

## B. Cost Recovery

### 1. Increased expensing (sec. 3101 of the House bill, secs. 13201 and 13311 of the Senate amendment, and sec. 168(k) of the Code)

#### Present Law

A taxpayer generally must capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over time through annual deductions for depreciation or amortization.<sup>431</sup>

#### Tangible property

Tangible property generally is depreciated under the modified accelerated cost recovery system (“MACRS”), which determines depreciation for different types of property based on an assigned applicable depreciation method, recovery period,<sup>432</sup> and convention.<sup>433</sup>

#### Bonus depreciation

An additional first-year depreciation deduction is allowed equal to 50 percent of the adjusted basis of qualified property acquired and placed in service before January 1, 2020 (January 1, 2021, for longer production period property<sup>434</sup> and certain aircraft<sup>435</sup>).<sup>436</sup> The 50-percent allowance is phased down for property placed in service after December 31, 2017 (after December 31, 2018 for longer production period property and certain aircraft). The bonus depreciation percentage rates are as follows.

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<sup>431</sup> See secs. 263(a) and 167. However, where property is not used exclusively in a taxpayer’s business, the amount eligible for a deduction must be reduced by the amount related to personal use. See, e.g., section 280A.

<sup>432</sup> The applicable recovery period for an asset is determined in part by statute and in part by historic Treasury guidance. Exercising authority granted by Congress, the Secretary issued Rev. Proc. 87-56, 1987-2 C.B. 674, laying out the framework of recovery periods for enumerated classes of assets. The Secretary clarified and modified the list of asset classes in Rev. Proc. 88-22, 1988-1 C.B. 785. In November 1988, Congress revoked the Secretary’s authority to modify the class lives of depreciable property. Rev. Proc. 87-56, as modified, remains in effect except to the extent that the Congress has, since 1988, statutorily modified the recovery period for certain depreciable assets, effectively superseding any administrative guidance with regard to such property.

<sup>433</sup> Sec. 168.

<sup>434</sup> As defined in section 168(k)(2)(B).

<sup>435</sup> As defined in section 168(k)(2)(C).

<sup>436</sup> Sec. 168(k). The additional first-year depreciation deduction is generally subject to the rules regarding whether a cost must be capitalized under section 263A.

| Placed in Service Year | Bonus Depreciation Percentage |  |
|------------------------|-------------------------------|--|
|                        | Qualified Property in General | Longer Production Period Property and Certain Aircraft |
| 2017                   | 50 percent                    | 50 percent   |
| 2018                   | 40 percent                    | 50 percent <sup>437</sup>                              |
| 2019                   | 30 percent                    | 40 percent   |
| 2020                   | None                          | 30 percent <sup>438</sup>                              |

The additional first-year depreciation deduction is allowed for both the regular tax and the alternative minimum tax (“AMT”),<sup>439</sup> but is not allowed in computing earnings and profits.<sup>440</sup> 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.<sup>441</sup> The amount of the additional first-year depreciation deduction is not affected by a short taxable year.<sup>442</sup> The taxpayer may elect out of the additional first-year depreciation for any class of property for any taxable year.<sup>443</sup>

The interaction of the additional first-year depreciation allowance with the otherwise applicable depreciation allowance may be illustrated as follows. Assume that in 2017 a taxpayer purchases new depreciable property and places it in service.<sup>444</sup> The property’s cost is \$10,000, and it is five-year property subject to the 200 percent declining balance method and half-year convention. The amount of additional first-year depreciation allowed is \$5,000. The remaining \$5,000 of the cost of the property is depreciable under the rules applicable to five-year property.

<sup>437</sup> It is intended that for longer production period property placed in service in 2018, 50 percent applies to the entire adjusted basis. Similarly, for longer production period property placed in service in 2019, 40 percent applies to the entire adjusted basis. A technical correction may be necessary with respect to longer production period property placed in service in 2018 and 2019 so that the statute reflects this intent.

<sup>438</sup> In the case of longer production period property described in section 168(k)(2)(B) and placed in service in 2020, 30 percent applies to the adjusted basis attributable to manufacture, construction, or production before January 1, 2020, and the remaining adjusted basis does not qualify for bonus depreciation. Thirty percent applies to the entire adjusted basis of certain aircraft described in section 168(k)(2)(C) and placed in service in 2020.

<sup>439</sup> Sec. 168(k)(2)(G). See also Treas. Reg. sec. 1.168(k)-1(d).

