Bonus Regulations

Transition Rules regarding September 27, 2017

Explanation

5. Date of Acquisition

The proposed regulations provide rules applicable to the acquisition requirements of the effective date under section 13201(h) of the Act. The proposed regulations provide that these rules apply to all property, including self-constructed property or property described in section 168(k)(2)(B) or (C).

A. Written Binding Contract

Pursuant to section 13201(h)(1)(A) of the Act, the proposed regulations provide that the property must be acquired by the taxpayer after September 27, 2017, or, acquired by the taxpayer pursuant to a written binding contract entered into by the taxpayer after September 27, 2017. Because of the clear language of section 13201(h)(1) of the Act regarding written binding contracts, the proposed regulations also provide that property that is manufactured, constructed, or produced for the taxpayer by another person under a written binding contract that is entered into prior to the manufacture, construction, or production of the property for use by the taxpayer in its trade or business or for its production of income is acquired pursuant to a written binding contract. Further, if the written binding contract states the date on which the contract was entered into and a closing date, delivery date, or other similar date, the date on which the contract was entered into is the date the taxpayer acquired the property. The proposed regulations retain the rules in §1.168(k)-1(b)(4)(ii) defining a binding contract. Additionally, the proposed regulations provide that a letter of intent for an acquisition is not a binding contract.

B. Self-Constructed Property

If a taxpayer manufactures, constructs, or produces property for its own use, the Treasury Department and the IRS recognize that the written binding contract rule in section 13201(h)(1) of the Act does not apply. In such case, the proposed regulations provide that the acquisition rules in section 13201(h)(1) of the Act are treated as met if the taxpayer begins manufacturing, constructing, or producing the property after September 27, 2017. The proposed regulations provide rules similar to those in §1.168(k)-1(b)(4)(iii)(B) for defining when manufacturing, construction, or production begins, including the safe harbor, and in §1.168(k)-1(b)(4)(iii)(C) for a contract to acquire, or for the manufacture, construction, or production of, a component of the larger self-constructed property. As stated in the preceding paragraph, these self-constructed rules in the proposed regulations do not apply to property that is manufactured, constructed, or produced for the taxpayer by another person under a written binding contract that is entered into prior to the manufacture, construction, or production of the property.

Regulations

(5) Acquisition of property—(i) In general. This paragraph (b)(5) provides rules for the acquisition requirements in section 13201(h) of the Act. These rules apply to all property, including self-constructed property or property described in section 168(k)(2)(B) or (C).

(ii) Acquisition date. Except as provided in paragraph (b)(5)(vi) of this section, depreciable property will meet the requirements of this paragraph (b)(5) if the property is acquired by the taxpayer after September 27, 2017, or is acquired by the taxpayer pursuant to a written binding contract entered into by the taxpayer after September 27, 2017. Property that is manufactured, constructed, or produced for the taxpayer by another person under a written binding contract that is entered into prior to the manufacture, construction, or production of the property for use by the taxpayer in its trade or business or for its production of income is acquired pursuant to a written binding contract. If a taxpayer acquired the property pursuant to a written binding contract and such contract states the date on which the contract was entered into and a closing date, delivery date, or other similar date, the date on which the contract was entered into is the date the taxpayer acquired the property. See paragraph (b)(5)(v) of this section for when a qualified film, television, or live theatrical production is treated as acquired for purposes of this paragraph (b)(5).

(iii) Definition of binding contract—(A) In general. A contract is binding only if it is enforceable under State law against the taxpayer or a predecessor, and does not limit damages to a specified amount (for example, by use of a liquidated damages provision). For this purpose, a contractual provision that limits damages to an amount equal to at least 5 percent of the total contract price will not be treated as limiting damages to a specified amount. In determining whether a contract limits damages, the fact that there may be little or no damages because the contract price does not significantly differ from fair market value will not be taken into account. For example, if a taxpayer entered into an irrevocable written contract to purchase an asset for $100 and the contract did not contain a provision for liquidated damages, the contract is considered binding notwithstanding the fact that the asset had a fair market value of $99 and under local law the seller would only recover the difference in the event the purchaser failed to perform. If the contract provided for a full refund of the purchase price in lieu of any damages allowable by law in the event of breach or cancellation, the contract is not considered binding.

