2.005	1.806
23				2.540	3.730	3.585	3.383	3.205	2.994	2.571	2.253	2.005	1.806
24					3.729	3.584	3.383	3.206	2.993	2.571	2.253	2.005	1.806
25					2.331	3.585	3.382	3.205	2.994	2.571	2.253	2.004	1.806
26						2.240	3.383	3.206	2.993	2.571	2.253	2.005	1.806
27							3.382	3.205	2.994	2.571	2.253	2.004	1.806
28							0.423	3.206	2.993	2.571	2.253	2.005	1.806
29								2.003	2.994	2.571	2.253	2.004	1.806
30									2.993	2.571	2.253	2.005	1.806
31									1.871	2.571	2.253	2.004	1.806
32										2.571	2.253	2.005	1.806
33										2.571	2.253	2.004	1.806
34										2.571	2.253	2.005	1.806
35										2.571	2.253	2.004	1.806
36										1.607	2.253	2.005	1.806
37											2.253	2.004	1.805
38											2.254	2.005	1.806
39											2.253	2.004	1.805
40											2.254	2.005	1.806
41											1.408	2.004	1.805
42												2.005	1.806
43												2.004	1.805
44												2.005	1.806
45												2.004	1.805
46												1.253	1.806
47													1.805
48													1.806
49													1.805
50													1.806
51													1.128

Table M 18:
150% Declining-Balance Method
Midquarter Convention
Property Placed in Service in Fourth Quarter

Year	Recovery periods in years												
	2.5	3	3.5	4	5	6	6.5	7	7.5	8	8.5	9	9.5
1	7.50%	6.25%	5.36%	4.69%	3.75%	3.13%	2.88%	2.68%	2.50%	2.34%	2.21%	2.08%	1.97%
2	55.50	46.88	40.56	35.74	28.88	24.22	22.41	20.85	19.50	18.31	17.26	16.32	15.48
3	26.91	25.00	23.18	22.34	20.21	18.16	17.24	16.39	15.60	14.88	14.21	13.60	13.03
4	10.09	21.87	22.47	19.86	16.40	14.06	13.26	12.87	12.48	12.09	11.70	11.33	10.98
5			8.43	17.37	16.41	14.06	13.10	12.18	11.41	10.74	10.16	9.65	9.24
6					14.35	14.06	13.10	12.18	11.41	10.75	10.16	9.65	9.17
7						12.31	13.10	12.19	11.41	10.74	10.16	9.64	9.17
8							4.91	10.66	11.41	10.75	10.16	9.65	9.17
9									4.28	9.40	10.17	9.64	9.17
10											3.81	8.44	9.18
11													3.44

Year	Recovery periods in years												
	10	10.5	11	11.5	12	12.5	13	13.5	14	15	16	16.5	17
1	1.88%	1.79%	1.70%	1.63%	1.56%	1.50%	1.44%	1.39%	1.34%	1.25%	1.17%	1.14%	1.10%
2	14.72	14.03	13.40	12.83	12.31	11.82	11.37	10.96	10.57	9.88	9.27	8.99	8.73
3	12.51	12.03	11.58	11.16	10.77	10.40	10.06	9.74	9.44	8.89	8.40	8.17	7.96
4	10.63	10.31	10.00	9.70	9.42	9.15	8.90	8.66	8.43	8.00	7.61	7.43	7.25
5	9.04	8.83	8.63	8.44	8.24	8.06	7.87	7.69	7.52	7.20	6.90	6.75	6.61
6	8.72	8.32	7.95	7.63	7.33	7.09	6.96	6.84	6.72	6.48	6.25	6.14	6.03
7	8.72	8.31	7.96	7.63	7.33	7.05	6.78	6.53	6.31	5.90	5.66	5.58	5.50
8	8.72	8.32	7.95	7.62	7.33	7.05	6.78	6.53	6.31	5.90	5.54	5.38	5.22
9	8.72	8.31	7.96	7.63	7.33	7.05	6.78	6.53	6.31	5.90	5.54	5.38	5.23
10	8.71	8.32	7.95	7.62	7.32	7.05	6.78	6.54	6.31	5.91	5.54	5.38	5.22
11	7.63	8.31	7.96	7.63	7.33	7.05	6.78	6.53	6.31	5.90	5.54	5.38	5.23
12		3.12	6.96	7.62	7.32	7.04	6.78	6.54	6.30	5.91	5.55	5.38	5.22
13				2.86	6.41	7.05	6.78	6.53	6.31	5.90	5.54	5.38	5.23
14						2.64	5.94	6.54	6.30	5.91	5.55	5.38	5.22
15								2.45	5.52	5.90	5.54	5.37	5.23
16										5.17	5.55	5.38	5.22
17											4.85	5.37	5.23
18												2.02	4.57

Table M 18 (Continued)

Year	Recovery periods in years												
	18	19	20	22	24	25	26.5	28	30	35	40	45	50
1	1.04%	0.99%	0.938%	0.852%	0.781%	0.750%	0.708%	0.670%	0.625%	0.536%	0.469%	0.417%	0.375%
2	8.25	7.82	7.430	6.760	6.201	5.955	5.620	5.321	4.969	4.263	3.732	3.319	2.989
3	7.56	7.20	6.872	6.299	5.814	5.598	5.302	5.036	4.720	4.080	3.592	3.209	2.899
4	6.93	6.63	6.357	5.870	5.450	5.262	5.002	4.766	4.484	3.905	3.458	3.102	2.812
5	6.35	6.11	5.880	5.469	5.110	4.946	4.719	4.511	4.260	3.738	3.328	2.998	2.728
6	5.82	5.63	5.439	5.097	4.790	4.649	4.452	4.269	4.047	3.578	3.203	2.898	2.646
7	5.34	5.18	5.031	4.749	4.491	4.370	4.200	4.041	3.845	3.424	3.083	2.802	2.567
8	4.94	4.77	4.654	4.425	4.210	4.108	3.962	3.824	3.653	3.278	2.968	2.708	2.490
9	4.94	4.69	4.458	4.124	3.947	3.862	3.738	3.619	3.470	3.137	2.856	2.618	2.415
10	4.94	4.69	4.458	4.062	3.730	3.630	3.526	3.426	3.296	3.003	2.749	2.531	2.342
11	4.95	4.69	4.458	4.062	3.729	3.582	3.383	3.242	3.132	2.874	2.646	2.447	2.272
12	4.94	4.69	4.458	4.062	3.730	3.582	3.382	3.204	2.994	2.751	2.547	2.365	2.204
13	4.95	4.69	4.458	4.062	3.729	3.582	3.383	3.204	2.994	2.633	2.451	2.286	2.138
14	4.94	4.69	4.458	4.061	3.730	3.582	3.382	3.204	2.994	2.570	2.359	2.210	2.074
15	4.95	4.69	4.458	4.062	3.729	3.582	3.383	3.204	2.994	2.571	2.271	2.136	2.011
16	4.94	4.69	4.458	4.061	3.730	3.583	3.382	3.204	2.994	2.570	2.253	2.065	1.951
17	4.95	4.68	4.458	4.062	3.729	3.582	3.383	3.204	2.994	2.571	2.253	2.005	1.893
18	4.94	4.69	4.459	4.061	3.730	3.583	3.382	3.204	2.994	2.570	2.253	2.005	1.836
19	4.33	4.68	4.458	4.062	3.729	3.582	3.383	3.204	2.993	2.571	2.253	2.005	1.806
20		4.10	4.459	4.061	3.730	3.583	3.382	3.204	2.994	2.570	2.253	2.005	1.806
21			3.901	4.062	3.729	3.582	3.383	3.204	2.993	2.571	2.253	2.005	1.806
22				4.061	3.730	3.583	3.382	3.204	2.994	2.570	2.253	2.005	1.806
23				3.554	3.729	3.582	3.383	3.205	2.993	2.571	2.253	2.005	1.806
24					3.730	3.583	3.382	3.204	2.994	2.570	2.253	2.005	1.805
25					3.263	3.582	3.383	3.205	2.993	2.571	2.253	2.005	1.806
26						3.135	3.382	3.204	2.994	2.570	2.252	2.005	1.805
27							3.383	3.205	2.993	2.571	2.253	2.004	1.806
28							1.268	3.204	2.994	2.570	2.252	2.005	1.805
29								2.804	2.993	2.571	2.253	2.004	1.806
30									2.994	2.570	2.252	2.005	1.805
31									2.619	2.571	2.253	2.004	1.806
32										2.570	2.252	2.005	1.805
33										2.571	2.253	2.004	1.806
34										2.570	2.252	2.005	1.805
35										2.571	2.253	2.004	1.806
36										2.249	2.252	2.005	1.805
37											2.253	2.004	1.806
38											2.252	2.005	1.805
39											2.253	2.004	1.806
40											2.252	2.005	1.805
41											1.971	2.004	1.806
42												2.005	1.805
43												2.004	1.806
44												2.005	1.805
45												2.004	1.806
46												1.754	1.805
47													1.806
48													1.805
49													1.806
50													1.805
51													1.580

ACRS Percentage Tables

ACRS 15-Year Real Property* (Other Than Low-Income Housing)			
Metod	**Life**	**Table**	**Page**
Regular ACRS	15	A 1	page VI-43
Alternate ACRS	35	A 11	page VI-46
Alternate ACRS	45	A 15	page VI-47

* 15-year ACRS real property was generally placed in service after 12/31/80 and before 3/16/84.

ACRS Low-Income Housing*				
Placed in Service	**Metod**	**Life**	**Table**	**Page**
Before 5/09/85	Regular ACRS	15	A 2	page VI-43
After 5/08/85	Regular ACRS	15	A 3	page VI-44
Before 5/09/85	Alternate ACRS	35	A 11	page VI-46
After 5/08/85	Alternate ACRS	35	A 12	page VI-46
After 12/31/80	Alternate ACRS	45	A 15	page VI-47

* Although ACRS low-income housing covers such property placed in service after 1980 and before 1987, there was a rate change effective May 9, 1985. This rate change did not affect ACRS low-income housing for which Alternate ACRS depreciation was elected over a 45-year life.

ACRS 18-Year Real Property*				
Placed in Service	**Metod**	**Life**	**Table**	**Page**
After 3/15/84 & Before 6/23/84	Regular ACRS	18	A 5	page VI-44
After 6/22/84	Regular ACRS	18	A 4	page VI-44
After 3/15/84 & Before 6/23/84	Alternate ACRS	18	A 8	page VI-45
After 6/22/84	Alternate ACRS	18	A 7	page VI-45
After 3/15/84 & Before 6/23/84	Alternate ACRS	35	A 11	page VI-46
After 6/22/84	Alternate ACRS	35	A 10	page VI-46
After 3/15/84 & Before 6/23/84	Alternate ACRS	45	A 15	page VI-47
After 6/22/84	Alternate ACRS	45	A 14	page VI-47

* 18-year ACRS real property was generally placed in service after 3/15/84 and before 5/9/85. There was a rate change effective June 23, 1984.