<sup>440</sup> Sec. 312(k)(3) and Treas. Reg. sec. 1.168(k)-1(f)(7).

<sup>441</sup> Sec. 168(k)(1)(B).

<sup>442</sup> *Ibid.*

<sup>443</sup> Sec. 168(k)(7). For the definition of a class of property, see Treas. Reg. sec. 1.168(k)-1(e)(2).

<sup>444</sup> Assume that the cost of the property is not eligible for expensing under section 179 or Treas. Reg. sec. 1.263(a)-1(f).

Thus, \$1,000 also is allowed as a depreciation deduction in 2017.<sup>445</sup> The total depreciation deduction with respect to the property for 2017 is \$6,000. The remaining \$4,000 adjusted basis of the property generally is recovered through otherwise applicable depreciation rules.

### Qualified property

Property qualifying for the additional first-year depreciation deduction must meet all of the following requirements.<sup>446</sup> First, the property must be: (1) property to which MACRS applies with an applicable recovery period of 20 years or less; (2) water utility property;<sup>447</sup> (3) computer software other than computer software covered by section 197; or (4) qualified improvement property.<sup>448</sup> Second, the original use<sup>449</sup> of the property must commence with the taxpayer.<sup>450</sup> Third, the taxpayer must acquire the property within the applicable time period (as described below). Finally, the property must be placed in service before January 1, 2020. As noted above, an extension of the placed-in-service date of one year (*i.e.*, before January 1, 2021) is provided for certain property with a recovery period of 10 years or longer, certain transportation property, and certain aircraft.<sup>451</sup>

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<sup>445</sup> \$1,000 results from the application of the half-year convention and the 200 percent declining balance method to the remaining \$5,000.

<sup>446</sup> Requirements relating to actions taken before 2008 are not described herein since they have little (if any) remaining effect.

<sup>447</sup> As defined in section 168(e)(5).

<sup>448</sup> The additional first-year depreciation deduction is not available for any property that is required to be depreciated under the alternative depreciation system of MACRS. Sec. 168(k)(2)(D)(i).

<sup>449</sup> The term “original use” means the first use to which the property is put, whether or not such use corresponds to the use of such property by the taxpayer. If in the normal course of its business a taxpayer sells fractional interests in property to unrelated third parties, then the original use of such property begins with the first user of each fractional interest (*i.e.*, each fractional owner is considered the original user of its proportionate share of the property). Treas. Reg. sec. 1.168(k)-1(b)(3).

<sup>450</sup> A special rule applies in the case of certain leased property. In the case of any property that is originally placed in service by a person and that is sold to the taxpayer and leased back to such person by the taxpayer within three months after the date that the property was placed in service, the property would be treated as originally placed in service by the taxpayer not earlier than the date that the property is used under the leaseback. If property is originally placed in service by a lessor, such property is sold within three months after the date that the property was placed in service, and the user of such property does not change, then the property is treated as originally placed in service by the taxpayer not earlier than the date of such sale. Sec. 168(k)(2)(E)(ii) and (iii).

<sup>451</sup> Property qualifying for the extended placed-in-service date must have an estimated production period exceeding one year and a cost exceeding \$1 million. Transportation property generally is defined as tangible personal property used in the trade or business of transporting persons or property. Certain aircraft which is not transportation property, other than for agricultural or firefighting uses, also qualifies for the extended placed-in-service date, if at the time of the contract for purchase, the purchaser made a nonrefundable deposit of the lesser of 10 percent of the cost or \$100,000, and which has an estimated production period exceeding four months and a cost exceeding \$200,000.

To qualify, property must be acquired (1) before January 1, 2020, or (2) pursuant to a binding written contract which was entered into before January 1, 2020. With respect to property that is manufactured, constructed, or produced by the taxpayer for use by the taxpayer, the taxpayer must begin the manufacture, construction, or production of the property before January 1, 2020.<sup>452</sup> Property that is manufactured, constructed, or produced for the taxpayer by another person under a contract that is entered into prior to the manufacture, construction, or production of the property is considered to be manufactured, constructed, or produced by the taxpayer.<sup>453</sup> For property eligible for the extended placed-in-service date, a special rule limits the amount of costs eligible for the additional first-year depreciation. With respect to such property, only the portion of the basis that is properly attributable to the costs incurred before January 1, 2020 (“progress expenditures”) is eligible for the additional first-year depreciation deduction.<sup>454</sup>

### Qualified improvement property

Qualified improvement property is any improvement to an interior portion of a building that is nonresidential real property if such improvement is placed in service after the date such building was first placed in service.<sup>455</sup> Qualified improvement property does not include any improvement for which the expenditure is attributable to the enlargement of the building, any elevator or escalator, or the internal structural framework of the building.