(B) Conditions. A contract is binding even if subject to a condition, as long as the condition is not within the control of either party or a predecessor. A contract will continue to be binding if the parties make insubstantial changes in its terms and conditions or if any term is to be determined by a standard beyond the control of either party. A contract that imposes significant obligations on the taxpayer or a predecessor will be treated as binding notwithstanding the fact that certain terms remain to be negotiated by the parties to the contract.

(C) Options. An option to either acquire or sell property is not a binding contract.

(D) Letter of intent. A letter of intent for an acquisition is not a binding contract.

(E) Supply agreements. A binding contract does not include a supply or similar agreement if the amount and design specifications of the property to be purchased have not been specified. The contract will not be a binding contract for the property to be purchased until both the amount and the design specifications are specified. For example, if the provisions of a supply or similar agreement state the design specifications of the property to be purchased, a purchase order under the agreement for a specific number of assets is treated as a binding contract.

(F) Components. A binding contract to acquire one or more components of a larger property will not be treated as a binding contract to acquire the larger property. If a binding contract to acquire the component does not satisfy the requirements of this paragraph (b)(5), the component does not qualify for the additional first year depreciation deduction.

(iv) Self-constructed property—(A) In general. If a taxpayer manufactures, constructs, or produces property for use by the taxpayer in its trade or business or for its production of income, the acquisition rules in paragraph (b) (5)(ii) of this section are treated as met for the property if the taxpayer begins manufacturing, constructing, or producing the property after September 27, 2017. This paragraph (b)(5)(iv) does not apply to property that is manufactured, constructed, or produced for the taxpayer by another person under a written binding contract that is entered into prior to the manufacture, construction, or production of the property for use by the taxpayer in its trade or business or for its production of income (for further guidance, see paragraphs (b)(5)(ii) and (iii) of this section).

(B) When does manufacture, construction, or production begin—(1) In general. For purposes of paragraph (b) (5)(iv)(A) of this section, manufacture, construction, or production of property begins when physical work of a significant nature begins. Physical work does not include preliminary activities such as planning or designing, securing financing, exploring, or researching. The determination of when physical work of a significant nature begins depends on the facts and circumstances. For example, if the taxpayer constructs a retail motor fuels outlet on-site for use by the taxpayer in its trade or business, construction begins when physical work of a significant nature commences at the site by the taxpayer; that is, when work begins on the excavation for footings, pouring the pads for the outlet, or the driving of foundation pilings into the ground. Preliminary work, such as clearing a site, test drilling to determine soil condition, or excavation to change the contour of the land (as distinguished from excavation for footings) does not constitute the beginning of construction. However, if the taxpayer assembles a retail motor fuels outlet on-site from modular units manufactured off-site by the taxpayer and delivered to the site where the outlet will be used, manufacturing begins when physical work of a significant nature commences at the off-site location by the taxpayer.

(2) Safe harbor. For purposes of paragraph (b)(5)(iv)(B)(1) of this section, a taxpayer may choose to determine when physical work of a significant nature begins in accordance with this paragraph (b)(5)(iv)(B)(2). Physical work of a significant nature will be considered to begin at the time the taxpayer incurs (in the case of an accrual basis taxpayer) or pays (in the case of a cash basis taxpayer) more than 10 percent of the total cost of the property (excluding the cost of any land and preliminary activities such as planning or designing, securing financing, exploring, or researching). A taxpayer chooses to apply this paragraph (b)(5)(iv)(B)(2) by filing a federal income tax return for the placed-in-service year of the property that determines when physical work of a significant nature begins consistent with this paragraph (b)(5)(iv)(B)(2).

