

KBKG TAX INSIGHT: IMPACT OF FINAL REGULATIONS AND NEW PROPOSED REGULATIONS FOR ADDITIONAL FIRST YEAR DEPRECIATION DEDUCTION

On September 13, 2019, the IRS and Treasury finalized first-year bonus regulations ([REG-104397-18](#)).

The final regulations adopt the proposed regulations which were released in August 2018 with some modifications.

On September 13, 2019, the IRS and Treasury Department released the much-anticipated final regulations that provide guidance regarding additional first year bonus depreciation deductions under section 168(k) of the Internal Revenue Code ([REG-104397-18](#)). While the final regulations cleared up some issues, there are still a few issues left to be resolved. The IRS and Treasury Department released an additional set of proposed regulations ([REG-106808-19](#)) to provide some more guidance on issues that were not previously addressed and has provided an October 23, 2019, deadline to submit commentary.

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The final regulations adopt the proposed regulations which were released in August 2018 with some modifications. The regulations address operational rules including; how to compute bonus depreciation, how to make certain elections under IRC Sec 168(k), and what qualifications must be met for bonus depreciation to be available.

Qualified Improvement Property:

Many taxpayers will be disappointed to see that the long-awaited technical corrections to Qualified Improvement Property (QIP) were not included in the final regulations. Although multiple commenters requested clarification that “QIP” placed into service after 2017 be considered “qualified property,” the Treasury Department and IRS declined to adopt commentary. Consequently, a legislative change must be enacted to provide a recovery period of 20 years or less for qualified improvement property placed into service after 2017 to be eligible for bonus depreciation.

Acquired and Self- Constructed Property:

The IRS and Treasury Department provided some relief for taxpayers who were struggling with the acquisition rules related to property constructed for a taxpayer by a third party. Under the proposed regulations, property that was manufactured, constructed, or produced for the taxpayer by another person under a written binding contract was considered “acquired” pursuant to a written binding contract. The final regulations provide that this type of property is now to be treated as self-constructed property. Taxpayers will no longer be weighed down by the “administrative burden” of determining the appropriate date in which the written binding contract was entered. Instead, the acquisition rule will be met under the self-constructed property rules for determining when construction of a substantial nature has been completed.

In addition, the final regulations provided some clarity on the acquisition date of used property acquired pursuant to a written binding contract. The date is determined to be the later of:

- the date on which the contract is entered;
- the date on which the contract is enforceable

under state law;

- if the contract has one or more cancellation periods, the date on which all cancellation periods end; or
- if the contract has one or more contingency clauses, the date on which all conditions subject to such clauses are satisfied.

Component Elections:

The proposed regulations provide that a taxpayer can make a special election to claim the 100% bonus rate on certain components acquired or self-constructed after September 27, 2017 that are part of larger new construction projects where construction began before September 28, 2017. The election was included after multiple commenters requested an election similar to the one provided in section 3.02(2)(b) of Rev. Proc. 2011-26. The proposed regulations provide the time and manner of making the election and provide examples to illustrate the proposed rules. The larger property must be eligible for bonus depreciation at the 50% rate. This is a significant change because in most cases taxpayers were advised to take bonus depreciation under the PATH Act rules at a rate of 40% in 2018 and 30% in 2019 for eligible property where construction began prior to September 28, 2017 but was completed and placed in service in 2018 and 2019.

Floor Plan Financing Provision:

The proposed regulations clarified that taxpayers leasing property to a trade or business with floor plan financing indebtedness or a rate-regulated utility may claim bonus depreciation provided the lessor is not described in section 168(k)(9)(A) or (B) and provided that all other requirements are met. However, section 1.168(k)-2(b)(2)(ii)(F) of the final regulations hold that taxpayers that operate these businesses as defined in section 163(j)(7)(A)(iv) are still excluded from additional first year bonus depreciation. This could be potentially good news for lessors of dealerships.

Previously Held Depreciable Interest in Newly Acquired Property:

The final regulations provide a definition for the

term “predecessor” as it relates to a taxpayer or their predecessor having a prior depreciable interest in acquired property. They define predecessor as:

- a transferor of an asset to a transferee in a transaction to which section 381(a) applies;
- a transferor of an asset to a transferee in a transaction in which the transferee’s basis in the asset is determined, in whole or in part, by reference to the basis of the asset in the hands of the transferor;
- a partnership that is considered as continuing under section 708(b)(2) and section 1.708-1;
- the decedent in the case of an asset acquired by an estate; or
- a transferor of an asset to a trust.

The IRS and Treasury Department now provide a lookback period of 5 years for determining whether a taxpayer or predecessor held a depreciable interest in property. This is a departure from proposed regulations. The IRS remarks that “this bright-line test will be easy for both taxpayers and the IRS to administer.”

Taxpayers who acquire property and then dispose of that property within 90 days of placing that property in service are considered to have no prior depreciable interest in that property. If the property is subsequently reacquired by the taxpayer, then the taxpayer is eligible for the 100% bonus rate. The IRS and Treasury Department point out that this rule does not apply if the taxpayer reacquires the property in the same taxable year in which it was disposed.

A taxpayer may choose to apply the final regulations, in their entirety, to qualified property acquired and placed in service after September 27, 2017 provided the taxpayer consistently applies all the rules in the final regulations. In addition, a taxpayer may rely on the proposed regulations under section 168(k) issued on August 8, 2018 to property acquired and placed in service after September 27, 2017, by the taxpayer during taxable years ending before the date of publication of the final regulations.

The final regulations adopt proposed regulations published in the Federal Register (REG-104397-18) with certain modifications. These regulations now



provide Taxpayers with only some clarity, but they delay clarification on key issues impacting Taxpayers in the current tax year and beyond.

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*To find out more about how
the Final Additional First-Year
Depreciation Deduction rules
impact you, contact us today.*