### Election to accelerate AMT credits in lieu of bonus depreciation

A corporation otherwise eligible for additional first-year depreciation may elect to claim additional AMT credits in lieu of claiming additional depreciation with respect to qualified property.<sup>456</sup> In the case of a corporation making this election, the straight line method is used for the regular tax and the AMT with respect to qualified property.<sup>457</sup>

A corporation making an election increases the tax liability limitation under section 53(c) on the use of minimum tax credits by the bonus depreciation amount. The aggregate increase in credits allowable by reason of the increased limitation is treated as refundable.

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<sup>452</sup> Sec. 168(k)(2)(E)(i).

<sup>453</sup> Treas. Reg. sec. 1.168(k)-1(b)(4)(iii).

<sup>454</sup> Sec. 168(k)(2)(B)(ii). For purposes of determining the amount of eligible progress expenditures, rules similar to section 46(d)(3) as in effect prior to the Tax Reform Act of 1986 apply.

<sup>455</sup> Sec. 168(k)(3).

<sup>456</sup> Sec. 168(k)(4).

<sup>457</sup> Sec. 168(k)(4)(A)(ii).

The bonus depreciation amount generally is equal to 20 percent of bonus depreciation for qualified property that could be claimed as a deduction absent an election under this provision.<sup>458</sup> As originally enacted, the bonus depreciation amount for all taxable years was limited to the lesser of (1) \$30 million or (2) six percent of the minimum tax credits allocable to the adjusted net minimum tax imposed for taxable years beginning before January 1, 2006. However, extensions of this provision have provided that this limitation applies separately to property subject to each extension.

For taxable years ending after December 31, 2015, the bonus depreciation amount for a taxable year (as defined under present law with respect to all qualified property) is limited to the lesser of (1) 50 percent of the minimum tax credit for the first taxable year ending after December 31, 2015 (determined before the application of any tax liability limitation) or (2) the minimum tax credit for the taxable year allocable to the adjusted net minimum tax imposed for taxable years ending before January 1, 2016 (determined before the application of any tax liability limitation and determined on a first-in, first-out basis).

All corporations treated as a single employer under section 52(a) are treated as one taxpayer for purposes of the limitation, as well as for electing the application of this provision.<sup>459</sup>

In the case of a corporation making an election which is a partner in a partnership, for purposes of determining the electing partner's distributive share of partnership items, bonus depreciation does not apply to any qualified property and the straight line method is used with respect to that property.<sup>460</sup>

In the case of a partnership having a single corporate partner owning (directly or indirectly) more than 50 percent of the capital and profits interests in the partnership, each partner takes into account its distributive share of partnership depreciation in determining its bonus depreciation amount.<sup>461</sup>

### Special rules

#### Passenger automobiles

The limitation under section 280F on the amount of depreciation deductions allowed with respect to certain passenger automobiles is increased in the first year by \$8,000 for automobiles that qualify (and for which the taxpayer does not elect out of the additional first-year

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<sup>458</sup> For this purpose, bonus depreciation is the difference between (i) the aggregate amount of depreciation determined if section 168(k)(1) applied to all qualified property placed in service during the taxable year and (ii) the amount of depreciation that would be so determined if section 168(k)(1) did not so apply. This determination is made using the most accelerated depreciation method and the shortest life otherwise allowable for each property.

<sup>459</sup> Sec. 168(k)(4)(B)(iii).

<sup>460</sup> Sec. 168(k)(4)(D)(ii).

<sup>461</sup> Sec. 168(k)(4)(D)(iii).

deduction).<sup>462</sup> The \$8,000 amount is phased down from \$8,000 by \$1,600 per calendar year beginning in 2018. Thus, the section 280F increase amount for property placed in service during 2018 is \$6,400, and during 2019 is \$4,800. While the underlying section 280F limitation is indexed for inflation,<sup>463</sup> the section 280F increase amount is not indexed for inflation. The increase does not apply to a taxpayer who elects to accelerate AMT credits in lieu of bonus depreciation for a taxable year.