(C) Components of self-constructed property—(1) Acquired components. If a binding contract, as defined in paragraph (b)(5)(iii) of this section, to acquire a component does not satisfy the requirements of paragraph (b)(5) (ii) of this section, the component does not qualify for the additional first year depreciation deduction. A binding contract described in the preceding sentence to acquire one or more components of a larger self-constructed property will not preclude the larger self-constructed property from satisfying the acquisition rules in paragraph (b)(5)(iv)(A) of this section. Accordingly, the unadjusted depreciable basis of the larger self-constructed property that is eligible for the additional first year depreciation deduction, assuming all other requirements are met, must not include the unadjusted depreciable basis of any component that does not satisfy the requirements of paragraph (b)(5)(ii) of this section. If the manufacture, construction, or production of the larger self-constructed property begins before September 28, 2017, the larger self-constructed property and any acquired components related to the larger self-constructed property do not qualify for the additional first year depreciation deduction under this section.

Examples

Example 4. On September 1, 2017, DD began constructing a retail motor fuels outlet for its own use. On

November 1, 2018, DD ceases construction of the retail motor fuels outlet prior to its completion. Between

September 1, 2017, and November 1, 2018, DD incurred $3,000,000 of expenditures for the construction of the retail motor fuels outlet. On May 1, 2019, DD resumed construction of the retail motor fuels outlet and completed

its construction on August 31, 2019. Between May 1, 2019, and August 31, 2019, DD incurred another

$1,600,000 of expenditures to complete the construction of the retail motor fuels outlet and, on September 1,

2019, DD placed the retail motor fuels outlet in service. None of DD's total expenditures of $4,600,000 qualify for the 100-percent additional first year depreciation deduction because, pursuant to paragraph (b)(5)(iv)(A) of this section, DD began constructing the retail motor fuels outlet before September 28, 2017.

Example 5. The facts are the same as in Example 4 of this paragraph (b)(5)(vii) except that DD began constructing the retail motor fuels outlet for its own use on October 1, 2017, and DD incurred the $3,000,000 between October 1, 2017, and November 1, 2018. DD's total expenditures of $4,600,000 qualify for the 100- percent additional first year depreciation deduction because, pursuant to paragraph (b)(5)(iv)(A) of this section, DD began constructing the retail motor fuels outlet after September 27, 2017, and DD placed the retail motor fuels outlet in service on September 1, 2019. Accordingly, assuming all other requirements are met, the additional first year depreciation deduction for the retail motor fuels outlet will be $4,600,000, computed as

$4,600,000 multiplied by 100 percent.

Example 6. On August 15, 2017, EE entered into a written binding contract with FF to manufacture an aircraft described in section 168(k)(2)(C) for use in EE's trade or business. FF begins to manufacture the aircraft on October 1, 2017. EE places the aircraft in service on March 1, 2018. Pursuant to paragraph (b)(5)(ii) of this section, the aircraft is acquired by EE pursuant to a written binding contract. Because EE entered into such contract before September 28, 2017, the aircraft does not qualify for the 100-percent additional first year

depreciation deduction.

Used Bonus

Explanation

Pursuant to section 168(k)(2)(A)(ii) and (k)(2)(E)(ii), the proposed regulations provide that the acquisition

of used property is eligible for the additional first year depreciation deduction if such acquisition meets the following requirements:

(1) The property was not used by the taxpayer or a predecessor at any time prior to the acquisition;

(2) the acquisition of the property meets the related party and carryover basis requirements of section 179(d)(2)(A), (B), and (C) and §1.179-4(c)(1)(ii), (iii), and (iv), or (c)(2); and

(3) the acquisition of the property meets the cost requirements of section 179(d)(3) and §1.179-4(d).

Regulations

(iii) Used property acquisition requirements—(A) In general. Depreciable property will meet the requirements of this paragraph (b)(3)(iii) if the acquisition of the used property meets the following requirements:

(1) Such property was not used by the taxpayer or a predecessor at any time prior to such acquisition;

(3) The acquisition of such property meets the requirements of section 179(d)(3) and §1.179-4(d) (cost of property) (for further guidance regarding like-kind exchanges and involuntary conversions, see paragraph (f)(5) of this section).