ACRS 19-Year Real Property*			
Metod	**Life**	**Table**	**Page**
Regular ACRS	19	A 6	page VI-45
Alternate ACRS	19	A 9	page VI-46
Alternate ACRS	35	A 13	page VI-47
Alternate ACRS	45	A 14	page VI-47

* 19-year ACRS real property was generally placed in service after 5/08/85 and before 1987.

Table A 1:
15-Year Real Property* (Other Than Low-Income Housing)

Year	Month Placed In Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	12.0%	11.0%	10.0%	9.0%	8.0%	7.0%	6.0%	5.0%	4.0%	3.0%	2.0%	1.0%
2nd	10.0	10.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	12.0
3rd	9.0	9.0	9.0	9.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
4th	8.0	8.0	8.0	8.0	8.0	8.0	9.0	9.0	9.0	9.0	9.0	9.0
5th	7.0	7.0	7.0	7.0	7.0	7.0	8.0	8.0	8.0	8.0	8.0	8.0
6th	6.0	6.0	6.0	6.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
7th	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
8th	6.0	6.0	6.0	6.0	6.0	6.0	5.0	6.0	6.0	6.0	6.0	6.0
9th	6.0	6.0	6.0	6.0	5.0	6.0	5.0	5.0	5.0	6.0	6.0	6.0
10th	5.0	6.0	5.0	6.0	5.0	5.0	5.0	5.0	5.0	5.0	6.0	5.0
11th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
12th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
13th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
14th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
15th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
16th	—	—	1.0	1.0	2.0	2.0	3.0	3.0	4.0	4.0	4.0	5.0

* Placed In Service After 1980 and Before March 16, 1984

Table A 2:
Low-Income Housing*

Year	Month Placed In Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	13.0%	12.0%	11.0%	10.0%	9.0%	8.0%	7.0%	6.0%	4.0%	3.0%	2.0%	1.0%
2nd	12.0	12.0	12.0	12.0	12.0	12.0	12.0	13.0	13.0	13.0	13.0	13.0
3rd	10.0	10.0	10.0	10.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0
4th	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	10.0	10.0	10.0	10.0
5th	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	9.0
6th	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
7th	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
8th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	6.0	6.0
9th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
10th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
11th	4.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
12th	4.0	4.0	4.0	5.0	4.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
13th	4.0	4.0	4.0	4.0	4.0	4.0	5.0	4.0	5.0	5.0	5.0	5.0
14th	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	5.0	4.0	4.0
15th	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
16th	—	—	1.0	1.0	2.0	2.0	2.0	3.0	3.0	3.0	4.0	4.0

* Placed In Service After 1980 and Before May 9, 1985

Table A 3:
Low-Income Housing*

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	13.3%	12.2%	11.1%	10.0%	8.9%	7.8%	6.6%	5.6%	4.4%	3.3%	2.2%	1.1%
2nd	11.6	11.7	11.9	12.0	12.1	12.3	12.5	12.6	12.7	12.9	13.0	13.2
3rd	10.0	10.1	10.2	10.4	10.5	10.7	10.8	10.9	11.1	11.2	11.3	11.4
4th	8.7	8.8	8.9	9.0	9.1	9.2	9.3	9.5	9.6	9.7	9.8	9.9
5th	7.5	7.6	7.7	7.8	7.9	8.0	8.1	8.2	8.3	8.4	8.5	8.6
6th	6.5	6.6	6.7	6.8	6.9	6.9	7.0	7.1	7.2	7.3	7.4	7.4
7th	5.7	5.7	5.8	5.9	5.9	6.0	6.1	6.1	6.2	6.3	6.4	6.5
8th	4.9	5.0	5.0	5.1	5.2	5.2	5.3	5.3	5.4	5.5	5.5	5.6
9th	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.7	4.8	4.8
10th	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
11th	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
12th	4.5	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
13th	4.5	4.5	4.6	4.5	4.6	4.6	4.6	4.6	4.6	4.5	4.6	4.6
14th	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.6	4.6	4.5	4.5	4.5
15th	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5
16th		0.4	0.7	1.1	1.5	1.9	2.3	2.6	3.0	3.4	3.7	4.1

* Placed In Service After May 8, 1985, and Before 1987

Table A 4:
18-Year Real Property*

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	9.0%	9.0%	8.0%	7.0%	6.0%	5.0%	4.0%	4.0%	3.0%	2.0%	1.0%	0.4%
2nd	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	10.0	10.0	10.0
3rd	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	9.0	9.0	9.0	9.0
4th	7.0	7.0	7.0	7.0	7.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
5th	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
6th	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
7th	5.0	5.0	5.0	5.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
8-12th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
13th	4.0	4.0	4.0	5.0	4.0	4.0	5.0	4.0	4.0	4.0	5.0	5.0
14-17th	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
18th	4.0	3.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
19th		1.0	1.0	1.0	2.0	2.0	2.0	3.0	3.0	3.0	3.0	3.6

* Placed In Service After June 22, 1984, and Before May 9, 1985

Table A 5:
18-Year Real Property*

Year	Month Placed in Service										
	1	2	3	4	5	6	7	8	9	10-11	12
1st	10.0%	9.0%	8.0%	7.0%	6.0%	6.0%	5.0%	4.0%	3.0%	2.0%	1.0%
2nd	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	10.0	10.0
3rd	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	9.0	9.0	9.0
4th	7.0	7.0	7.0	7.0	7.0	7.0	8.0	8.0	8.0	8.0	8.0
5th	6.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
6th	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
7th	5.0	5.0	5.0	5.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
8-12th	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
13th	4.0	4.0	4.0	5.0	5.0	4.0	4.0	5.0	4.0	4.0	4.0
14-18th	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
19th			1.0	1.0	1.0	2.0	2.0	2.0	3.0	3.0	4.0

* Placed In Service After March 15 and Before June 23, 1984

Table A 6:
19-Year Real Property*

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	8.8%	8.1%	7.3%	6.5%	5.8%	5.0%	4.2%	3.5%	2.7%	1.9%	1.1%	0.4%
2nd	8.4	8.5	8.5	8.6	8.7	8.8	8.8	8.9	9.0	9.0	9.1	9.2
3rd	7.6	7.7	7.7	7.8	7.9	7.9	8.0	8.1	8.1	8.2	8.3	8.3
4th	6.9	7.0	7.0	7.1	7.1	7.2	7.3	7.3	7.4	7.4	7.5	7.6
5th	6.3	6.3	6.4	6.4	6.5	6.5	6.6	6.6	6.7	6.8	6.8	6.9
6th	5.7	5.7	5.8	5.9	5.9	5.9	6.0	6.0	6.1	6.1	6.2	6.2
7th	5.2	5.2	5.3	5.3	5.3	5.4	5.4	5.5	5.5	5.6	5.6	5.6
8th	4.7	4.7	4.8	4.8	4.8	4.9	4.9	5.0	5.0	5.1	5.1	5.1
9th	4.2	4.3	4.3	4.4	4.4	4.5	4.5	4.5	4.5	4.6	4.6	4.7
10-19th	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
20th	0.2	0.5	0.9	1.2	1.6	1.9	2.3	2.6	3.0	3.3	3.7	4.0

* Placed In Service After May 8, 1985, and Before 1987

Table A 7:
18-Year Real Property*

Year	Month Placed in Service					
	1-2	3-4	5-7	8-9	10-11	12
1st	5.0%	4.0%	3.0%	2.0%	1.0%	0.2%
2-10th	6.0	6.0	6.0	6.0	6.0	6.0
11th	5.0	5.0	5.0	5.0	5.0	5.8
12-18th	5.0	5.0	5.0	5.0	5.0	5.0
19th	1.0	2.0	3.0	4.0	5.0	5.0

* Placed In Service After June 22, 1984
If Alternate ACRS Method Elected Over 18-Year Period

Table A 8:
18-Year Real Property*

Year	Month Placed in Service						
	1	2-3	4-5	6-7	8-9	10-11	12
1st	6.0%	5.0%	4.0%	3.0%	2.0%	1.0%	0.5%
2-10th	6.0	6.0	6.0	6.0	6.0	6.0	6.0
11th	5.0	5.0	5.0	5.0	5.0	5.0	5.5
12-18th	5.0	5.0	5.0	5.0	5.0	5.0	5.0
19th		1.0	2.0	3.0	4.0	5.0	5.0

* Placed In Service After March 15 and Before June 23, 1984
If Alternate ACRS Method Elected Over 18-Year Period

Table A 9:
19-Year Real Property*

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	5.0%	4.6%	4.2%	3.7%	3.3%	2.9%	2.4%	2.0%	1.5%	1.1%	0.7%	0.2%
2-13th	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
14-19th	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
20th	0.2	0.6	1.0	1.5	1.9	2.3	2.8	3.2	3.7	4.1	4.5	5.0

* If Alternate ACRS Method Elected Over 19-Year Period

Table A 10:
18-Year Real Property*

Year	Month Placed in Service				
	1-2	3-6	7-10	11	12
1st	3.0%	2.0%	1.0%	0.4%	0.1%
2-30th	3.0	3.0	3.0	3.0	3.0
31st	2.0	2.0	2.0	2.6	2.9
32-35th	2.0	2.0	2.0	2.0	2.0
36th		1.0	2.0	2.0	2.0

* Placed In Service After June 22, 1984
If Alternate ACRS Method Elected Over 35-Year Period

Table A 11:
18-Year Real Property[1]
15-Year Real Property and Low-Income Housing[2]

Year	Month Placed in Service		
	1-2	3-6	7-12
1st	3.0%	2.0%	1.0%
2-30th	3.0	3.0	3.0
31-35th	2.0	2.0	2.0
36th		1.0	2.0

[1] Placed In Service After March 15 and Before June 23, 1984
[2] Placed In Service Before May 9, 1985
If Alternate ACRS Method Elected Over 35-Year Period

Table A 12:
Low-Income Housing*

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	2.9%	2.6%	2.4%	2.1%	1.9%	1.7%	1.4%	1.2%	1.0%	0.7%	0.5%	0.2%
2-20th	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
21-35th	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
36th		0.3	0.5	0.8	1.0	1.2	1.5	1.7	1.9	2.2	2.4	2.7

*Placed In Service after May 8, 1985
If Alternate ACRS Method Elected Over 35-Year Period

Table A 13:
19-Year Real Property*

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	2.7%	2.5%	2.3%	2.0%	1.8%	1.5%	1.3%	1.1%	0.8%	0.6%	0.4%	0.1%
2-20th	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
21-35th	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
36th	0.2	0.4	0.6	0.9	1.1	1.4	1.6	1.8	2.1	2.3	2.5	2.8

*If Alternate ACRS Method Elected Over 35-Year Period

Table A 14:
18-Year Real Property[1]
19-Year Real Property

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	2.1%	1.9%	1.8%	1.6%	1.4%	1.2%	1.0%	0.8%	0.6%	0.5%	0.3%	0.1%
2-11th	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
12-45th	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
46th	0.1	0.3	0.4	0.6	0.8	1.0	1.2	1.4	1.6	1.7	1.9	2.1