#### Certain plants bearing fruits and nuts

A special election is provided for certain plants bearing fruits and nuts.<sup>464</sup> Under the election, the applicable percentage of the adjusted basis of a specified plant which is planted or grafted after December 31, 2015, and before January 1, 2020, is deductible for regular tax and AMT purposes in the year planted or grafted by the taxpayer, and the adjusted basis is reduced by the amount of the deduction.<sup>465</sup> The percentage is 50 percent for 2017, 40 percent for 2018, and 30 percent for 2019. A specified plant is any tree or vine that bears fruits or nuts, and any other plant that will have more than one yield of fruits or nuts and generally has a preproductive period of more than two years from planting or grafting to the time it begins bearing fruits or nuts.<sup>466</sup> The election is revocable only with the consent of the Secretary, and if the election is made with respect to any specified plant, such plant is not treated as qualified property eligible for bonus depreciation in the subsequent taxable year in which it is placed in service.

#### Long-term contracts

In general, in the case of a long-term contract, the taxable income from the contract is determined under the percentage-of-completion method.<sup>467</sup> Solely for purposes of determining the percentage of completion under section 460(b)(1)(A), the cost of qualified property with a MACRS recovery period of seven years or less is taken into account as a cost allocated to the contract as if bonus depreciation had not been enacted for property placed in service before January 1, 2020 (January 1, 2021, in the case of longer production period property).<sup>468</sup>

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<sup>462</sup> Sec. 168(k)(2)(F).

<sup>463</sup> Sec. 280F(d)(7).

<sup>464</sup> See sec. 168(k)(5).

<sup>465</sup> Any amount deducted under this election is not subject to capitalization under section 263A.

<sup>466</sup> A specified plant does not include any property that is planted or grafted outside the United States.

<sup>467</sup> Sec. 460.

<sup>468</sup> Sec. 460(c)(6). Other dates involving prior years are not described herein.

## **Intangible property**

MACRS does not apply to certain property, including any motion picture film, video tape, or sound recording, or to any other property if the taxpayer elects to exclude such property from MACRS and the taxpayer properly applies a unit-of-production method or other method of depreciation not expressed in a term of years.<sup>469</sup> Section 197 (amortization of goodwill and certain other intangibles) does not apply to certain intangible property, including certain property produced by the taxpayer or any interest in a film, sound recording, video tape, book or similar property not acquired in a transaction (or a series of related transactions) involving the acquisition of assets constituting a trade or business or substantial portion thereof.<sup>470</sup> Thus, the recovery of the cost of a film, video tape, or similar property that is produced by the taxpayer or is acquired on a “stand-alone” basis by the taxpayer may not be determined under either the MACRS depreciation provisions or under the section 197 amortization provisions. The cost recovery of such property may be determined under section 167, which allows a depreciation deduction for the reasonable allowance for the exhaustion, wear and tear, or obsolescence of the property if it is used in a trade or business or held for the production of income. In addition, the costs of motion picture films, video tapes, sound recordings, copyrights, books, and patents are eligible to be recovered using the income forecast method of depreciation.<sup>471</sup>

### **Expensing of certain qualified film, television and live theatrical productions**

Under section 181, a taxpayer may elect<sup>472</sup> to deduct the cost of any qualifying film, television and live theatrical production, commencing prior to January 1, 2017, in the year the expenditure is incurred in lieu of capitalizing the cost and recovering it through depreciation allowances.<sup>473</sup> A taxpayer may elect to deduct up to \$15 million of the aggregate cost of the film or television production under this section.<sup>474</sup> The threshold is increased to \$20 million if a significant amount of the production expenditures are incurred in areas eligible for designation as

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<sup>469</sup> Sec. 168(f)(1), (3) and (4).

<sup>470</sup> Sec. 197(c)(2) and (e)(4)(A). If section 197 applies to the acquisition of intangible assets held in connection with a trade or business, any value properly attributable to a “section 197 intangible” is amortizable on a straight-line basis over 15 years. Sec. 197(a) and (c).

<sup>471</sup> Sec. 167(g)(6). Under the income forecast method, a property’s depreciation deduction for a taxable year is determined by multiplying the adjusted basis of the property by a fraction, the numerator of which is the gross income generated by the property during the year, and the denominator of which is the total forecasted or estimated gross income expected to be generated prior to the close of the tenth taxable year after the year the property is placed in service. Any costs that are not recovered by the end of the tenth taxable year after the property is placed in service may be taken into account as depreciation in that year. Sec. 167(g)(1).

