

Qualified Real Property Improvements MACRS Life of 15 Years is Mandatory

The CARES Act retroactively reinstated, back to 2018 returns, the 15-year MACRS life for qualified real property improvements. This is an opportunity for taxpayers receive quicker write-offs for qualifying improvements. And 15-year MACRS life qualifies for bonus depreciation. Section 179 isn't affected since section 179 was already allowed on this property.

But what about those taxpayers who have already filed their 2018 or 2019 returns? IRS has provided procedures in Revenue Procedure 2020-25. Here are some of the details of this RevProc.

When Congress passed the Tax Cuts and Jobs Act (TCJA 2017), Congress decided to merge into one category the real estate improvements eligible for Section 179, Bonus depreciation, and 15-year MACRS life. In the process of making this change Congress succeeded in removing the old verbiage but forgot to create the new verbiage, with the exception of including this property as eligible for Section 179. Therefore, Qualified Improvement Property typically fell into their normal MACRS Recovery Class of 39-years and bonus depreciation was no longer available.

The CARES Act reinstated, back to property placed in service after December 31, 2017, the 15-year MACRS life for qualified property improvements, and resultant eligibility for bonus depreciation.

In Revenue Procedure 2020-25, IRS has explained the rules as they currently apply. Using a 39-year MACRS class life for Qualified Improvement Property is an impermissible life. Taxpayers are REQUIRED to apply the CARES Act changes to all Qualified Real Property Improvement, including a 15-year MACRS class life for qualifying assets.

QUALIFYING ASSET PLACED IN SERVICE IN 2018 OR 2019. If a qualifying asset was placed in service during 2018 or 2019 and the 2018 and/or 2019 return used the now "impermissible" MACRS class life of 39 years: The taxpayer MUST do one of the following:

- 1) Amend the return(s) no later than October 15, 2021, to "correct" the MACRS class life to 15 years, OR
- 2) File Form 3115 with a timely filed subsequent return (such as the 2019 return (if not already filed) or the 2020 return) to "correct" the prior depreciation and start using the correct life.

If a qualifying asset was placed in service during 2018 or 2019 and the 2018/2019 return(s) used the now "impermissible" MACRS class life of 39 years and the taxpayer does not make the change, potential snags can exist.

- The depreciation for future years has to take into account that bonus depreciation was used in original unless the taxpayer made the formal election out of bonus depreciation for 15-year property. Since bonus depreciation for original was 100%, this means there

would be no basis remaining to depreciate, unless the taxpayer elected out of bonus depreciation.

- The amount of allowed/allowable depreciation taken into account when the property is sold or otherwise disposed of, will be the total depreciation that would have been allowable if the taxpayer had depreciated the property using the MACRS 15-year class life and method, plus bonus depreciation if the taxpayer had not elected out of bonus depreciation.

- If IRS examines the tax return, IRS could require the taxpayer to change to the correct 15-year MACRS life, including taking into account bonus depreciation unless the taxpayer elected out.

BONUS DEPRECIATION under Section 168(k) applies to assets falling into the MACRS class lives of 20-years or shorter. Since Qualified Improvement Property now retroactively falls into the 15-year MACRS class lives, it is subject to bonus depreciation. To elect out of bonus depreciation, the taxpayer must make an election on a timely filed return. Revenue Procedure 2020-25 permits taxpayers to make a late election to ELECT OUT of bonus depreciation for Qualified Improvement Property placed in service in 2018, 2019, or 2020 AS LONG AS the taxpayer has not previously revoked a prior election out of bonus. This late election can be made:

- 1) On a correcting tax return filed no later than October 15, 2021, or
- 2) By attaching Form 3115 to a timely filed original Federal income tax return:
 - a) For the taxpayer's first or second taxable year succeeding the year in which the taxpayer placed the qualified improvement property in service, OR
 - b) For any return that is filed on or after April 17, 2020, and on or before October 15, 2021.

Revenue Procedure 2020-25 also permits taxpayers to REVOKE a prior election out of bonus depreciation for any class(es) of property. This late election can be made:

- 1) On a correcting tax return filed no later than October 15, 2021, or
- 2) By attaching Form 3115 to a timely filed original Federal income tax return:
 - a) For the taxpayer's first or second taxable year succeeding the year in which the taxpayer placed the qualified improvement property in service, OR
 - b) For any return that is filed on or after April 17, 2020, and on or before October 15, 2021.

Revenue Procedure 2020-25 can be found on our web site (ataxprof.com) under the Tax Pros Newsletters tab, or by going to irs.gov/pub/irs-drop and clicking on rp-2020-25.

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