SEC. 179 EXPENSING INCREASED AND BONUS DEPRECIATION ALLOWED UNDER "PROTECTING AMERICANS FROM TAX HIKES" ACT

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On December 18, 2015, Congress passed and the President signed into law an agreement on tax extenders and numerous other tax provisions in the "Protecting Americans from Tax Hikes (PATH) of 2015" (the Act). Tax extenders are the 50+ tax provisions that are routinely extended by Congress on a one- or two-year basis. The Act makes permanent many of the individual and business extenders. Some of the more pertinent provisions are as follows:

Section 179 Expense Deduction

Under Sec. 179 of the Internal Revenue Code, a taxpayer may elect to deduct as an expense, rather than to depreciate over time, up to a specified amount, the cost of new or used tangible personal property placed in service during the tax year in the taxpayer's trade or business. In this case, "taxpayer" does not include an estate, trust, or certain non-corporate lessors. 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.

The old law provided that, for 2015, the maximum expensing limit was $25,000 and the investment ceiling was $200,000. Pursuant to the new law, the expensing limit was increased to $500,000 and the investment ceiling was increased to $2,000,000 before the phase-out begins. These amounts were made retroactive to the beginning of 2015 and they were made permanent for future use. In addition, for any tax year beginning after December 31, 2015, both the $500,000 and the $2,000,000 are indexed for inflation.

The amount eligible to be expensed in a tax year cannot exceed the taxable income derived from the taxpayer's active conduct of a trade or business. The amount deducted under Code Sec. 179 can offset the taxpayer's income, but it cannot be used to create a loss. However, any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding tax years.

"Eligible property" for Code Sec. 179 purposes is any tangible property that is Code Sec. 1245 property (generally machinery and equipment) depreciated under the MACRS rules of Code Sec. 168, regardless of its depreciation recovery period. In short, if you can depreciate it, the property would qualify for Sec. 179 treatment. "Eligible property" includes machinery and equipment; property contained in or attached to a building (other than structural components), such as milk tanks, automatic feeders, barn cleaners, and office equipment; livestock, including horses, cattle, hogs, sheep, goats, mink and other fur bearing animals; grain bins; single purpose livestock and horticultural structures; and agricultural fences and drainage tile. Both new and used property qualifies.

The Code Sec. 179 deduction applies to the tax year when the eligible property is "placed in service." This may be different than the date of purchase. Property is "placed in service" when it is ready and available for a specific use, even if the item is not being currently used. Warning: writing a check on the last day of the year to purchase new machinery or equipment does not automatically qualify that item to be deducted in that tax year. In addition to writing the check, the machinery or equipment must be ready and available to use in that tax year. This may be extremely important when taking on a long-term project, such as constructing a building.

A Code Sec. 179 deduction is taken on tax form 4562. The taxpayer may elect to deduct the entire cost of the property (within limitations), none of the cost, or a portion of the cost of the item. Even though Code Sec. 179 provides for a "deduction," taking the deduction reduces the basis in the property the same as if it was depreciated. A "recapture" of the deduction may be triggered if the item is later sold for more than its basis.

Bonus First-Year Depreciation Extended Through 2019

There was no Accelerated First-Year Depreciation (AFYD) for 2015 under the old law. Under the new law, Congress provided some future stability by providing for AFYD through 2019, albeit on a decreasing scale. Eligible taxpayers will be able to claim:

(1) A 50% bonus depreciation allowance for qualified property placed in service in 2015, 2016, and 2017;
(2) A 40% bonus depreciation allowance for qualified property placed in service in 2018; and
(3) A 30% bonus depreciation allowance for property placed in service in 2019.

In general, property qualifies for the bonus depreciation allowance if it is property to which the modified accelerated cost recovery system (MACRS) rules apply with a recovery period of 20 years or less. This includes virtually all of the items used in agriculture. Unlike the Code Sec. 179 expense deduction, which applies to both new and used property, the bonus depreciation allowance applies to only new property. Its original use must commence with the taxpayer.

The bonus depreciation allowance is also taken on tax form 4562. 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 (as opposed to an individual item) for any tax year.

New Rule for Plants With Long Production Periods

The Act contains a special new rule for plants planted or grafted after December 31, 2015 and before January 1, 2020. Bonus depreciation is allowed for certain trees, vines, and plants bearing fruit or nuts when planted or grafted rather than when the plant reaches income-producing stage. Under the old law, for depreciation purposes, fruit-bearing or nut-bearing plants were deemed "placed in service" when they reached an income-producing stage. The "placed in service" rule was relaxed in the Act so that a fruit-bearing or nut-bearing plant is deemed "placed in service" when planted or grafted. Therefore, plants with a long pre-production period can qualify for the bonus depreciation allowance under the new law.

A "specified plant" that qualifies is a plant, planted or grafted in the United States, that is: (1) any tree, vine, or plant that bears fruit or nuts; or (2) any other plant that will have more than one yield of fruits or nuts and generally has a pre-productive period of more than two years from the time of planting or grafting to the time that the plant bears fruit or nuts.

Other Extended Provisions Worth Noting

In addition to the foregoing provisions, the PATH Act extended the following provisions, among others:

- A permanent extension of the general state and local sales tax deduction.
- A permanent extension of the $250 educator expense deduction.
- A permanent extension of the Credit for Increasing Research Activities (research credit).
- A permanent extension of the 15-year recovery period for qualified leasehold improvements, qualified restaurant property and qualified retail improvements.
- An extension of the tuition and fees deduction through 2016.
- An extension of the nonbusiness energy credit through 2016.
- An extension of mortgage insurance premiums paid or accrued as an itemized deduction through 2016.
- An extension of the qualified principal residence indebtedness exclusion for debt discharge income through 2016.