<sup>472</sup> See Treas. Reg. sec. 1.181-2 for rules on making an election under this section.

<sup>473</sup> For this purpose, a qualified film or television production is treated as commencing on the first date of principal photography. The date on which a qualified live theatrical production commences is the date of the first public performance of such production for a paying audience.

<sup>474</sup> Sec. 181(a)(2)(A). See Treas. Reg. sec. 1.181-1 for rules on determining eligible production costs.

a low-income community or eligible for designation by the Delta Regional Authority as a distressed county or isolated area of distress.<sup>475</sup>

A qualified film, television or live theatrical production means any production of a motion picture (whether released theatrically or directly to video cassette or any other format), television program or live staged play if at least 75 percent of the total compensation expended on the production is for services performed in the United States by actors, directors, producers, and other relevant production personnel.<sup>476</sup> The term “compensation” does not include participations and residuals (as defined in section 167(g)(7)(B)).<sup>477</sup>

Each episode of a television series is treated as a separate production, and only the first 44 episodes of a particular series qualify under the provision.<sup>478</sup> Qualified productions do not include sexually explicit productions as referenced by section 2257 of title 18 of the U.S. Code.<sup>479</sup>

A qualified live theatrical production is defined as a live staged production of a play (with or without music) which is derived from a written book or script and is produced or presented by a commercial entity in any venue which has an audience capacity of not more than 3,000, or a series of venues the majority of which have an audience capacity of not more than 3,000.<sup>480</sup> In addition, qualified live theatrical productions include any live staged production which is produced or presented by a taxable entity no more than 10 weeks annually in any venue which has an audience capacity of not more than 6,500.<sup>481</sup> In general, in the case of multiple live-staged productions, each such live-staged production is treated as a separate production. Similar to the exclusion for sexually explicit productions from the definition of qualified film or television productions, qualified live theatrical productions do not include stage performances that would be excluded by section 2257(h)(1) of title 18 of the U.S. Code, if such provision were extended to live stage performances.<sup>482</sup>

For purposes of recapture under section 1245, any deduction allowed under section 181 is treated as if it were a deduction allowable for amortization.<sup>483</sup>

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<sup>475</sup> Sec. 181(a)(2)(B).

<sup>476</sup> Sec. 181(d)(3)(A).

<sup>477</sup> Sec. 181(d)(3)(B).

<sup>478</sup> Sec. 181(d)(2)(B).

<sup>479</sup> Sec. 181(d)(2)(C).

<sup>480</sup> Sec. 181(e)(2)(A).

<sup>481</sup> Sec. 181(e)(2)(D).

<sup>482</sup> Sec. 181(e)(2)(E).

<sup>483</sup> Sec. 1245(a)(2)(C).



## House Bill

### Full expensing for certain business assets

The provision extends and modifies the additional first-year depreciation deduction through 2022 (through 2023 for longer production period property and certain aircraft). The 50-percent allowance is increased to 100 percent for property acquired and placed in service after September 27, 2017, and before January 1, 2023 (January 1, 2024, for longer production period property and certain aircraft), as well as for specified plants planted or grafted after September 27, 2017, and before January 1, 2023.

#### Special rules

The \$8,000 increase amount in the limitation on the depreciation deductions allowed with respect to certain passenger automobiles is increased to \$16,000 for passenger automobiles acquired and placed in service after September 27, 2017, and before January 1, 2023.

The provision extends the special rule under the percentage-of-completion method for the allocation of bonus depreciation to a long-term contract for property placed in service before January 1, 2023 (January 1, 2024, in the case of longer production period property).

### Application to used property

The provision removes the requirement that the original use of qualified property must commence with the taxpayer. Thus, the provision applies to purchases of used as well as new items. To prevent abuses, the additional first-year depreciation deduction applies only to property purchased in an arm's-length transaction. It does not apply to property received as a gift or from a decedent.<sup>484</sup> In the case of trade-ins, like-kind exchanges, or involuntary conversions, it applies only to any money paid in addition to the traded-in property or in excess of the adjusted basis of the replaced property.<sup>485</sup> It does not apply to property acquired in a nontaxable exchange such as a reorganization, to property acquired from a member of the taxpayer's family, including a spouse, ancestors, and lineal descendants, or from another related entity as defined in section 267, nor to property acquired from a person who controls, is controlled by, or is under common control with, the taxpayer.<sup>486</sup> Thus it does not apply, for example, if one member of an affiliated group of corporations purchases property from another member, or if an individual who controls a corporation purchases property from that corporation.