[1]Placed In Service After June 22, 1984
If Alternate ACRS Method Elected Over a 45-Year Period

Table A 15:
18-Year Real Property[1]
15-Year Real Property and Low-Income Housing[2]

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	2.3%	2.0%	1.9%	1.7%	1.5%	1.3%	1.2%	0.9%	0.7%	0.6%	0.4%	0.2%
2-10th	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
11-45th	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
46th		0.3	0.4	0.6	0.8	1.0	1.1	1.4	1.6	1.7	1.9	2.1

[1]Placed In Service After March 15 and Before June 23, 1984
[2]Placed In Service After December 31, 1980
If Alternate ACRS Method Elected Over a 45-Year Period

Tables for Listed Property

Method	Type of Property	Table	Page
ACRS	Owned	ALP 1 & 2	page VI-49
MACRS	Owned	M 8—12	page VI-21
ACRS	Leased (other than cars)	ALL 1 & 2	page VI-50
MACRS	Leased (other than cars)	MLL 1 & 2	page VI-51

Table ALP 1:
Listed Property Not Used Predominantly (Other Than 18- or 19-Year Real Property)

Year	Recovery Period		
	5	12	25
1st	10.0%	4.0%	2.0%
2nd-5th	20.0	9.0	4.0
6th	10.0	8.0	4.0
7th-12th	—	8.0	4.0
13th	—	4.0	4.0
14th-25th	—	—	4.0
26th	—	—	2.0

Table ALP 2:
40-Year Recovery Period (For 18- or 19-Year Listed Property Not Used Predominantly)

Year	Month Placed in Service											
	1	2	3	4	5	6	7	8	9	10	11	12
1st	2.4%	2.2%	2.0%	1.8%	1.6%	1.4%	1.1%	0.9%	0.7%	0.5%	0.3%	0.1%
2-40th	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
41st	0.1	0.3	0.5	0.7	0.9	1.1	1.4	1.6	1.8	2.0	2.2	2.4

Table ALL 1:
5-Year Recovery Property

Lease Term	Tax year during the lease term that the business percentage decreases to 50% or less											
	1	2	3	4	5	6	7	8	9	10	11	12
1 Year	2.7%											
2 Years	5.3	1.2%										
3 Years	9.9	6.1	1.6%									
4 Years	14.4	11.1	7.3	2.3%								
5 Years	18.4	15.7	12.4	8.2	3.0%							
6 Years or more	21.8	19.6	16.7	13.5	9.6	5.25%	4.4%	3.6%	2.8%	1.8%	1.0%	0%

Table ALL 2:
10-Year Recovery Property

Lease Term	Tax year during the lease term that the business percentage decreases to 50% or less														
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1 Year	2.5%														
2 Years	5.1	0.6%													
3 Years	9.8	5.6	1.0%												
4 Years	14.0	10.3	6.2	1.4%											
5 Years	17.9	14.5	10.9	6.7	1.8%										
6 Years	21.3	18.3	15.1	11.4	7.1	2.1%									
7 Years	21.9	19.0	15.9	12.4	8.4	3.9	2.4%								
8 Years	22.4	19.6	16.7	13.4	9.7	5.5	4.5	2.7%							
9 Years	22.9	20.2	17.4	14.3	10.9	7.0	6.4	5.1	3.0%						
10 Years	23.5	20.9	18.2	15.2	11.9	8.3	8.1	7.2	5.7	3.3%					
11 Years	23.9	21.4	18.8	16.0	12.8	9.3	9.4	8.9	7.7	5.9	3.1%				
12 Years	24.3	21.9	19.3	16.5	13.4	10.1	10.3	10.0	9.3	7.8	5.5	2.9%			
13 Years	24.7	22.2	19.7	16.9	14.0	10.7	11.1	11.0	10.4	9.2	7.4	5.2	2.7%		
14 Years	25.0	22.5	20.1	17.3	14.4	11.1	11.6	11.7	11.3	10.3	8.8	6.9	4.8	2.5%	
15 Years or more	25.3	22.8	20.3	17.5	14.7	11.5	12.0	12.2	11.9	11.1	9.8	8.2	6.5	4.5	2.3%

Table MLL 1:
Rates To Figure Inclusion Amounts for Leased Listed Property
Amount A Percentages

Recovery Period of Property Under ADS	First Tax Year During Lease In Which Business Use Is 50% or Less											
	1	2	3	4	5	6	7	8	9	10	11	12 & Later
Less than 7 years	2.1%	−7.2%	−19.8%	−20.1%	−12.4%	−12.4%	−12.4%	−12.4%	−12.4%	−12.4%	−12.4%	−12.4%
7 to 10 years	3.9%	−3.8%	−17.7%	−25.1%	−27.8%	−27.2%	−27.1%	−27.6%	−23.7%	−14.7%	−14.7%	−14.7%
More than 10 years	6.6%	−1.6%	−16.9%	−25.6%	−29.9%	−31.1%	−32.8%	−35.1%	−33.3%	−26.7%	−19.7%	−12.2%

Table MLL 2:
Rates To Figure Inclusion Amounts for Leased Listed Property
Amount B Percentages

Recovery Period of Property Under ADS	First Tax Year During Lease In Which Business Use Is 50% or Less											
	1	2	3	4	5	6	7	8	9	10	11	12 & Later
Less than 7 years	0.0%	10.0%	22.0%	21.2%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%	12.7%
7 to 10 years	0.0%	9.3%	23.8%	31.3%	33.8%	32.7%	31.6%	30.5%	25.0%	15.0%	15.0%	15.0%
More than 10 years	0.0%	10.1%	26.3%	35.4%	39.6%	40.2%	40.8%	41.4%	37.5%	29.2%	20.8%	12.5%

Section VII: Quick Reference

In this section:

IRS Code Sections and Regulations

This Quick Reference is a useful listing of the IRS Code sections and regulations that relate to depreciation. The list is presented in two ways:

- Numerically by the IRS Code section, and
- Alphabetically, using key words.

This reference guide will assist you when you need an IRS Code cite or when you want to read something first-hand. It is important to remember, however, that when reading any section of the IRS Code, there is always the possibility that another section or regulation of the Code may either supersede or add additional meaning to the one you are presently reading. The only way you will know whether such a section or regulation exists, however, is either to read the *entire* IRS Code or to depend on reference books such as this one.

We have listed both the IRS Code Sections and the IRS Regulations. You can easily identify the regulations, as they are formatted with the code section, preceded by "1." In other words, the IRS regulations for IRS Code Section 168, are stated as "1.168 etc."

For IRS Code Section 167, we have only listed the IRS Regulations and have not included the code section itself. Section 167 has, for the most part, been either repealed or amended. The regulations are both more detailed and easier to understand.

IRS Code Sections and Regulations in Numerical Order

IRS Code Sec. or Reg.	Brief Description — Numerical Order
29	Nonconventional Fuel Production Credit
30	Electric Vehicles Tax Credit
30B	Alternative Motor Vehicle Credit for Fuel Cell, Hybrid, Lean Burn Technology, and Alternative Fuel Vehicles
38	General Business Credit (Replaced Investment Credit Code Section)
38(b)	Qualified Alternative Fuel Vehicle Refueling Property
38(b)(23)	Energy Efficient Home Credit Available to Eligible Contractors
38(b)(24)	Business Tax Credit for Manufacturers of Energy Efficient Dishwashers, Clothes Washers, and Refrigerators
46	Tax Credit for Investment in Certain Property
46(3)	Investment Tax Credit Expanded for Qualified Investment in a Qualifying Advanced Coal Project
46(4)	Investment Tax Credit Expanded for Qualified Investment in a Qualifying Gasification Property
48(a)(1)	Qualified Microturbine Property Energy Credit; Qualified Fuel Cell Property Energy Credit
56	Alternative Minimum Tax Adjustments
56(g)	Adjusted Current Earnings (See also ACE)
56(g)(1)	ACE – Overview
56(g)(2)	ACE – Negative adjustments allowed
56(g)(3)	ACE – Definition
56(g)(4)	ACE – Adjustments
56(g)(4)(A)	ACE – Depreciation – Adjustments
56(g)(4)(A)	ACE – Depreciation – MACRS Post-1989 Property (i)
56(g)(4)(A)	ACE – Depreciation – MACRS Pre-1990 Property (ii)
56(g)(4)(A)	ACE – Depreciation – ACRS Property (iii)

IRS Code Sec. or Reg.	Brief Description — Numerical Order
56(g)(4)(A)	ACE – Depreciation – Pre-1981 Property (iv)
56(g)(4)(A)	ACE – Depreciation – Special Rules for Certain Property (v)
1.56(g)-1	Adjusted Current Earnings (See also ACE)
1.56(g)-1(a)	ACE – Overview
1.56(g)-1(b)	ACE – Depreciation
1.56(g)-1(b)	ACE – Depreciation – MACRS Post-1989 Property (1)
1.56(g)-1(b)	ACE – Depreciation – MACRS Pre-1990 Property (2)
1.56(g)-1(b)	ACE – Depreciation – ACRS Property (3)
1.56(g)-1(b)	ACE – Depreciation – Special Rules for Certain Property (4)
1.56(g)-1(b)	ACE – Depreciation – Excluded Property (5)
57	Tax Preference Items
1.162-3	Materials and Supplies
1.167(a)-1	Depreciation in General
1.167(a)-1(A)	Reasonable Allowance
1.167(a)-1(B)	Useful Life
1.167(a)-1(C)	Salvage
1.167(a)-2	Tangible Property
1.167(a)-3	Intangibles
1.167(a)-4	Leased Property
1.167(a)-5	Apportionment of Basis
1.167(a)-6(A)	Copyrights
1.167(a)-6(A)	Patents
1.167(a)-6(B)	Farmers
1.167(a)-7	Accounting for Depreciable Property
1.167(a)-7(A)	Accounting – Grouping Assets By Account
1.167(a)-7(B)	Accounting – Composite Asset Accounts
1.167(a)-8	Retirements of Assets

