

Proposed Bonus Depreciation Regulations Detail TCJA Requirements

By Kristine A. Tidgren | August 11, 2018



On August 3, IRS issued proposed regulations, [REG-104397-18](#), to detail how bonus depreciation (the additional first-year depreciation deduction) under IRC § 168(k) should work in light of changes made by the Tax Cuts and Jobs Act, PL 115-97. Guidance provided in the proposed regulations closely tracks the statutory language, updates existing guidance (Prop. Treas. Reg. § 1.168(k)-1) and creates a new subsection of rules (Prop. Treas. Reg. § 1.168(k)-2).

Generally, the TCJA modified bonus depreciation in the following key ways:

- Increasing the additional first-year depreciation deduction from 50 to 100 percent
- Expanding property eligible for bonus depreciation to include certain **used** property and certain film, television, or live theatrical productions
- Allowing 100 percent bonus depreciation for qualified property acquired and placed in service after September 27, 2017, and placed in service before January 1, 2023 (property is not treated as acquired after the date on which a written binding contract is entered into for such acquisition; letters of intent do not count as written binding contracts, and delivery dates don't alter the terms in a binding contract)
- Allowing 100-percent additional first-year depreciation deduction for a specified plant planted or grafted after September 27, 2017, and before January 1, 2023 (if taxpayers elects)
- Decreasing the 100-percent additional first year depreciation deduction by 20 percent annually for qualified property placed in service, or a specified plant planted or grafted, after December 31, 2022
- Extending the placed-in-service date for eligible property from before January 1, 2020, to before January 1, 2027

The TCJA also repealed (1) the election to accelerate alternative minimum tax credits in lieu of the additional first year depreciation deduction for taxable years beginning after December 31, 2017 and (2) IRC § 168(k)(3) (relating to qualified improvement property) for property placed in service after December 31, 2017 (more on this below).

Eligibility Requirements

Generally, the TCJA and proposed regulations require that to qualify for bonus depreciation:

1. the depreciable property must be of a specified type

2. the original use of the depreciable property must commence with the taxpayer or used depreciable property must meet certain acquisition requirements
3. the depreciable property must be placed in service by the taxpayer within a specified time period or must be planted or grafted by the taxpayer before a specified date
4. the depreciable property must be acquired by the taxpayer after September 27, 2017

Qualified Property

Specifically, the regulations track the TCJA and provide that, to be qualified property, it must be:

- MACRS property that has a recovery period of 20 years or less
- Computer software as defined in, and depreciated under, IRC § 167(f)(1)
- Certain water utility property
- Certain qualified film or television productions
- Certain qualified live theatrical productions
- A specified plant as defined in section 168(k)(5)(B) and for which the taxpayer has made an election to apply section 168(k)(5)
- Qualified improvement property acquired after September 27, 2017, and placed in service after September 27, 2017, and before January 1, 2018

Qualified Improvement Property

The proposed regulations do not specifically address the fact that for property placed in service after December 31, 2017, the TCJA eliminated the 15-year MACRS classification for qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property and amended IRC § 168(k) to eliminate qualified improvement property as a specific category of qualified property. Instead, the proposed regulations allow additional first-year depreciation **only** on qualified improvement property acquired and placed in service after September 27, 2017, and before January 1, 2018. The proposed regulations leave it to Congress to make a technical correction for qualified improvement property placed in service after December 31, 2018. For now, this property remains 39-year property, not eligible for bonus. For more information on this problem, click [here](#).

Note: On August 16, 2018, Senate Finance Republicans sent a [letter](#) to Treasury and IRS, stating that a drafting error was made and that Congress intended that qualified improvement property would have a 15-year MACRS life and would, thus, be eligible for bonus depreciation.

Property Not Eligible for Bonus Depreciation

The following types of property are generally not eligible for the additional first-year depreciation deduction:

- Property described in IRC § 168(f), such as automobiles for which the taxpayer uses the optional business standard mileage rate
- Property required to be depreciated under ADS
- Property in a class for which the taxpayer elects not to take bonus
- A specified plant for which the taxpayer made an election to apply the special bonus depreciation allowed under IRC § 168(k)(5) during a prior tax year
- Property placed in service and disposed of in the same taxable year (except in the case of the technical termination of a partnership)

Used Property Requirements

The proposed regulations largely point to provisions already in place for IRC § 179 to prevent potential abuse related to taxpayers claiming bonus depreciation for used property. Three requirements must be met for used property to qualify:

- The property must not have been previously used by the taxpayer or a predecessor prior to acquisition.
 - This previous use is limited to situations where the taxpayer had a depreciable interest in the property

- The acquisition cannot be from certain related parties or received by gift or inheritance
 - The proposed regulations also include provisions restricting bonus in certain series of related transactions involving members of consolidated groups
- The cost of the acquired property cannot depend on the basis of other property held by the purchaser

Partnership Adjustment Issues Stemming from Used Property Requirements

IRC § 704(c) allows depreciation of remedial allocations in situations where partners contribute depreciable property to a partnership and the partnership's book value in the property is higher than its adjusted tax basis. The proposed regulations state that these remedial allocations do not qualify for bonus depreciation. This is because in such transactions, the partnership's basis is determined by reference to the contributing partner's basis, thus violation IRC § 179(d)(2)(C). The proposed regulations also provide that IRC § 734(b) basis step-ups are not eligible for the additional first-year depreciation deduction. In contrast, the proposed regulation do allow bonus depreciation for some partnership IRC § 743 adjustments made when a new partner enters a partnership and a section 754 election is made. It is possible that these rules will be revised before the final regulations are issued.

Elections

The proposed regulations retain the general rule that elections out of bonus depreciation can be made on a class-by-class basis. The special election to apply 50 percent bonus to property acquired by a taxpayer and placed in service during its taxable year that includes September 28, 2017, however, must be made for all qualifying property or not at all.

Application

Until final regulations are issued, taxpayers may apply the proposed regulations to property placed in service after September 27, 2017.

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