### Exception for certain businesses not subject to limitation on interest expense

The provision excludes from the definition of qualified property any property used in a real property trade or business, *i.e.*, any real property development, redevelopment, construction,

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<sup>484</sup> By reference to section 179(d)(2)(C). See also Treas. Reg. sec. 1.179-4(c)(1)(iv).

<sup>485</sup> By reference to section 179(d)(3). See also Treas. Reg. sec. 1.179-4(d).

<sup>486</sup> By reference to section 179(d)(2)(A) and (B). See also Treas. Reg. sec. 1.179-4(c).

reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business.<sup>487</sup>

The provision also excludes from the definition of qualified property any property used in the trade or business of certain regulated public utilities, *i.e.*, the trade or business of the furnishing or sale of (1) electrical energy, water, or sewage disposal services, (2) gas or steam through a local distribution system, or (3) transportation of gas or steam by pipeline, if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.<sup>488</sup>

In addition, the provision excludes from the definition of qualified property any property used in a trade or business that has had floor plan financing indebtedness,<sup>489</sup> unless the taxpayer with such trade or business is not a tax shelter prohibited from using the cash method and is exempt from the interest limitation rules in section 3301 of the bill by meeting the \$25 million gross receipts test of section 448(c).

### **Election to accelerate AMT credits in lieu of bonus depreciation**

As a conforming amendment to the repeal of AMT,<sup>490</sup> the provision repeals the election to accelerate AMT credits in lieu of bonus depreciation.

### **Transition rule**

The present-law phase-down of bonus depreciation is maintained for property acquired before September 28, 2017, and placed in service after September 27, 2017. Under the provision, in the case of property acquired and adjusted basis incurred before September 28, 2017, the bonus depreciation rates are as follows.

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<sup>487</sup> As defined in section 3301 of the House bill (Interest), by cross reference to section 469(c)(7)(C). Note that a mortgage broker who is a broker of financial instruments is not in a real property trade or business for this purpose. See, *e.g.*, CCA 201504010 (December 17, 2014).

<sup>488</sup> As defined in section 3301 of the House bill (Interest).

<sup>489</sup> As defined in section 3301 of the House bill (Interest).

<sup>490</sup> See section 2001 of the House bill (Repeal of alternative minimum tax).

| <b>Phase-Down for Portion of Basis of Qualified Property<br/>Acquired before September 28, 2017</b> |  |   |
|---|--|---|
| <b>Placed in Service Year</b>   | <b>Bonus Depreciation Percentage</b>     |   |
|   | <b>Qualified Property<br/>in General</b> | <b>Longer Production Period<br/>Property and<br/>Certain Aircraft</b> |
| 2017  | 50 percent                               | 50 percent  |
| 2018  | 40 percent                               | 50 percent  |
| 2019  | 30 percent                               | 40 percent  |
| 2020  | None                                     | 30 percent  |

Similarly, the section 280F increase amount in the limitation on the depreciation deductions allowed with respect to certain passenger automobiles acquired before September 28, 2017, and placed in service after September 27, 2017, is \$8,000 for 2017, \$6,400 for 2018, and \$4,800 for 2019.

Effective date.—The provision generally applies to property acquired<sup>491</sup> and placed in service after September 27, 2017, and to specified plants planted or grafted after such date.

A transition rule provides that, for a taxpayer’s first taxable year ending after September 27, 2017, the taxpayer may elect to apply section 168 without regard to the amendments made by this provision.

In the case of any taxable year that includes any portion of the period beginning on September 28, 2017, and ending on December 31, 2017, the amount of any net operating loss for such taxable year which may be treated as a net operating loss carryback is determined without regard to the amendments made by this provision.<sup>492</sup>

**Senate Amendment**

**In general**

The provision extends and modifies the additional first-year depreciation deduction through 2026 (through 2027 for longer production period property and certain aircraft). The 50-percent allowance is increased to 100 percent for property placed in service after September 27, 2017, and before January 1, 2023 (January 1, 2024, for longer production period property and certain aircraft), as well as for specified plants planted or grafted after September 27, 2017, and before January 1, 2023. Thus, the provision repeals the phase-down of the 50-percent allowance for property placed in service after December 31, 2017, and for specified plants planted or

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<sup>491</sup> Property is not treated as acquired after the date on which a written binding contract is entered into for such acquisition.