(B) Property was not used by the taxpayer at any time prior to acquisition—(1) In general. Solely for purposes of paragraph (b)(3)(iii)(A)(1) of this section, the property is treated as used by the taxpayer or a predecessor at any time prior to acquisition by the taxpayer or predecessor if the taxpayer or the predecessor had a depreciable interest in the property at any time prior to such acquisition, whether or not the taxpayer or the predecessor claimed depreciation deductions for the property. If a lessee has a depreciable interest in the improvements made to leased property and subsequently the lessee acquires the leased property of which the improvements are a part, the unadjusted depreciable basis, as defined in §1.168(b)-1(a)(3), of the acquired property that is eligible for the additional first year depreciation deduction, assuming all other requirements are met, must not include the unadjusted depreciable basis attributable to the improvements.

(2) Taxpayer has a depreciable interest in a portion of the property. If a taxpayer initially acquires a depreciable interest in a portion of the property and subsequently acquires a depreciable interest in an additional portion of the same property, such additional depreciable interest is not treated as used by the taxpayer at any time prior to its acquisition by the taxpayer. This paragraph (b)(3)(iii)(B)(2) does not apply if the taxpayer or a predecessor previously had a depreciable interest in the subsequently acquired additional portion. For purposes of this paragraph (b)(3)(iii)(B)(2), a portion of the property is considered to be the percentage interest in the property. If a taxpayer holds a depreciable interest in a portion of the property, sells that portion or a part of that portion, and subsequently acquires a depreciable interest in another portion of the same property, the taxpayer will be treated as previously having a depreciable interest in the property up to the amount of the portion for which the taxpayer

held a depreciable interest in the property before the sale.

Requirement # 2 – (2) The acquisition of such property meets the requirements of section 179(d)(2)(A), (B), and (C), and §1.179-4(c)(1)(ii), (iii), and (iv), or 1.179-4(c)(2) (property is acquired by purchase); and

Regulation 1.179-4(c) Purchase

(1)

(i)

Except as otherwise provided in paragraph (c)(2) of this section, the term "purchase" means any acquisition of the property, but only if all the requirements of paragraphs (c)(1)(ii), (iii), and (iv) of this section are satisfied.

(ii)

Property is not acquired by purchase if it is acquired from a person whose relationship to the person acquiring it would result in the disallowance of losses under section 267 or 707(b). The property is considered not acquired by purchase only to the extent that losses would be disallowed under section 267 or 707(b). Thus, for example, if property is purchased by a husband and wife jointly from the husband's

father, the property will be treated as not acquired by purchase only to the extent of the husband's interest in the property. However, in applying the rules of section 267(b) and (c) for this purpose,
section 267(c)(4) shall be treated as providing that the family of an individual will include only his spouse, ancestors, and lineal descendants. For example, a purchase of property from a corporation by a taxpayer who owns, directly or indirectly, more than 50 percent in value of the outstanding stock of such corporation does not qualify as a purchase under section 179(d)(2); nor does the purchase of property by a husband from his wife. However, the purchase of section 179 property by a taxpayer from his brother or sister does qualify as a purchase for purposes of section 179(d)(2).

(iii)

The property is not acquired by purchase if acquired from a component member of a controlled group of corporations (as defined in paragraph (g) of this section) by another component member of the same group.

(iv)

The property is not acquired by purchase if the basis of the property in the hands of the person acquiring it is determined in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired, is determined under section 1014(a), relating to property acquired from a decedent, or is determined under section 1022, relating to property acquired from certain decedents who died in 2010. For example, property acquired by gift or bequest does not qualify as property acquired by purchase for purposes of
section 179(d)(2); nor does property received in a corporate distribution the basis of which is determined under section 301(d)(2)(B), property acquired by a corporation in a transaction to which section 351 applies, property acquired by a partnership through contribution (section 723), or property received in a partnership distribution which has a carryover basis under section 732(a)(1).

(2)

Property deemed to have been acquired by a new target corporation as a result of a section 338 election (relating to certain stock purchases treated as asset acquisitions) will be considered acquired by purchase.

Requirement # 3 – (3) The acquisition of such property meets the requirements of section 179(d)(3) and §1.179-4(d) (cost of property) (for further guidance regarding like-kind exchanges and involuntary conversions, see paragraph (f)(5) of this section).

