

Understanding MACRS & ADS

Business Aircraft Federal Tax Depreciation Basics (Part 2)

Attorney Troy Rolf continues his treatment of depreciation methods and requirements for business aircraft with a discussion on mixed business use.

Many companies that own and operate business aircraft attempt to offset some costs by holding the aircraft out for charter at times when it is not otherwise being utilized by the owner. Such mixed utilization of aircraft can affect the depreciation schedule of the asset.

As previously mentioned, aircraft other than helicopters, used in commercial activities or contract carrying of passengers and freight by air generally may be depreciated under MACRS over seven years, and aircraft used for qualified business purposes or for the production of income, and all depreciable helicopters, may be depreciated under MACRS over a recovery period of five years.

Consequently, when a fixed-wing aircraft (i.e., other than a helicopter) is used part of the time in commercial or contract carrying of passengers and freight by air, and part of the time for other qualified business purposes or for the production of income, questions concerning the appropriate MACRS recovery period are likely to arise.

'Primarily Used' Standard

Treasury regulations specify that when property is used for different purposes at various times in such a manner that the property could potentially be classified into more than one asset class, the property shall be included in the asset class for the activity in which the property is primarily used.

Property is to be classified according to the primary use to which the property is put, even though the activity in which the property is used is insubstantial in relation to all of the activities of the taxpayer. In addition, the asset class of an aircraft that is subject to a lease is determined as if the aircraft were owned by the lessee.

Although not further defined in the regulations, the "primarily used" standard appears to suggest that a fixed-wing aircraft will be depreciated under MACRS over a seven-year recovery period if the proportion of the time it is used in commercial activities exceeds the proportion of time that it is used for other qualified business purposes or for the production of income. Conversely the same aircraft will be depreciated under MACRS over a five year recovery period if the proportion of the time it is used for other qualified business purposes or for the production of income exceeds the proportion of time that it is used in commercial or contract carrying of passengers and freight by air.



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Partial Recapture

For purposes of determining the appropriate asset class for a mixed-use aircraft, it is necessary to determine the primary use of the aircraft during each taxable year that the aircraft is in service. If at any time the primary use of the aircraft changes, it may be necessary to convert from one depreciation schedule to another. This can result in a partial recapture event if, for example, an aircraft is used primarily for business purposes in the first year or so after being placed in service (and is therefore depreciated under MACRS over a five year recovery period), but in later years is used primarily in commercial or contract carrying of passengers and freight by air (and therefore must be depreciated under MACRS over a seven year recovery period).

Depreciation is highly useful in reducing the taxes resulting from income generation. But the rules are involved, and care must be taken to minimize or eliminate the consequences of improper filings. The Internal Revenue Service expects filings that involve depreciation to comply with all applicable tax codes. Thus the reader is advised to seek qualified council in all matters related to taxes associated with the use of a business aircraft. ■

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