<sup>492</sup> See section 3302 of the House bill (Modification of net operating loss deduction).

grafted after such date. The 100-percent allowance is phased down by 20 percent per calendar year for property placed in service, and specified plants planted or grafted, in taxable years beginning after 2022 (after 2023 for longer production period property and certain aircraft). Under the provision, the bonus depreciation percentage rates are as follows.

| Placed in Service Year <sup>493</sup> | Bonus Depreciation Percentage |  |
|---------------------------------------|-------------------------------|--|
|                                       | Qualified Property in General | Longer Production Period Property and Certain Aircraft |
| 2023                                  | 80 percent                    | 100 percent  |
| 2024                                  | 60 percent                    | 80 percent   |
| 2025                                  | 40 percent                    | 60 percent   |
| 2026                                  | 20 percent                    | 40 percent   |
| 2027                                  | None                          | 20 percent <sup>494</sup>                              |

### Special rules

The provision maintains the section 280F increase amount of \$8,000 for passenger automobiles placed in service after December 31, 2017.

The provision extends the special rule under the percentage-of-completion method for the allocation of bonus depreciation to a long-term contract for property placed in service before January 1, 2027 (January 1, 2028, in the case of longer production period property).

### **Application to qualified film, television and live theatrical productions**

The provision expands the definition of qualified property eligible for the additional first-year depreciation allowance to include qualified film, television and live theatrical productions<sup>495</sup> placed in service after September 27, 2017, and before January 1, 2027, for which a deduction otherwise would have been allowable under section 181 without regard to the dollar limitation or termination of such section. For purposes of this provision, a production is considered placed in service at the time of initial release, broadcast, or live staged performance (*i.e.*, at the time of the first commercial exhibition, broadcast, or live staged performance of a production to an audience).

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<sup>493</sup> In the case of specified plants, this is the year of planting or grafting.

<sup>494</sup> Twenty percent applies to the adjusted basis attributable to manufacture, construction, or production before January 1, 2027, and the remaining adjusted basis does not qualify for bonus depreciation. Twenty percent applies to the entire adjusted basis of certain aircraft described in section 168(k)(2)(C) and placed in service in 2027.

<sup>495</sup> As defined in section 181(d) and (e).

## **Exception for certain businesses not subject to limitation on interest expense**

The provision excludes from the definition of qualified property any property which is primarily used in the trade or business of the furnishing<sup>496</sup> or sale of (1) electrical energy, water, or sewage disposal services, (2) gas or steam through a local distribution system, or (3) transportation of gas or steam by pipeline, if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, by a public service or public utility commission or other similar body of any State or political subdivision thereof, or by the governing or ratemaking body of an electric cooperative.<sup>497</sup>

In addition, the provision excludes from the definition of qualified property any property used in a trade or business that has had floor plan financing indebtedness,<sup>498</sup> unless the taxpayer with such trade or business is not a tax shelter prohibited from using the cash method and is exempt from the interest limitation rules in section 13301 of the Senate amendment by meeting the small business gross receipts test of section 448(c).

Effective date.—The provision generally applies to property placed in service after September 27, 2017, in taxable years ending after such date, and to specified plants planted or grafted after such date.

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.<sup>499</sup>

## **Conference Agreement**

The conference agreement follows the Senate amendment but also includes the House bill's removal of the requirement that the original use of qualified property must commence with the taxpayer (*i.e.*, it allows the additional first-year depreciation deduction for new and used property).

In addition, the conference agreement also follows the House bill's application of the present-law phase-down of bonus depreciation to property acquired before September 28, 2017, and placed in service after September 27, 2017, as well as the present-law phase-down of the section 280F increase amount in the limitation on the depreciation deductions allowed with respect to certain passenger automobiles acquired before September 28, 2017, and placed in

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<sup>496</sup> The term "furnishing" includes generation, transmission, and distribution activities.

<sup>497</sup> See sec. 13301 of the Senate amendment (Limitation on deduction for interest).

<sup>498</sup> As defined in section 13311 of the Senate amendment (Floor plan financing).