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1.167(a)-9	Obsolescence
1.167(a)-10	Timing of Depreciation – When Is It Allowable?
1.167(a)-11	ADR – Asset Depreciation Range System
1.167(a)-11(a)	ADR – Overview
1.167(a)-11(b)	ADR – Depreciation Ranges' Reasonable Allowance
1.167(a)-11(c)	ADR – Manner of Determining Depreciation Allowance
1.167(a)-11(d)	ADR – Rules for Salvage, Repairs, and Retirements
1.167(a)-11(e)	ADR – Accounting for Eligible ADR Property
1.167(a)-11(f)	ADR – Electing ADR for Eligible Property
1.167(a)-11(g)	ADR – Relationship to Useful Life and Straight-Line Depreciation
1.167(a)-12	Pre-1971 Assets
1.167(a)-12(a)	Pre-1971 Assets – Generally
1.167(a)-12(b)	Pre-1971 Assets – Determination of Class Lives
1.167(a)-12(c)	Pre-1971 Assets – Salvage Value
1.167(a)-12(d)	Pre-1971 Assets – Accounting for Eligible Property
1.167(a)-12(e)	Pre-1971 Assets – Election for Tax Years Ending After 1970
1.167(a)-12(f)	Pre-1971 Assets – Depreciation for Tax Years Ending Before 1971
1.167(b)-0	Methods of Computing Depreciation – Overview
1.167(b)-1	Methods – Straight-Line
1.167(b)-2	Methods – Declining-Balance
1.167(b)-3	Methods – Sum-of-the-Years'-Digits
1.167(b)-4	Methods – Miscellaneous Methods
1.167(c)	Methods – Limitations on Methods Under 167(b)-2, 3 and 4
1.167(d)	Useful Life and Rates of Depreciation Agreement
1.167(e)	Change in Method
1.167(f)	Salvage Value – Reduction for Personal Property
1.167(g)	Basis for Depreciation
1.167(h)	Trusts and Estates – Life Tenants and Beneficiaries
1.167(i)	Mining, Oil and Gas Wells, and Other Natural Deposits
1.167(j)	Accelerated Depreciation – Limitations for Real Property

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1.167(k)	Rehabilitation Expenditures – Depreciation on Property
1.167(l)	Public Utilities – Limitations on Depreciation
1.167(m)	ADR – Class Lives
168(a)	MACRS – General
168(b)	MACRS – Methods of Depreciation
168(c)	MACRS – Recovery Periods
168(d)	MACRS – Conventions (Averaging Conventions)
168(d)(1)	MACRS – Conventions – Half-Year
168(d)(2)	MACRS – Conventions – Midmonth
168(d)(3)	MACRS – Conventions – Midquarter (MQ)
168(d)(4)	MACRS – Conventions – Definitions
168(e)	MACRS – Classification of Property
168(e)(1)	MACRS – Classification of Property – Overview
168(e)(2)(A)	MACRS – Classification of Property – Residential Rental
168(e)(2)(B)	MACRS – Classification of Property – Nonresidential
168(e)(3)(A)	MACRS – Classification of Property – 3-Year
168(e)(3)(B)	MACRS – Classification of Property – 5-Year
168(e)(3)(C)	MACRS – Classification of Property – 7-Year
168(e)(3)(D)	MACRS – Classification of Property – 10-Year
168(e)(3)(E)	MACRS – Classification of Property – 15-Year
168(e)(4)	MACRS – Classification of Property – Railroad Grading and Tunnel Bores
168(e)(5)	MACRS – Classification of Property – Water Utility Property
168(f)	MACRS – Excluded Property
168(f)(1)	MACRS – Excluded Property – Certain Methods of Depreciation
168(f)(2)	MACRS – Excluded Property – Certain Public Utility Property
168(f)(3)	MACRS – Excluded Property – Films and Videotapes
168(f)(4)	MACRS – Excluded Property – Sound Recordings
168(f)(5)	MACRS – Excluded Property – Churning Transactions
168(g)	MACRS – ADS

IRS Code Sec. or Reg.	Brief Description — Numerical Order
168(g)(1)	MACRS – ADS – Overview
168(g)(2)	MACRS – ADS – Method, Conventions, Recovery Periods
168(g)(3)	MACRS – ADS – Class Life Rules
168(g)(4)	MACRS – ADS – Property Used Outside of U.S.
168(g)(5)	MACRS – ADS – Tax-Exempt Financed Property
168(g)(6)	MACRS – ADS – Imported Property
168(g)(7)	MACRS – ADS – Election
168(h)	MACRS – Tax-Exempt Use Property
168(h)(1)	MACRS – Tax-Exempt Use – Overview
168(h)(2)	MACRS – Tax-Exempt Use – Tax-Exempt Entity
168(h)(3)	MACRS – Tax-Exempt Use – High Technology Equipment
168(h)(4)	MACRS – Tax-Exempt Use – Related Entities
168(h)(5)	MACRS – Tax-Exempt Use – Property Leased to Partnerships, etc.
168(h)(6)	MACRS – Tax-Exempt Use – Property Owned by Partnerships, etc.
168(i)	MACRS – Definitions and Special Rules
168(i)(1)	MACRS – Definition – Class Life
168(i)(2)(A)	MACRS – Definition – Qualified Technological Equipment
168(i)(2)(B)	MACRS – Definition – Computer and Peripheral Equipment
168(i)(2)(C)	MACRS – Definition – High Technology Medical Equipment
168(i)(3)	MACRS – Special Rules – Lease Term
168(i)(4)	MACRS – Special Rules – General Asset Accounts
168(i)(5)	MACRS – Special Rules – Changes in Use
168(i)(6)	MACRS – Special Rules – Improvements or Additions
168(i)(7)	MACRS – Special Rules – Transferees
168(i)(8)	MACRS – Special Rules – Leasehold Improvements
168(i)(9)	MACRS – Special Rules – Normalization Method of Accounting
168(i)(10)	MACRS – Special Rules – Public Utility Property
168(i)(11)	MACRS – Definition – Research and Experimentation
168(i)(12)	MACRS – Definition – Section 1245 and 1250 Property
168(i)(13)	MACRS – Definition – Single-Purpose Agricultural and Horticultural Structure and Livestock

IRS Code Sec. or Reg.	Brief Description — Numerical Order
168(j)	MACRS – Indian Reservation Property
168(j)(1)	MACRS – Indian Reservation Property – General
168(j)(2)	MACRS – Indian Reservation Property – Applicable Recovery Period
168(j)(3)	MACRS – Indian Reservation Property – AMT Adjustment
168(j)(4)	MACRS – Indian Reservation Property – Qualifying Property
168(j)(5)	MACRS – Indian Reservation Property – Real Estate Rentals
168(j)(6)	MACRS – Indian Reservation Property – Definition of Indian Reservation
168(j)(7)	MACRS – Indian Reservation Property – Coordination with non-revenue laws
168(j)(8)	MACRS – Indian Reservation Property – Termination
168(k)	MACRS – Special Allowance
168(k)(1)	MACRS – Additional Allowance
168(k)(2)	MACRS – Qualified Property
168(k)(3)	MACRS – Qualified Leasehold Improvement Property
168(k)(4)	MACRS – 50% Bonus Depreciation
168(k)(5)	MACRS - Special Rules for Certain Plants bearing Fruits and Nuts
168(k)(6)	MACRS - Phase Down of Bonus Depreciation
1.168-1	ACRS – Overview
1.168-2	ACRS – Deduction for Depreciation
1.168-2(a)	ACRS – Deduction – Computation
1.168-2(b)	ACRS – Deduction – Applicable Percentage
1.168-2(c)	ACRS – Deduction – Alternate ACRS – Straight-Line Method
1.168-2(d)	ACRS – Deduction – Unadjusted Basis
1.168-2(e)	ACRS – Deduction – Components and Improvements
1.168-2(f)	ACRS – Deduction – Short Tax Years
1.168-2(g)	ACRS – Deduction – Property Used Outside of U.S.
1.168-2(h)	ACRS – Deduction – Mass Asset Accounts
1.168-2(i)	ACRS – Deduction – **Reserved by IRS**
1.168-2(j)	ACRS – Deduction – Changes in Use
1.168-2(k)	ACRS – Deduction – Accrues Ratably Over Year

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1.168-2(l)	ACRS – Deduction – Definitions
1.168-2(l)(1)	ACRS – Deduction – Definition – Disposition
1.168-2(l)(2)	ACRS – Deduction – Definition – Placed in Service
1.168-2(l)(3)	ACRS – Deduction – Definition – Recovery Year
1.168-2(l)(4)	ACRS – Deduction – Definition – Recovery Period
1.168-2(m)	ACRS – Deduction – Industrial Development Bonds
1.168-2(n)	ACRS – Deduction – Basis of Partnership Property
1.168-3	ACRS – Property (Recovery Property)
1.168-3(a)	ACRS – Property – Overview
1.168-3(b)	ACRS – Property – Classes of Recovery Property
1.168-3(c)	ACRS – Property – Definitions
1.168-3(c)(1)	ACRS – Property – Definition – 3-Year Property
1.168-3(c)(2)	ACRS – Property – Definition – 5-Year Property
1.168-3(c)(3)	ACRS – Property – Definition – 10-Year Property
1.168-3(c)(4)	ACRS – Property – Definition – 15-Year Property
1.168-3(c)(5)	ACRS – Property – Definition – 15-Year Public Utility
1.168-3(c)(6)	ACRS – Property – Definition – Section 1245 Property
1.168-3(c)(7)	ACRS – Property – Definition – Section 1250 Property
1.168-3(c)(8)	ACRS – Property – Definition – Present Class Life
1.168-3(c)(9)	ACRS – Property – Definition – Coal Utilization Property
1.168-3(c)(10)	ACRS – Property – Definition – Public Utility Property
1.168-3(c)(11)	ACRS – Property – Definition – Original Use
1.168-4	ACRS – Excluded Property
1.168-4(a)	ACRS – Excluded Property – Pre-1981 Property
1.168-4(b)	ACRS – Excluded Property – Certain Methods of Depreciation
1.168-4(c)	ACRS – Excluded Property – Public Utility Property
1.168-4(d)	ACRS – Excluded Property – Churning Transactions
1.168-5	Retirement-Replacement-Betterment (RRB) Property
1.168-6	ACRS – Dispositions: Gain or Loss Recognized
1.168(d)-1	MACRS – Conventions (Averaging Conventions)

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1.168(d)-1(a)	MACRS – Conventions – Overview
1.168(d)-1(b)	MACRS – Conventions – Midquarter (MQ)
1.168(d)-1(b)	MACRS – Conventions – MQ – Listed Property (2)
1.168(d)-1(b)	MACRS – Conventions – MQ – Placed in Service and Disposed of in Same Year (3)
1.168(d)-1(b)	MACRS – Conventions – MQ – Aggregate Basis of Property (4)
1.168(d)-1(b)	MACRS – Conventions – MQ – Affiliated Groups (5)
1.168(d)-1(b)	MACRS – Conventions – MQ – S Corporations and Partnerships (6)
1.168(d)-1(b)	MACRS – Conventions – MQ – Nonrecognition Transactions (7)
1.168(d)-1(c)	MACRS – Conventions – Effect on Dispositions
1.168(i)-1	MACRS – General Asset Accounts
1.168(k)-1T	Additional First Year Depreciation Deduction
169	Amortization of Pollution Control Facilities
174	Research and Development (Experimental) Expenses
179	Section 179 Expense Deduction
179(a)	Section 179 – Overview
179(b)	Section 179 – Limitations
179(b)(1)	Section 179 – Limitations – Dollar Limitation
179(b)(2)	Section 179 – Limitations – Reduction in Limitation
179(b)(3)	Section 179 – Limitations – Based on Income
179(b)(3)(B)	Section 179 – Limitations – Based on Income – Carryover Amount
179(b)(4)	Section 179 – Limitations – Married Filing Separately
179(b)(5)	Limitation on Cost Taken into Account for Certain Passenger Vehicles
179(b)(6)	Inflation Adjustment
179(c)	Section 179 – Election
179(d)	Section 179 – Definitions and Special Rules
179(d)(1)	Section 179 – Definition – Qualifying Property
179(d)(2)	Section 179 – Definition – Purchase

