

ROBERTS, McKENZIE, MANGAN & CUMMINGS, PC
NEWS NOTES

**Depreciation Provisions – The Protecting Americans from
Tax Hikes Act of 2015**

Congress passed and President Obama, on December 18, signed H.R. 2029, the tax (the “Protecting Americans from Tax Hikes Act of 2015” (PATH Act)) and spending bills (Consolidated Appropriations Act, 2016) to fund the government for its 2016 fiscal year. The tax portion includes a two-year delay on taxing high-cost “Cadillac” health plans, as well extensions to several renewable energy credits and a tax break for oil refiners, with tax extenders language making permanent or extending dozens of expired business and household tax breaks. This News Note is the third of four covering these very important provisions. In this News Note, we review some of the major Depreciation Provisions of the PATH Act.

Enhanced Expensing Made Permanent

Under **Code Sec. 179**, a taxpayer, other than an estate, a trust, or certain noncorporate lessors, may elect to deduct as an expense, rather than to depreciate, up to a specified amount of the cost of new or used tangible personal property placed in service during the tax year in the taxpayer's trade or business. The maximum annual expensing amount generally is reduced dollar-for-dollar by the amount of **Code Sec. 179** property placed in service during the tax year in excess of a specified investment ceiling. Amounts ineligible for expensing due to excess investments in expensing-eligible property can't be carried forward and expensed in a subsequent year. Rather, they can only be recovered through depreciation. The amount eligible to be expensed for a tax year can't exceed the taxable income derived from the taxpayer's active conduct of a trade or business. And any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding tax years.

For tax years beginning in 2014: (1) the dollar limitation on the expensing deduction was \$500,000; and (2) the investment-based reduction in the dollar limitation began to take effect when property placed in service in the tax year exceeds \$2 million (the investment ceiling). Under the 2014 limits, the **Code Sec. 179** deduction didn't phase out completely until the cost of expensing-eligible property exceeded \$2.5 million (\$2 million (investment ceiling) + \$500,000 (dollar limit)). Under pre-Act law, for tax years beginning after 2014, the maximum expensing limit dropped to \$25,000, and the investment ceiling dropped to \$200,000. Thus, the **Code Sec. 179** deduction phased out completely when the cost of expensing-eligible property exceeded \$225,000 (\$200,000 (investment ceiling) + \$25,000 (dollar limit)).

New law. The Act makes the following changes to the **Code Sec. 179** expensing election: The \$500,000 expensing limitation and \$2 million phase-out amounts are retroactively extended and made permanent.

- For any tax year beginning after 2015, both the \$500,000 and \$2 million limits are indexed for inflation.
- The rule that allows expensing for computer software is retroactively extended and made permanent.
- For tax years beginning after Dec. 31, 2014, an expensing election or specification of property to be expensed may be revoked without IRS's consent is made permanent.

- Qualified real property is eligible to be expensed for tax years beginning before 2016. No portion of disallowed expensing may be carried to a tax year beginning after 2015.
- For tax years beginning after Dec. 31, 2015, expensing of qualified real property is made permanent without a carryover limitation and the \$250,000 expensing limitation with respect to qualifying real property is eliminated.
- For tax years beginning after Dec. 31, 2015, air conditioning and heating units are eligible for expensing.

15-Year Writeoff for Qualified Leasehold and Retail Improvements and Restaurant Property Made Permanent

Qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property that was placed in service before Jan. 1, 2015 was included in the 15-year MACRS class for depreciation purposes—that is, such property was depreciated over 15 years under MACRS. Under pre-Act law, the 15-year writeoff didn't apply to property placed in service after Dec. 31, 2014.

New law. Effective for property placed in service after Dec. 31, 2014, the Act retroactively extends and makes permanent the inclusion of qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property in the 15-year MACRS class.

Bonus First-Year Depreciation Extended Through 2019

Under pre-Act law, **Code Sec. 168(k)** generally allows an additional first-year depreciation deduction (also called bonus first-year depreciation) equal to 50% of the adjusted basis of qualified property acquired and placed in service after Dec. 31, 2011, and before Jan. 1, 2015 (before Jan. 1, 2016 for certain longer-lived and transportation property). The additional first-year depreciation deduction is allowed for both regular tax and alternative minimum tax (AMT) purposes, but is not allowed for purposes of computing earnings and profits. The basis of the property and the depreciation allowances in the year of purchase and later years are appropriately adjusted to reflect the additional first-year depreciation deduction. A taxpayer may elect out of additional first-year depreciation for any class of property for any tax year.

In general, an asset qualifies for the bonus depreciation allowance if:

- . . . It falls into one of the following categories: property to which the modified accelerated cost recovery system (MACRS) rules apply with a recovery period of 20 years or less; computer software other than computer software covered by **Code Sec. 197**; qualified leasehold improvement property; or certain water utility property.
- . . . It is placed in service before Jan. 1, 2015. (Certain long-production-period property and certain transportation property may be placed in service before Jan. 1, 2016)
- . . . Its original use commences with the taxpayer. Original use is the first use to which the property is put, whether or not that use corresponds to the taxpayer's use of the property.