<sup>499</sup> Such election shall be made at such time and in such form and manner as prescribed by the Secretary.

service after September 27, 2017. Under the conference agreement, the bonus depreciation rates are as follows.

| Placed in Service Year <sup>500</sup>  | Bonus Depreciation Percentage                  |  |
|--|--|--|
|  | Qualified Property in General/Specified Plants | Longer Production Period Property and Certain Aircraft |
| <b>Portion of Basis of Qualified Property Acquired before Sept. 28, 2017</b> |  |  |
| Sept. 28, 2017 – Dec. 31, 2017   | 50 percent                                     | 50 percent   |
| 2018   | 40 percent                                     | 50 percent   |
| 2019   | 30 percent                                     | 40 percent   |
| 2020   | None   | 30 percent <sup>501</sup>                              |
| 2021 and thereafter  | None   | None   |
| <b>Portion of Basis of Qualified Property Acquired after Sept. 27, 2017</b>  |  |  |
| Sept. 28, 2017 – Dec. 31, 2022   | 100 percent                                    | 100 percent  |
| 2023   | 80 percent                                     | 100 percent  |
| 2024   | 60 percent                                     | 80 percent   |
| 2025   | 40 percent                                     | 60 percent   |
| 2026   | 20 percent                                     | 40 percent   |
| 2027   | None   | 20 percent <sup>502</sup>                              |
| 2028 and thereafter  | None   | None   |

As a conforming amendment to the repeal of corporate AMT, the conference agreement repeals the election to accelerate AMT credits in lieu of bonus depreciation.

Effective date.—The provision generally applies to property acquired and placed in service after September 27, 2017, and to specified plants planted or grafted after such date.

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<sup>500</sup> In the case of specified plants, this is the year of planting or grafting.

<sup>501</sup> Thirty percent applies to the adjusted basis attributable to manufacture, construction, or production before January 1, 2020, and the remaining adjusted basis does not qualify for bonus depreciation. Thirty percent applies to the entire adjusted basis of certain aircraft described in section 168(k)(2)(C) and placed in service in 2020.

<sup>502</sup> Twenty percent applies to the adjusted basis attributable to manufacture, construction, or production before January 1, 2027, and the remaining adjusted basis does not qualify for bonus depreciation. Twenty percent applies to the entire adjusted basis of certain aircraft described in section 168(k)(2)(C) and placed in service in 2027.

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.

## **2. Modifications to depreciation limitations on luxury automobiles and personal use property (sec. 13202 of the Senate amendment and sec. 280F of the Code)**

### **Present Law**

Section 280F(a) limits the annual cost recovery deduction with respect to certain passenger automobiles. This limitation is commonly referred to as the "luxury automobile depreciation limitation." For passenger automobiles placed in service in 2017, and for which the additional first-year depreciation deduction under section 168(k) is not claimed, the maximum amount of allowable depreciation is \$3,160 for the year in which the vehicle is placed in service, \$5,100 for the second year, \$3,050 for the third year, and \$1,875 for the fourth and later years in the recovery period.<sup>503</sup> This limitation is indexed for inflation and applies to the aggregate deduction provided under present law for depreciation and section 179 expensing. Hence, passenger automobiles subject to section 280F are eligible for section 179 expensing only to the extent of the applicable limits contained in section 280F. For passenger automobiles eligible for the additional first-year depreciation allowance in 2017, the first-year limitation is increased by an additional \$8,000.<sup>504</sup>

For purposes of the depreciation limitation, passenger automobiles are defined broadly to include any four-wheeled vehicles that are manufactured primarily for use on public streets, roads, and highways and which are rated at 6,000 pounds unloaded gross vehicle weight or less.<sup>505</sup> In the case of a truck or a van, the depreciation limitation applies to vehicles that are rated at 6,000 pounds gross vehicle weight or less. Sport utility vehicles are treated as a truck for the purpose of applying the section 280F limitation.

Basis not recovered in the recovery period of a passenger automobile is allowable as an expense in subsequent taxable years.<sup>506</sup> The expensed amount is limited in each such subsequent taxable year to the amount of the limitation in the fourth year in the recovery period.

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<sup>503</sup> Rev. Proc. 2017-29, Table 3, 2017-14 I.R.B. 1065.

<sup>504</sup> Sec. 168(k)(2)(F). For proposed changes to section 168(k), see section II.B.1. of this document (Increased expensing).

<sup>505</sup> Sec. 280F(d)(5). Exceptions are provided for any ambulance, hearse, or combination ambulance-hearse used by the taxpayer directly in a trade or business, or any vehicle used by the taxpayer directly in the trade or business of transporting persons or property for compensation or hire.

<sup>506</sup> Sec. 280F(a)(1)(B).