An (Unexpected) Interest in ADS (Part II)

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Capital Recovery & Leasing Committee
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Section 168(g)(2) provides that the alternative depreciation system is depreciation determined by using—

- The straight-line method (without regard to salvage value),
- The applicable convention determined under section 168(d), and
- A recovery period generally determined using the class life of the property
  - 12 years for property without a class life

Comparison of GDS to ADS for common asset types

- 39 to 40 years for non-residential real property
- 27.5 to 30 years for residential real property (reduced from 40 by TCJA)
- 15 to 20 years for land improvements
- 7 to 10 years for office furniture and fixtures
- Possible technical correction for qualified improvement property
  - 15 to 20 years
ADS - Continued

Generally applies to—
— Tangible property used predominantly outside of the United States
  - E.g., CFCs (earning and profits, Subpart F income, tested income)
— Tax-exempt use property
— Tax-exempt bond financed property
— Any imported property covered by an executive order under section 168(g)(6)
— Any property for which the taxpayer elects to use ADS under section 168(g)(7)

Section 168(k)(2)(D)—Additional first year depreciation deduction not available
Use of ADS in Other Code Provisions

Section 163(j)
— Taxpayers making a real property trade or business (RPTOB) election or an electing farming business required to depreciate certain assets using ADS
  - Property with a recovery period of 10 years or more which is held by an electing farming business (Section 168(g)(2)(G))
  - Nonresidential real property, residential rental property, and qualified improvement property held by an electing RPTOB (Section 168(g)(8))
  - Technical correction proposed to add qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property
— Allocation of interest between excepted and non-excepted items (Prop. Reg. section 1.163(j)-10)

Section 250 Deduction (FDII and GILTI)
— Used in the computation of Qualified Business Asset Investment (“QBAI”) as defined in section 951A(d) with certain modifications to reflect section 250 terminology
Use of ADS in Other Code Provisions

Section 861

— The alternative tax book value method of apportioning interest expense (including for foreign tax credit purposes) requires use of ADS depreciation (Reg. section 1.861-9(i))

— TCJA repealed the fair market value method for interest expense allocation for tax years beginning after Dec. 31, 2017
  - Taxpayers are required to apportion using either tax book value or alternative tax book value method going forward
Final GILTI regulations
— Computation of QBAI using ADS depreciation is not a method of accounting
  - However, determination of basis (e.g., capitalization, is a method of accounting)
— Computation of tested income using ADS is a change in method of accounting
  - Same as for E&P and Subpart F pre-TCJA, and presumably for DEI under FDII
— Is there still a “duty of consistency” on asset classification?
— Transition rule: pre-effective date asset additions not required to use ADS for QBAI
  - Not applicable to FDII
  - Use of transition rule is elective

Implications of materiality exception
— For tested income, final reg. section 1.951A-2(c)(2) provides for use of rules similar to reg. 1.952-2 (Subpart F income)
Discussion Topics – Section 951A/Section 250 (Cont’d)

Accounting method change procedural issues for CFCs
— Are methods of accounting adopted or subject to a change in method of accounting for the first GILTI year?
— If a depreciation change in method is needed, are changes in the first tested income year made with a section 481(a) adjustment or on a cut-off basis?
— If there is a section 481(a) adjustment, how is it characterized
  - Impact of section 7.07 of Rev. Proc. 2015-13
  - Final GILTI regulation preamble refers to need to update section 7.07 and provide additional procedures. What are those contemplated procedures and timing?
— Does the CFC have audit protection for back years including transition tax year?
  - Impact of section 8.02(5) of Rev. Proc. 2015-13
  - Would limited amended return period be permitted for the section 965 year?

Definition of “tangible property” in determining QBAI clarified by the final GILTI regulations
— Bonus eligibility not dispositive as under the proposed regulations

Daily proration clarified in the final GILTI regulations
— Daily proration for the full year’s depreciation starts from the actual acquisition or placed in service date and ends with the last day of the year
Discussion Topics – Section 861

Determination of ADS based on ADS rules in year assets placed in service creating a potentially different ADS Computation than used for QBAI—any consistency issues?

For FTC purposes

— What is the legacy intended treatment of elective changes from tax book value, fair market value and alternative tax book value?

— What is the legacy intended treatment if one of the elective methods was calculated incorrectly?
Discussion Topics – Section 163(j)

Government issued Rev. Proc. 2019-08 providing guidance on change in use for electing RPTOB or electing farming business
— Any additional guidance?
— What happens for QLIP/QRIP/QRP if technical correction not passed timely for 2018—how would taxpayers apply the change in use?

Status of section 163(j) guidance?
Additional Questions?
Thank you