IRS Code Sec. or Reg.	Brief Description — Numerical Order
179(d)(3)	Section 179 – Definition – Cost
179(d)(4)	Section 179 – Special Rules – Estates and Trusts
179(d)(5)	Section 179 – Special Rules – Noncorporate Lessors
179(d)(6)	Section 179 – Special Rules – Controlled Group
179(d)(7)	Section 179 – Definition – Controlled Group
179(d)(8)	Section 179 – Special Rules – S Corporations and Partnerships
179(d)(9)	Section 179 – Special Rules – Coordination With IRS Code Section 38
179(d)(10)	Section 179 – Recapture in Certain Cases
179(e)	Special Rules for Qualified Disaster Assistance Property
179(f)	Special Rules for Qualified Real Property
1.179-1(a)	Section 179 – Overview
1.179-1(b)	Section 179 – Amount of Expense
1.179-1(c)	Section 179 – Proration Not Required
1.179-1(d)	Section 179 – Partial Business Use
1.179-1(e)	Section 179 – Change in Use – Recapture
1.179-1(f)	Section 179 – Basis
1.179-1(g)	Section 179 – Coordination With IRS Code Section 38
1.179-1(h)	Section 179 – Special Rules – S Corporations and Partnerships
1.179-1(i)	Section 179 – Leasing Section 179 Property
1.179-1(j)	Section 179 – Coordination With Other IRS Code Sections
1.179-2	Section 179 – Limitations on Amount Subject to Section 179
1.179-2(a)	Section 179 – General
1.179-2(b)	Section 179 – Dollar Limitation
1.179-2(c)	Section 179 – Taxable Income Limitation
1.179-2(d)	Section 179 – Examples
1.179-3	Section 179 – Carryover
1.179-3(a)	Section 179 – Carryover – General
1.179-3(b)	Section 179 – Carryover – Deduction
1.179-3(c)	Section 179 – Carryover – Unused Expense
1.179-3(d)	Section 179 – Carryover – Example

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1.179-3(e)	Section 179 – Carryover – Recordkeeping Requirement
1.179-3(f)	Section 179 – Carryover – Dispositions and Other Transfers
1.179-3(g)	Section 179 – Carryover – Partnerships and S Corps
1.179-3(h)	Section 179 – Carryover – Partnerships and S Corp Shareholders
1.179-4	Section 179 – Definitions
1.179-4(a)	Section 179 – Definition – Section 179 Property
1.179-4(b)	Section 179 – Definition – Section 38 Property
1.179-4(c)	Section 179 – Definition – Purchase
1.179-4(d)	Section 179 – Definition – Cost
1.179-4(e)	Section 179 – Definition – Placed in Service
1.179-4(f)	Section 179 – Definition – Controlled Group
1.179-5	Section 179 – Election
1.179-6	Section 179 – Effective Dates
179A	Section 179A – Deductions for Clean-Fuel Vehicles and Clean-Fuel Vehicle Refueling Property
179B	Section 179B – Deductions for Costs of Diesel Fuel Sulfur Control Compliance
179C	Section 179C – Deductions for Certain Costs of Property that is Part of a New Refinery or Increases Output or Throughput of an Existing Refinery
179D	Section 179D – Deductions for Costs of Energy Efficient Commercial Building Property
194	Amortization of Reforestation Expenditures
197	Amortization of Intangible Assets
212	Expenses for Production of Income
263	Capital Expenditures
1.263(a)	Capital Expenditures

IRS Code Sec. or Reg.	Brief Description — Numerical Order
263A	Capitalization and Inclusion in Inventory of Certain Expenses
267	Related Taxpayers
280F	Listed Property
280F(a)	Listed – Cars – Luxury Cars
280F(b)	Listed – Business Use 50% or Less
280F(c)	Listed – Leased Property
280F(d)	Listed – Definitions and Special Rules
280F(d)(1)	Listed – Coordination With Section 179
280F(d)(2)	Listed – Subsequent Years' Depreciation
280F(d)(3)	Listed – Special Rules – Employee Use
280F(d)(4)	Listed – Definition – Listed Property
280F(d)(5)	Listed – Definition – Passenger Automobile
280F(d)(6)	Listed – Business-Use Percentage
280F(d)(7)	Listed – Cars – Price Inflation Adjustment
280F(d)(8)	Listed – Definition – Unrecovered Basis
280F(d)(9)	Listed – Cars – Multiple Owners
280F(d)(10)	Listed – Nonrecognition Transactions
1.280F-1T(a)	Listed – Overview
1.280F-1T(b)	Listed – Code Provisions
1.280F-1T(c)	Listed – Effective Dates
1.280F-2T(a)	Listed – Cars – Limitation on Investment Credit
1.280F-2T(b)	Listed – Cars – Limitation on Depreciation
1.280F-2T(c)	Listed – Cars – Subsequent Years' Depreciation
1.280F-2T(d)	Listed – Cars – Short Tax Year
1.280F-2T(e)	Listed – Cars – Examples
1.280F-2T(f)	Listed – Cars – Improvements That Are Capitalized
1.280F-2T(g)	Listed – Cars – Exchanges and Involuntary Conversion

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1.280F-2T(h)	Listed – Cars – Other Nonrecognition Transactions
1.280F-2T(i)	Listed – Cars – Limitations
1.280F-3T(a)	Listed – Bus. Use 50% or Less – Overview
1.280F-3T(b)	Listed – Bus. Use 50% or Less – ITC Limitation
1.280F-3T(c)	Listed – Bus. Use 50% or Less – Method of Depreciation
1.280F-3T(d)	Listed – Bus. Use 50% or Less – Depreciation Recapture
1.280F-3T(e)	Listed – Bus. Use 50% or Less – Earnings and Profits Life
1.280F-3T(f)	Listed – Bus. Use 50% or Less – Examples
1.280F-4T(a)	Listed – Bus. Use 50% or Less – Subsequent Years' Depreciation
1.280F-4T(b)	Listed – Special Rules – Improvements That Are Capitalized
1.280F-5T(a)	Listed – Leased Property – Overview
1.280F-5T(b)	Listed – Leased – Coordination With Investment Tax Credit
1.280F-5T(c)	Listed – Leased – Definition
1.280F-5T(d)	Listed – Leased Cars – Income Inclusion 6/19/84 – 4/2/85
1.280F-5T(e)	Listed – Leased Cars – Income Inclusion 4/3/85 – 12/31/86
1.280F-5T(f)	Listed – Leased Other Property – Income Inclusions
1.280F-5T(g)	Listed – Leased – Special Rules – Income Inclusions
1.280F-5T(h)	Listed – Leased – Definition – Lease Term (1)
1.280F-5T(h)	Listed – Leased – Definition – Fair Market Value (2)
1.280F-5T(h)	Listed – Leased – Definition – Average Bus/Investment Use (3)
1.280F-5T(i)	Listed – Leased – Examples
1.280F-6T	Listed – Definitions and Special Rules
1.280F-6T(a)	Listed – Definition – Deductions of Employee
1.280F-6T(b)	Listed – Definition – Listed Property
1.280F-6T(c)	Listed – Definition – Passenger Automobile
1.280F-6T(d)	Listed – Definition – Business-Use Percentage (1)
1.280F-6T(d)	Listed – Definition – Qualified Business Use (2)
1.280F-6T(e)	Listed – Allocation of Use
1.280F-7(a)	Listed – Leased Cars – Post-1986 Income Inclusion
1.280F-7(b)	Listed – Leased Other Property – Post-1986 Income Inclusion

IRS Code Sec. or Reg.	Brief Description — Numerical Order
291	Corporate Tax Preference Items
611	Depletion
1011	Basis – for Determining Gain or Loss
1012	Basis – Cost
1013	Basis – Included in Inventory
1014	Basis – Property Acquired from a Decedent
1015	Basis – Property Acquired by Gift and Transfers in Trust
1016	Basis – Adjustments
1038	Real Property – Certain Reacquisitions
1245	Personal Property
1250	Real Property
1253	Franchises, Trademarks, and Trade Names – Transfers
1397A	Enterprise Zones – Increased Section 179 Expense
1400L	Tax Benefits for New York Liberty Zone
1400L(a)	Work Opportunity Tax Credit
1400L(b)	Special Allowance

IRS Code Sec. or Reg.	Brief Description — Numerical Order
1400L(c)	L/H Improvements – 5 Year Recovery Period
1400L(d)	Tax-Exempt Bond Financing
1400L(e)	Advance Refundings of Certain Tax-Exempt Bonds
1400L(f)	Section 179 Increase
1400L(g)	Extension of Replacement Period for Nonrecognition of Gain
1400L(h)	New York Liberty Zone
1400L(b)-1T	Additional First Year Depreciation Deduction

IRS Code Sections and Regulations in Alphabetical Order

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.167(j)	Accelerated Depreciation – Limitations for Real Property
1.167(a)-7	Accounting for Depreciable Property
1.167(a)-7(b)	Accounting – Composite Asset Accounts
1.167(a)-7(a)	Accounting – Grouping Assets by Account
56(g)(4)	ACE – Adjustments
56(g)(3)	ACE – Definition
1.56(g)-1(b)	ACE – Depreciation
1.56(g)-1(b)	ACE – Depreciation – ACRS Property (3)
56(g)(4)(A)	ACE – Depreciation – ACRS Property (iii)
56(g)(4)(A)	ACE – Depreciation – Adjustments
1.56(g)-1(b)	ACE – Depreciation – Excluded Property (5)
1.56(g)-1(b)	ACE – Depreciation – MACRS Post-1989 Property (1)
56(g)(4)(A)	ACE – Depreciation – MACRS Post-1989 Property (i)
56(g)(4)(A)	ACE – Depreciation – MACRS Pre-1990 Property (ii)
1.56(g)-1(b)	ACE – Depreciation – MACRS Pre-1990 Property (2)
56(g)(4)(A)	ACE – Depreciation – Pre-1981 Property (iv)
56(g)(4)(A)	ACE – Depreciation – Special Rules for Certain Property (v)
1.56(g)-1(b)	ACE – Depreciation – Special Rules for Certain Property (4)
56(g)(2)	ACE – Negative Adjustments Allowed
1.56(g)-1(a)	ACE – Overview
56(g)(1)	ACE – Overview
1.168-2	ACRS – Deduction for Depreciation
1.168-2(i)	ACRS – Deduction – **Reserved by IRS**
1.168-2(k)	ACRS – Deduction – Accrues Ratably Over Year
1.168-2(c)	ACRS – Deduction – Alternate ACRS – Straight-Line Method
1.168-2(b)	ACRS – Deduction – Applicable Percentage
1.168-2(n)	ACRS – Deduction – Basis of Partnership Property
1.168-2(j)	ACRS – Deduction – Changes in Use
1.168-2(e)	ACRS – Deduction – Components and Improvements