Regulation 1.179-4(d) Cost.—

The cost of section 179 property does not include so much of the basis of such property as is determined by reference to the basis of other property held at any time by the taxpayer. For example, X Corporation purchases a new drill press costing $10,000 in November 1984 which qualifies as section 179 property, and is granted a trade-in allowance of $2,000 on its old drill press. The old drill press had a basis of $1,200. Under the provisions of sections 1012 and 1031(d), the basis of the new drill press is $9,200 ($1,200 basis of old drill press plus cash expended of $8,000). However, only $8,000 of the basis of the new drill press qualifies as cost for purposes of the section 179 expense deduction; the remaining $1,200 is not part of the cost because it is determined by reference to the basis of the old drill press.

Examples

Example 2. C, an automobile dealer, uses some of its automobiles as demonstrators in order to show them to prospective customers. The automobiles that are used as demonstrators by C are held by C primarily for sale to customers in the ordinary course of its business. On November 1, 2017, D buys from C an automobile that was previously used as a demonstrator by C . D will use the automobile solely for business purposes. The use of the automobile by C as a demonstrator does not constitute a “use” for purposes of the original use requirement and, therefore, D will be considered the original user of the automobile for purposes of paragraph (b)(3)(ii) of this section. Assuming all other requirements are met, D's purchase price of the automobile qualifies for the additional first year depreciation deduction for D, subject to any limitation under section 280F.

Example 6. K is in the trade or business of leasing equipment to others. During 2016, K buys a new machine (Machine #1) and then leases it to L for use in L's trade or business. The lease between K and L for Machine #1 is a true lease for federal income tax purposes. During 2018, L enters into a written binding contract with K to buy Machine #1 at its fair market value on May 15, 2018. L did not have any depreciable interest in Machine #1 before L acquired it on May 15, 2018. As a result, L's acquisition of Machine #1 satisfies the used property acquisition requirements of paragraph (b)(3)(iii) of this section. Assuming all other requirements are met, L's purchase price of Machine #1 qualifies for the additional first year depreciation deduction for L.

Example 7. The facts are the same as in Example 6 of this paragraph (b)(3)(vi), except that K and L are related parties within the meaning of section 179(d)(2)(A) or (B) and §1.179-4(c). As a result, L's acquisition of Machine #1 does not satisfy the used property acquisition requirements of paragraph (b)(3)(iii) of this section. Thus, Machine #1 is not eligible for the additional first year depreciation deduction for L.

Example 8. The facts are the same as in Example 6 of this paragraph (b)(3)(vi), except L incurred capital expenditures of $5,000 to improve Machine #1 on September 5, 2017, and has a depreciable interest in such improvements. L's purchase price of $5,000 for the improvements to Machine #1 satisfies the original use requirement of §1.168(k)-1(b)(3)(i) and, assuming all other requirements are met, qualifies for the 50-percent additional first year depreciation deduction. Because L had a depreciable interest only in the improvements to Machine #1, L's acquisition of Machine #1, excluding L's improvements to such machine, satisfies the used property acquisition requirements of paragraph (b)(3)(iii) of this section. Assuming all other requirements are met, L's unadjusted depreciable basis of Machine #1, excluding the amount of such unadjusted depreciable basis attributable to L's improvements to Machine #1, qualifies for the 100-percent additional first year

depreciation deduction.

Example 17. In November 2017, AA Corporation purchases a used drill press costing $10,000 and is granted a

trade-in allowance of $2,000 on its old drill press. The used drill press is qualified property under section 168(k) (2)(A)(i). The old drill press had a basis of $1,200. Under sections 1012 and 1031(d), the basis of the used drill press is $9,200 ($1,200 basis of old drill press plus cash expended of $8,000). Only $8,000 of the basis of the used drill press satisfies the requirements of section 179(d)(3) and §1.179-4(d) and, thus, satisfies the used property acquisition requirement of paragraph (b)(3)(iii) of this section. The remaining $1,200 of the basis of the used drill press does not satisfy the requirements of section 179(d)(3) and §1.179-4(d) because it is determined