New law. The Act extends bonus depreciation for qualified property acquired and placed in service during 2015 through 2019 (through 2020 for certain longer-lived and transportation property). Eligible taxpayers will be able to claim:

- (1) a 50% bonus depreciation allowance for qualified property placed in service in 2015 through 2017 ;
- (2) a 40% bonus depreciation allowance for qualified property placed in service in 2018; and

- (3) a 30% bonus depreciation allowance for qualified property placed in service in 2019. (**Code Sec. 168(k)**, as amended by Act Sec. 143; Joint Committee Explanation)

The percentages apply to certain longer-lived and transportation property placed in service one year later than shown in the list above. (Joint Committee Explanation)

Related changes. The Act also provides that:

- After 2015, additional first-year depreciation is allowed for qualified improvement property without regard to whether the improvements are property subject to a lease, and there is no requirement that the improvement must be placed in service more than three years after the date the building was first placed in service.
- For plants planted or grafted after Dec. 31, 2015 and before Jan. 1, 2020, 50% bonus depreciation is allowed for certain trees, vines, and plants bearing fruit or nuts when planted or grafted, rather than when placed in service.
- The special rule for the allocation of bonus depreciation to a long-term contract is extended for five years to property placed in service before Jan. 1, 2020 (Jan. 1, 2021, in the case of certain longer-lived and transportation property).
 - **Enhanced First-Year Depreciation Cap for Autos and Trucks Extended Through 2019**

Under the luxury auto dollar limits of **Code Sec. 280F**, depreciation deductions (including **Code Sec. 179** expensing) that can be claimed for passenger autos are subject to dollar limits that are annually adjusted for inflation. For passenger automobiles placed in service in 2015, the adjusted first-year limit is \$3,160. For light trucks or vans, the adjusted first-year limit is \$3,460. Light trucks or vans are passenger automobiles built on a truck chassis, including minivans and sport-utility vehicles (SUVs) built on a truck chassis that are subject to the **Code Sec. 280F** limits because they are rated at 6,000 points gross (loaded) vehicle weight or less.

The applicable first-year depreciation limit is increased by \$8,000 (not indexed for inflation) for any passenger automobile that is “qualified property” under the bonus depreciation rules of **Code Sec. 168(k)** and which isn't subject to a taxpayer election to decline bonus depreciation.

Under pre-Act law, qualified property didn't include property placed in service after Dec. 31, 2014 (except for certain aircraft and certain long-production-period property that had, instead, a Dec. 31, 2015 placed-in-service deadline). Thus, under pre-Act law, the \$8,000 boost in first-year depreciation allowances wasn't available for new cars and trucks purchased after 2014.

New law. For property placed in service after Dec. 31, 2015 and before Jan. 1, 2018, the Act provides that the **Code Sec. 280F** limitation for a passenger auto or light truck or van that is qualified property is increased by \$8,000. For an auto or light truck or van placed in service in 2018, the **Code Sec. 280F** limitation is increased by \$6,400. For an auto or light truck or van placed in service in 2019, the **Code Sec. 280F** limitation is increased by \$4,800.

Choice to Forego Bonus Depreciation and Claim Credits Instead Is Extended

Code Sec. 168(k)(4) generally permits a corporation to increase the alternative minimum tax (AMT) credit limitation by the bonus depreciation amount with respect to certain property placed in service after Dec. 31, 2010 and before Jan. 1, 2015 (Jan. 1, 2016 in the case of certain longer-lived and transportation property) if it forgoes bonus depreciation on that property.

Under pre-Act law, the above provision didn't apply to such property placed in service after Dec. 31, 2014 (Dec. 31, 2015 in the case of certain longer-lived and transportation property).

New law. For property placed in service during 2015, the Act allows taxpayers to elect to accelerate the use of AMT credits in lieu of bonus depreciation under special rules. Beginning in 2016, the Act modifies the AMT rules by increasing the amount of unused AMT credits that may be claimed in lieu of bonus depreciation.

Miscellaneous Provisions Extended Through 2016

In addition to the above, The Act retroactively extends the following provisions for two years:

- . . . Classification of certain race horses as 3-year property, for horses placed in service before Jan. 1, 2017 (regardless of age when placed in service).
- . . . Accelerated depreciation for business property on an Indian reservation, for property placed in service before Jan. 1, 2017. (**Code Sec. 168(j)**), as modified by Act Sec. 167(a)) For tax years beginning after Dec. 31, 2015, taxpayers can make an irrevocable election out of these accelerated depreciation rules for any class of property.
- . . . Election to treat 50% of the cost of any qualified mine safety equipment as an expense in the tax year in which the equipment is placed in service, for property placed in service before Jan. 1, 2017.

Please keep in mind that this is only a summary of these new provisions. If you would like to discuss this matter further, please do not hesitate to call.