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.168-2(a)	ACRS – Deduction – Computation
1.168-2(l)	ACRS – Deduction – Definitions
1.168-2(l)(1)	ACRS – Deduction – Definition – Disposition
1.168-2(l)(2)	ACRS – Deduction – Definition – Placed in Service
1.168-2(l)(4)	ACRS – Deduction – Definition – Recovery Period
1.168-2(l)(3)	ACRS – Deduction – Definition – Recovery Year
1.168-2(m)	ACRS – Deduction – Industrial Development Bonds
1.168-2(h)	ACRS – Deduction – Mass Asset Accounts
1.168-2(g)	ACRS – Deduction – Property Used Outside of U.S.
1.168-2(f)	ACRS – Deduction – Short Tax Years
1.168-2(d)	ACRS – Deduction – Unadjusted Basis
1.168-6	ACRS – Dispositions: Gain or Loss Recognized
1.168-4	ACRS – Excluded Property
1.168-4(b)	ACRS – Excluded Property – Certain Methods of Depreciation
1.168-4(d)	ACRS – Excluded Property – Churning Transactions
1.168-4(a)	ACRS – Excluded Property – Pre-1981 Property
1.168-4(c)	ACRS – Excluded Property – Public Utility Property
1.168-1	ACRS – Overview
1.168-3	ACRS – Property (Recovery Property)
1.168-3(b)	ACRS – Property – Classes of Recovery Property
1.168-3(c)	ACRS – Property – Definitions
1.168-3(c)(1)	ACRS – Property – Definition – 3-Year Property
1.168-3(c)(2)	ACRS – Property – Definition – 5-Year Property
1.168-3(c)(3)	ACRS – Property – Definition – 10-Year Property
1.168-3(c)(4)	ACRS – Property – Definition – 15-Year Property
1.168-3(c)(5)	ACRS – Property – Definition – 15-Year Public Utility
1.168-3(c)(9)	ACRS – Property – Definition – Coal Utilization Property
1.168-3(c)(11)	ACRS – Property – Definition – Original Use
1.168-3(c)(8)	ACRS – Property – Definition – Present Class Life
1.168-3(c)(10)	ACRS – Property – Definition – Public Utility Property

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.168-3(c)(6)	ACRS – Property – Definition – Section 1245 Property
1.168-3(c)(7)	ACRS – Property – Definition – Section 1250 Property
1.168-3(a)	ACRS – Property – Overview
56(g)	Adjusted Current Earnings (See also ACE)
1.56(g)-1	Adjusted Current Earnings (See also ACE)
1.167(a)-11(e)	ADR – Accounting for Eligible ADR Property
1.167(a)-11	ADR – Asset Depreciation Range System
1.167(m)	ADR – Class Lives
1.167(a)-11(b)	ADR – Depreciation Ranges' Reasonable Allowance
1.167(a)-11(f)	ADR – Electing ADR for Eligible Property
1.167(a)-11(c)	ADR – Manner of Determining Depreciation Allowance
1.167(a)-11(a)	ADR – Overview
1.167(a)-11(g)	ADR – Relationship to Useful Life and Straight-Line Depreciation
1.167(a)-11(d)	ADR – Rules for Salvage, Repairs, and Retirements
56	Alternative Minimum Tax Adjustments
30B	Alternative Motor Vehicle Credit for Fuel Cell, Hybrid, Lean Burn Technology, and Alternative Fuel Vehicles
197	Amortization of Intangible Assets
169	Amortization of Pollution Control Facilities
194	Amortization of Reforestation Expenditures
1.167(a)-5	Apportionment of Basis
1.167(g)	Basis for Depreciation
1016	Basis – Adjustments
1012	Basis – Cost
1011	Basis – for Determining Gain or Loss
1013	Basis – Included in Inventory
1015	Basis – Property Acquired by Gift and Transfers in Trust
1014	Basis – Property Acquired from a Decedent
38(b)(24)	Business Tax Credit for Manufacturers of Energy Efficient Dishwashers, Clothes Washers, and Refrigerators
263	Capital Expenditures

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
179	Capital Expense Deduction (See also Section 179)
263A	Capitalization and Inclusion in Inventory of Certain Expenses
1.167(e)	Change in Method
179A	Clean-Fuel Vehicles – Expense Deduction
1.167(a)-6(A)	Copyrights
291	Corporate Tax Preference Items
611	Depletion
1.167(a)-1	Depreciation in General
30	Electric Vehicles Tax Credit
38(b)(23)	Energy Efficient Home Credit Available to Eligible Contractors
1397A	Enterprise Zones – Increased Section 179 Expense
212	Expenses for Production of Income
1.167(a)-6(B)	Farmers
1253	Franchises, Trademarks, and Trade Names – Transfers
38	General Business Credit (Replaced Investment Credit Section)
1.167(a)-3	Intangibles
46(3)	Investment Tax Credit Expanded for Qualified Investment in a Qualifying Advanced Coal Project
46(4)	Investment Tax Credit Expanded for Qualified Investment in a Qualifying Gasification Property
1.167(a)-4	Leased Property
280F	Listed Property
1.280F-6T(e)	Listed – Allocation of Use
280F(b)	Listed – Business Use 50% or Less
1.280F-3T(d)	Listed – Bus. Use 50% or Less – Depreciation Recapture
1.280F-3T(e)	Listed – Bus. Use 50% or Less – Earnings and Profits Life
1.280F-3T(f)	Listed – Bus. Use 50% or Less – Examples
1.280F-3T(b)	Listed – Bus. Use 50% or Less – ITC Limitation
1.280F-3T(c)	Listed – Bus. Use 50% or Less – Method of Depreciation
1.280F-3T(a)	Listed – Bus. Use 50% or Less – Overview
1.280F-4T(a)	Listed – Bus. Use 50% or Less – Subsequent Years' Depreciation

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
280F(d)(6)	Listed – Business-Use Percentage
1.280F-2T(e)	Listed – Cars – Examples
1.280F-2T(g)	Listed – Cars – Exchanges and Involuntary Conversion
1.280F-2T(f)	Listed – Cars – Improvements that are Capitalized
1.280F-2T(b)	Listed – Cars – Limitation on Depreciation
1.280F-2T(a)	Listed – Cars – Limitation on Investment Credit
1.280F-2T(i)	Listed – Cars – Limitations
280F(a)	Listed – Cars – Luxury Cars
280F(d)(9)	Listed – Cars – Multiple Owners
1.280F-2T(h)	Listed – Cars – Other Nonrecognition Transactions
280F(d)(7)	Listed – Cars – Price Inflation Adjustment
1.280F-2T(d)	Listed – Cars – Short Tax Year
1.280F-2T(c)	Listed – Cars – Subsequent Years' Depreciation
1.280F-1T(b)	Listed – Code Provisions
280F(d)(1)	Listed – Coordination With Section 179
1.280F-6T(d)	Listed – Definition – Business-Use Percentage
1.280F-6T(a)	Listed – Definition – Convenience of Employer
1.280F-6T(b)	Listed – Definition – Listed Property
280F(d)(4)	Listed – Definition – Listed Property
1.280F-6T(b)	Listed – Definition – Means of Transportation
1.280F-6T(c)	Listed – Definition – Passenger Automobile
280F(d)(5)	Listed – Definition – Passenger Automobile
1.280F-6T(b)	Listed – Definition – Property Used for Entertainment
1.280F-6T(d)	Listed – Definition – Qualified Business Use
1.280F-6T(b)	Listed – Definition – Regular Business Establishment
280F(d)(8)	Listed – Definition – Unrecovered Basis
1.280F-6T	Listed – Definitions and Special Rules
280F(d)	Listed – Definitions and Special Rules
1.280F-1T(c)	Listed – Effective Dates
1.280F-5T(e)	Listed – Leased Cars – Income Inclusion 4/3/85 – 12/31/86

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.280F-5T(d)	Listed – Leased Cars – Income Inclusion 6/19/84 – 4/2/85
1.280F-7T(a)	Listed – Leased Cars – Post-1986 Income Inclusion
1.280F-5T(f)	Listed – Leased Other Property – Income Inclusions
1.280F-7T(b)	Listed – Leased Other Property – Post-1986 Income Inclusion
280F(c)	Listed – Leased Property
1.280F-5T(a)	Listed – Leased Property – Overview
1.280F-5T(b)	Listed – Leased – Coordination With Investment Tax Credit
1.280F-5T(c)	Listed – Leased – Definition
1.280F-5T(h)	Listed – Leased – Definition – Average Bus/Investment Use(3)
1.280F-5T(h)	Listed – Leased – Definition – Fair Market Value (2)
1.280F-5T(h)	Listed – Leased – Definition – Lease Term (1)
1.280F-5T(i)	Listed – Leased – Examples
1.280F-5T(g)	Listed – Leased – Special Rules – Income Inclusions
280F(d)(10)	Listed – Nonrecognition Transactions
1.280F-1T(a)	Listed – Overview
1.280F-6T(b)	Listed – Special Rules – Computers
1.280F-6T(a)	Listed – Special Rules – Condition of Employment
1.280F-6T(a)	Listed – Special Rules – Employee Use
280F(d)(3)	Listed – Special Rules – Employee Use
1.280F-4T(b)	Listed – Special Rules – Improvements That Are Capitalized
280F(d)(2)	Listed – Subsequent Years' Depreciation
168(g)	MACRS – ADS
168(g)(3)	MACRS – ADS – Class Life Rules
168(g)(7)	MACRS – ADS – Election
168(g)(6)	MACRS – ADS – Imported Property
168(g)(2)	MACRS – ADS – Method, Conventions, Recovery Periods
168(g)(1)	MACRS – ADS – Overview
168(g)(4)	MACRS – ADS – Property Used Outside of U.S.
168(g)(5)	MACRS – ADS – Tax-Exempt Financed Property
168(e)	MACRS – Classification of Property

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
168(e)(3)(D)	MACRS – Classification of Property – 10 Year
168(e)(3)(E)	MACRS – Classification of Property – 15 Year
168(e)(3)(F)	MACRS – Classification of Property – 20 Year
168(e)(3)(A)	MACRS – Classification of Property – 3 Year
168(e)(3)(B)	MACRS – Classification of Property – 5 Year
168(e)(3)(C)	MACRS – Classification of Property – 7 Year
168(e)(2)(B)	MACRS – Classification of Property – Nonresidential
168(e)(1)	MACRS – Classification of Property – Overview
168(e)(4)	MACRS – Classification of Property – Railroad Grading
168(e)(2)(A)	MACRS – Classification of Property – Residential Rental
168(e)(4)	MACRS – Classification of Property – Tunnel Bore
1.168(d)-1	MACRS – Conventions (Averaging Conventions)
168(d)	MACRS – Conventions (Averaging Conventions)
168(d)(4)	MACRS – Conventions – Definitions
1.168(d)-1(c)	MACRS – Conventions – Effect on Dispositions
168(d)(1)	MACRS – Conventions – Half-Year
168(d)(2)	MACRS – Conventions – Midmonth
168(d)(3)	MACRS – Conventions – Midquarter (MQ)
1.168(d)-1(b)	MACRS – Conventions – Midquarter (MQ)
1.168(d)-1(b)	MACRS – Conventions – MQ – Affiliated Groups (5)
1.168(d)-1(b)	MACRS – Conventions – MQ – Aggregate Basis of Property (4)
1.168(d)-1(b)	MACRS – Conventions – MQ – Excluded Property (1)
1.168(d)-1(b)	MACRS – Conventions – MQ – Listed Property (2)
1.168(d)-1(b)	MACRS – Conventions – MQ – Nonrecognition Transactions (7)
1.168(d)-1(b)	MACRS – Conventions – MQ – Placed in Service and Disposed of in Same Year (3)
1.168(d)-1(b)	MACRS – Conventions – MQ – S Corporations and Partnerships (6)
1.168(d)-1(a)	MACRS – Conventions – Overview
168(i)(1)	MACRS – Definition – Class Life
168(i)(2)(B)	MACRS – Definition – Computer and Peripheral Equipment
168(i)(2)(C)	MACRS – Definition – High Technology Medical Equipment

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
168(i)(2)(A)	MACRS – Definition – Qualified Technological Equipment
168(i)(11)	MACRS – Definition – Research and Experimentation
168(i)(12)	MACRS – Definition – Section 1245 and 1250 Property
168(i)(13)	MACRS – Definition – Single-Purpose Agricultural and Horticultural Structure and Livestock
168(i)	MACRS – Definitions and Special Rules
168(f)	MACRS – Excluded Property
168(f)(1)	MACRS – Excluded Property – Certain Methods of Depreciation
168(f)(2)	MACRS – Excluded Property – Certain Public Utility Property
168(f)(5)	MACRS – Excluded Property – Churning Transactions
168(f)(3)	MACRS – Excluded Property – Films and Videotapes
168(f)(4)	MACRS – Excluded Property – Sound Recordings
168(a)	MACRS – General
1.168(i)-1	MACRS – General Asset Accounts
168(b)	MACRS – Methods of Depreciation
168(c)	MACRS – Recovery Periods
168(i)(5)	MACRS – Special Rules – Changes in Use
168(i)(4)	MACRS – Special Rules – General Asset Accounts
168(i)(6)	MACRS – Special Rules – Improvements or Additions
168(i)(3)	MACRS – Special Rules – Lease Term
168(i)(8)	MACRS – Special Rules – Leasehold Improvements
168(i)(9)	MACRS – Special Rules – Normalization Method of Accounting
168(i)(10)	MACRS – Special Rules – Public Utility Property
168(i)(7)	MACRS – Special Rules – Transferees
168(h)	MACRS – Tax-Exempt Use Property
168(h)(3)	MACRS – Tax-Exempt Use – High Technology Equipment
168(h)(1)	MACRS – Tax-Exempt Use – Overview
168(h)(5)	MACRS – Tax-Exempt Use – Property Leased to Partnerships, etc.
168(h)(6)	MACRS – Tax-Exempt Use – Property Owned by Partnerships, etc.
168(h)(4)	MACRS – Tax-Exempt Use – Related Entities
168(h)(2)	MACRS – Tax-Exempt Use – Tax-Exempt Entity

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.167(b)-0	Methods of Computing Depreciation – Overview
1.167(b)-2	Methods – Declining-Balance
1.167(c)	Methods – Limitations on Methods Under 167(b)-2, 3 and 4
1.167(b)-4	Methods – Miscellaneous Methods
1.167(b)-1	Methods – Straight-Line
1.167(b)-3	Methods – Sum-of-the-Years'-Digits
1.167(i)	Mining, Oil and Gas Wells, and Other Natural Deposits
29	Nonconventional Fuel Production Credit
1.167(a)-9	Obsolescence
1.167(a)-6(A)	Patents
1245	Personal Property
1.167(a)-12	Pre-1971 Assets
1.167(a)-12(d)	Pre-1971 Assets – Accounting for Eligible Property
1.167(a)-12(f)	Pre-1971 Assets – Depreciation for Tax Years Ending Before 1971
1.167(a)-12(b)	Pre-1971 Assets – Determination of Class Lives
1.167(a)-12(e)	Pre-1971 Assets – Election for Tax Years Ending After 1970
1.167(a)-12(a)	Pre-1971 Assets – Generally
1.167(a)-12(c)	Pre-1971 Assets – Salvage Value
1.167(l)	Public Utilities – Limitations on Depreciation
38(b)	Qualified Alternative Fuel Vehicle Refueling Property
48(a)(1)	Qualified Microturbine Property Energy Credit; Qualified Fuel Cell Property Energy Credit
1250	Real Property
1038	Real Property – Certain Reacquisitions
1.167(j)	Real Property – Limitations on Accelerated Depreciation
1.167(a)-1(a)	Reasonable Allowance
1.167(k)	Rehabilitation Expenditures – Depreciation on Property
267	Related Taxpayers
174	Research and Development (Experimental) Expenses
1.168-5	Retirement-Replacement-Betterment (RRB) Property
1.167(a)-8	Retirements of Assets

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.167(a)-1(c)	Salvage
1.167(f)	Salvage Value – Reduction for Personal Property
179	Section 179
1.179-1(b)	Section 179 – Amount of Expense
1.179-1(f)	Section 179 – Basis
1.179-1(e)	Section 179 – Change in Use – Recapture
1.179-1(g)	Section 179 – Coordination With IRS Code Section 38
1.179-1(j)	Section 179 – Coordination With Other IRS Code Sections
1.179-3	Section 179 – Definitions
1.179-3(a)	Section 179 – Definition – Section 179 Property
1.179-3(g)	Section 179 – Definition – Controlled Group
179(d)(7)	Section 179 – Definition – Controlled Group
1.179-3(e)	Section 179 – Definition – Cost
179(d)(3)	Section 179 – Definition – Cost
1.179-3(f)	Section 179 – Definition – Placed in Service
1.179-3(d)	Section 179 – Definition – Purchase
179(d)(2)	Section 179 – Definition – Purchase
179(d)(1)	Section 179 – Definition – Qualifying Property
1.179-3(b)	Section 179 – Definition – Recovery Property
1.179-3(c)	Section 179 – Definition – Section 38 Property
179(d)	Section 179 – Definitions and Special Rules
1.179-2	Section 179 – Dollar Limitation
1.179-2(b)	Section 179 – Dollar Limitation – Controlled Group
1.179-2(e)	Section 179 – Dollar Limitation – Married Filing Jointly
1.179-2(f)	Section 179 – Dollar Limitation – Married Filing Separately
1.179-2(a)	Section 179 – Dollar Limitation – Maximum Amount
1.179-2(c)	Section 179 – Dollar Limitation – Partnerships
1.179-2(d)	Section 179 – Dollar Limitation – S Corporations
1.179-5	Section 179 – Effective Dates
1.179-4	Section 179 – Election

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
179(c)	Section 179 – Election
1.179-1(i)	Section 179 – Leasing Section 179 Property
179(b)	Section 179 – Limitations
179(b)(3)	Section 179 – Limitations – Based on Income
179(b)(3)(B)	Section 179 – Limitations – Based on Income – Carryover Amount
179(b)(1)	Section 179 – Limitations – Dollar Limitation
179(b)(4)	Section 179 – Limitations – Married Filing Separately
179(b)(2)	Section 179 – Limitations – Reduction in Limitation
1.179-1(a)	Section 179 – Overview
179(a)	Section 179 – Overview
1.179-1(d)	Section 179 – Partial Business Use
1.179-1(c)	Section 179 – Proration Not Required
179(d)(6)	Section 179 – Special Rules – Controlled Group
179(d)(9)	Section 179 – Special Rules – Coordination With IRS Code Section 38
179(d)(4)	Section 179 – Special Rules – Estates and Trusts
179(d)(5)	Section 179 – Special Rules – Noncorporate Lessors
179(d)(8)	Section 179 – Special Rules – S Corporations and Partnerships
1.179-1(h)	Section 179 – Special Rules – S Corporations and Partnerships
179A	Section 179A – Deductions for Clean-Fuel Vehicles and Clean-Fuel Vehicle Refueling Property
179B	Section 179B – Deductions for Costs of Diesel Fuel Sulfur Control Compliance
179C	Section 179C – Deductions for Certain Costs of Property that is Part of a New Refinery or Increases Output or Throughput of an Existing Refinery
179D	Section 179D – Deductions for Costs of Energy Efficient Commercial Building Property
1.167(a)-2	Tangible Property
46	Tax Credit for Investment in Certain Property
57	Tax Preference Items
1.167(a)-10	Timing of Depreciation – When Is It Allowable?
1.167(h)	Trusts and Estates – Life Tenants and Beneficiaries
1.167(a)-1(B)	Useful Life

IRS Code Sec. or Reg.	Brief Description — Alphabetical Order
1.167(d)	Useful Life and Rates of Depreciation Agreement

Glossary

A

Accounting Period

The economic cycle about which financial records are maintained.

Accumulated Depreciation

The amount of depreciation taken, including current year-to-date depreciation, from the date the asset was placed in service to the date through which depreciation was last calculated.

ACE

Adjusted Current Earnings, defined in IRS Code Section 56(g), the recalculation of C corporation income for purposes of computing an adjustment amount as required for the Alternative Minimum Tax.

Acquisition Value

The cost of obtaining an asset. This may be the asset's purchase price, its fair market value, or its basis in the hands of the transferor, depending on the type of transaction.

ACRS

Accelerated Cost Recovery System, a depreciation system for property placed in service after 1980, but before 1987, which simplified the depreciation rules and accelerated the rate of depreciation for most property.

Additional Bonus Depreciation

Additional depreciation, prior to 1981, allowed for qualifying property the first year in which it was placed in service, up to 20% of the property's basis.

Adjusted Basis

The original cost of property (its acquired value), plus certain additions and improvements, minus certain reductions, such as accumulated depreciation.

Adjusted Current Earnings

See ACE.

ADR

Asset Depreciation Range System, a depreciation system for property placed in service after 1970, but before 1981, which grouped assets by industry type.

ADS

Alternative Depreciation System, a depreciation system, under MACRS, which uses straight-line depreciation over limited recovery periods.

Agreement Not To Compete

See Covenant-Not-To-Compete.

Allocation Method

Under MACRS, one of two methods for manually computing depreciation for an asset that is placed in service during a short tax year (see also Simplified Method).

Alternative Depreciation System

See ADS.

Alternative Minimum Tax

See AMT.

Amortizable Property

Intangible assets whose value is being expensed under the rules of Amortization.

Amortization

A method of recovering the cost of intangible assets using straight-line depreciation.

AMT

Alternative Minimum Tax, a group of tax law provisions to ensure that taxpayers with high incomes pay a certain amount of tax, by reducing various tax benefits available to them.

Asset Depreciation Range

See ADR.

Averaging Conventions

A set of rules for determining how depreciation is prorated for the year in which property is placed in service, as well as for the year in which property is disposed of (if it is disposed of before it is fully depreciated).

B

Basis

Usually refers to Acquired Value. Also see Depreciable Basis.

Boot

In a trade-in of one asset for another, any cash or note payable given to the seller in addition to the asset traded.

Business-Use Percentage

The portion of an otherwise depreciable asset for which depreciation is allowed. When a business asset is used partially for personal use, the business may only take depreciation on the asset to the extent that it is used for business (i.e., the depreciable basis of the asset is reduced by the personal use portion).

C

Calendar Year

The most widely used accounting period: a period of 12 months beginning January 1 and ending December 31.

Capital Expense Deduction (CED)

See Section 179 Expense Deduction.

Capitalization

Adding certain expenditures to asset accounts on the balance sheet, rather than deducting them as a current expense on the income statement.

Class Life

The number of years that establishes an asset's property class and recovery period under MACRS, ACRS, and ADS. It is the midpoint of the Asset Depreciation Range in which the asset belongs.

Clean-fuel Vehicle Property

Motor vehicles produced by an original equipment manufacturer and designed to be propelled by a clean-burning fuel. Or any property installed on a motor vehicle to enable it to be propelled by a clean-burning fuel if the property is an engine (or modification or an engine) that can use a clean burning fuel or the property is used to store or deliver that fuel to the engine or to exhaust gases from the combustion of that fuel.

Clean-fuel Vehicle Refueling Property

Any property (other than a building or its structural components) used to store or dispense a clean-burning fuel into the fuel tank of a motor vehicle propelled by the fuel, but only if the storage or dispensing is at the point where the fuel is delivered into the tank. Or any property used to recharge motor vehicles propelled by electricity, but only if the property is located at the point where the vehicles are recharged.

Conventions

See Averaging Conventions.

Cost Recovery

Expensing (i.e., recovering) the cost of an asset under MACRS or ACRS depreciation methods.

Covenant-Not-To-Compete

A promise by the seller of a business, made to the purchaser of that business, not to engage in a similar business within a specified area for a specified period of time, so as not to vie for the same customers.

D

Declining-Balance Depreciation

An accelerated method of depreciation, whereby the property's net book value is multiplied by a constant rate (125%, 150%, 175%, or 200%, divided by the estimated life or recovery period), and which results in a greater amount of depreciation being expensed in the early years of an asset's life and a smaller amount in later years.

Depreciable Basis

The amount of the Acquired Value of property for which a business is allowed to claim a depreciation expense.

Depreciation

The process of allocating the cost expiration of tangible property against income, and which is applied to business assets that have a useful life of more than one year.

Depreciation Recapture

The recognition as ordinary income of some or all of the depreciation previously expensed, due to a certain event, such as the sale of the asset or a decrease in the amount of the business use of the asset.

Disposal Date

The day on which an asset is sold, lost, damaged, stolen, exchanged, used up, worn out, broken, retired, or given away.

E

Electric Vehicle Credit

See Section 30 Credit.

Enterprise Zone Business

A business that meets certain criteria as an active, rather than a passive, business. An enterprise zone business is entitled to a higher amount of Section 179 expense (IRS Code Sec. 1397A).

Estimated Useful Life

The period of time that most accurately reflects an asset's true economic usefulness, over which the asset will be depreciated for financial reporting purposes.

F

Fair Market Value

The price at which property would be exchanged in an arms-length transaction, where both the buyer and the seller know all of the necessary facts and neither is obliged to complete the transaction.

52-53-Week Accounting Cycle

In a 52/53week accounting cycle, each fiscal year ends on the same day of the week. Because of this, some years will have 52 weeks while others will have 53 weeks. A 52/53-week accounting cycle can use various interim reporting periods that are based on weeks: 4-5-4, 4-4-5, 5-4-4, or 13 4-week periods.

Fiscal Year

The economic period ending on the last day of any month chosen to be the year-end.

Fixed Asset

Property used for the production of income and having an estimated life of more than one year.

G

GAAP

Generally Accepted Accounting Principles, the guidelines and specific rules and procedures issued by bodies within the accounting industry, principally the Financial Accounting Standards Board (FASB) and the American Institute of Certified Public Accountants (AICPA), which standardize accounting practices and ensure that a business's financial records fairly reflect its operations.

Goodwill

An intangible property that represents the benefit acquired in the purchase of a business, beyond the value of its assets.

H

Half-Year Convention

Treats all property as placed in service during any taxable year (or disposed of during any taxable year) as placed in service (or disposed of) at the midpoint of such year.

I

Income Forecasting

A depreciation method whereby depreciation expense for an asset is based on how much income the asset earns each year as compared to the total estimated income the asset is expected to earn. If the property is placed in service after 9/13/95, only the income earned by the asset for the first eleven years of its life is taken into account.

Intangible Property

Property that lacks physical substance.

Investment Tax Credit (ITC)

A tax credit taken for the purchase of certain qualifying business property.

ITC Recapture

Repayment of Investment Tax Credit (ITC) by the taxpayer on a prorated basis when an asset for which ITC was taken is disposed of before the end of its estimated life or recovery period.

L

Listed Property

Certain property that, according to IRS Code Section 280F, lends itself to personal use and for which ACRS or MACRS deductions are limited.

Low-Income Housing

A building that has met federal guidelines and where the dwelling units are held for occupancy on a rental basis by people with moderate income.

M

MACRS

Modified Accelerated Cost Recovery System, a depreciation system for property placed in service after 1986, which modified the previous ACRS system of depreciation.

Midmonth Convention

Treats all property placed in service during any month (or disposed of) as placed in service (or disposed of) at the midpoint of such month.

Midquarter Convention

Treats all MACRS property placed in service during any quarter of a taxable year (or disposed of) as placed in service (or disposed of) at the midpoint of such quarter and is mandatory if certain conditions exist.

N

Net Book Value

An asset's acquired value less its total accumulated depreciation less any Section 179 Expense taken.

Nonrecovery Property

Property that is not being depreciated under ACRS or MACRS, which was generally placed in service prior to 1981, but which also includes property being depreciated by a method not expressed in terms of years (for example a Production or Use method, or Income Forecasting).

P

Personal Property

Tangible property that is not real property and that is moveable (i.e., not attached to the land), such as equipment and machinery.

Placed in Service

The date that property is ready and available for a specified use.

Production or Use Methods

Depreciation methods whereby the basis of property is expensed according to its use, rather than according to the passage of time.

R

Real Property

Land and generally anything erected on or attached to the land, such as a building or a parking lot.

Recapture

See Depreciation Recapture and ITC Recapture.

Recovery Period

The prescribed number of years over which ACRS and MACRS property is depreciated.

Recovery Property

Property that is being depreciated under either ACRS or MACRS.

Remaining Value Over Remaining Life

The method for switching to straight-line depreciation when using an accelerated depreciation method for the early years of an asset's life.

Residential Rental

Real property, if 80% or more of its gross rental income for the tax year is from dwelling units (excludes real property, such as hotels, where more than half of the units are used on a transient basis).

S

Salvage Value

The estimated dollar amount for which an asset could be sold at the end of its useful life.

Section 30 Credit

A tax credit for qualified electric vehicles placed in service after June 30, 1993, and before 2005.

Section 30B Credit

The 2005 Energy bill introduced new tax credits under Section 30B for vehicles placed in service after 2005 for the purchase of hybrid, fuel cell, advanced lean burn diesel and other alternative power vehicles. The amount of the credit varies depending on the weight class of the vehicle and the rate fuel economy. Termination dates vary with the type of alternative power vehicles.

Section 179 Expense Deduction

Defined in IRS Code Sec. 179; allows a business to expense up to a specified dollar amount of qualifying property in the year in which it is placed in service, subject to certain limitations.

Section 179A Expense Deduction

An expense deduction for clean-fuel vehicles and certain refueling property.

Section 179B Expense Deduction

Expense deduction that allows a small business refiner an election to deduct 75 percent of qualified capital costs paid or incurred during the tax year in order to be in compliance with the Highway Diesel Fuel Sulfur Control Requirements of EPA.

Section 179C Expense Deduction

Expense deduction that allows taxpayers to deduct 50% of the cost of “any qualified refinery property” for the tax year in which the qualified property is placed in service.

Section 179D Expense Deduction

Expense deduction that allows taxpayers to deduct a calculated amount based on square footage for the cost of “energy efficient commercial building property.”

Section 179E Expense Deduction

Expense deduction that allows taxpayers to deduct 50% of the cost of any qualified mine safety equipment property for the tax year in which the property is placed in service.

Section 197 Intangible

An intangible asset that has a 15-year standardized period for recovering its cost. This IRS Code Section was created by the Revenue Reconciliation Act of 1993.

Section 1245 Property

Personal property; i.e., all tangible property except real property.

Section 1250 Property

Real property; i.e., buildings and land, and generally anything that is growing on or attached to land.

Section 1397A

This code section increases the amount of allowable Section 179 expense by $20,000 for enterprise zones.

Simplified Method

Under MACRS, one of two methods for manually computing depreciation for an asset that is placed in service during a short tax year (see also Allocation Method).

Single-Purpose Structure

A building that is specifically designed, built, and used only for a qualifying purpose.

Straight-Line Depreciation

A depreciation method that allows an equal amount of depreciation for each year of the asset's estimated useful life.

Structural Components

Parts that together form an entire structure such as a building. The term includes those parts of a building such as walls, partitions, floors and ceilings, as well as any permanent coverings such as paneling or components of a central air conditioning or heating system including motors, compressors, pipes and ducts. It also includes plumbing fixtures such as sinks, bathtubs, electrical wiring and lighting fixtures, and other parts that form the structure.

Sum-of-the-Years'-Digits Depreciation

An accelerated method of depreciation that results in a greater amount of depreciation being expensed in the early years of an asset's life and a smaller amount in later years.

T

Tangible Property

Property that can be seen or touched.

Tax Credit

A dollar-for-dollar reduction of income tax liability in a given year.

Tax Preference

Used in calculating the Alternative Minimum Tax (AMT), the difference between the special AMT treatment of an item and its regular tax treatment.

Taxable Year

The period of time for which taxable income is computed.

Timing Difference

Using different methods of depreciation for the same property for different purposes creates a temporary difference in the basis of the property, which is fully reconciled at the close of the property's useful life.

Transitional Property

If, at the time that a tax provision expires, a company has a firm agreement that certain property be delivered, that property is called transitional property. The rules of the tax provision can usually be applied to transitional property even though the property was not yet placed in service when the tax provision expired.

U

Useful Life

See Estimated Useful Life.

V

Vintage Accounts

The fixed asset accounts under the Asset Depreciation Range System, where the "vintage" denotes the year in which the assets in a particular account were placed in service.

Index

Numerics

A

B

C

G

H

I

S

T

U

V

W