

TITLE II--GROWTH INCENTIVES FOR BUSINESS

SEC. 201. INCREASE AND EXTENSION OF BONUS DEPRECIATION.

(a) IN GENERAL.--Section 168(k) (relating to special allowance for certain property acquired after September 10, 2001, and before September 11, 2004) is amended by adding at the end the following new paragraph:

"(4) 50-PERCENT BONUS DEPRECIATION FOR CERTAIN PROPERTY.--

"(A) IN GENERAL.--In the case of 50-percent bonus depreciation property--

"(i) paragraph (1)(A) shall be applied by substituting '50 percent' for '30 percent', and

"(ii) except as provided in paragraph (2)(C), such property shall be treated as qualified property for purposes of this subsection.

"(B) 50-PERCENT BONUS DEPRECIATION PROPERTY.--For purposes of this subsection, the term '50-percent bonus depreciation property' means property described in paragraph (2)(A)(i)--

"(i) the original use of which commences with the taxpayer after May 5, 2003,

"(ii) which is acquired by the taxpayer after May 5, 2003, and before January 1, 2005, but only if no written binding contract for the acquisition was in effect before May 6, 2003, and

"(iii) which is placed in service by the taxpayer before January 1, 2005, or, in the case of property described in paragraph (2)(B) (as modified by subparagraph (C) of this paragraph), before January 1, 2006.

"(C) SPECIAL RULES.--Rules similar to the rules of subparagraphs (B) and (D) of paragraph (2) shall apply for purposes of this paragraph; except that references to September 10, 2001, shall be treated as references to May 5, 2003.

"(D) AUTOMOBILES.--Paragraph (2)(E) shall be applied by substituting '\$7,650' for '\$4,600' in the case of 50-percent bonus depreciation property.

"(E) ELECTION OF 30-PERCENT BONUS.--If a taxpayer makes an election under this subparagraph with respect to any class of property for any taxable year, subparagraph (A)(i) shall not apply to all property in such class placed in service during such taxable year."

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(b) EXTENSION OF CERTAIN DATES FOR 30-PERCENT BONUS DEPRECIATION PROPERTY.--

- (1) PORTION OF BASIS TAKEN INTO ACCOUNT.--
 - (A) Subparagraphs (B)(ii) and (D)(i) of section 168(k)(2) are each amended by striking "September 11, 2004" each place it appears in the text and inserting "January 1, 2005".
 - (B) Clause (ii) of section 168(k)(2)(B) is amended by striking "PRE-SEPTEMBER 11, 2004" in the heading and inserting "PRE-JANUARY 1, 2005".
- (2) ACQUISITION DATE.--Clause (iii) of section 168(k)(2)(A) is amended by striking "September 11, 2004" each place it appears and inserting "January 1, 2005".
- (3) ELECTION.--Clause (iii) of section 168(k)(2)(C) is amended by adding at the end the following: "The preceding sentence shall be applied separately with respect to property treated as qualified property by paragraph (4) and other qualified property."

(c) CONFORMING AMENDMENTS.--

- (1) The subsection heading for section 168(k) is amended by striking "SEPTEMBER 11, 2004" and inserting "JANUARY 1, 2005".
- (2) The heading for clause (i) of section 1400L(b)(2)(C) is amended by striking "30-PERCENT ADDITIONAL ALLOWANCE PROPERTY" and inserting "BONUS DEPRECIATION PROPERTY UNDER SECTION 168(k)".

(d) EFFECTIVE DATE.--The amendments made by this section shall apply to taxable years ending after May 5, 2003.

SEC. 202. INCREASED EXPENSING FOR SMALL BUSINESS.

(a) IN GENERAL.--Paragraph (1) of section 179(b) (relating to dollar limitation) is amended to read as follows:

"(1) DOLLAR LIMITATION.--The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed \$25,000 (\$100,000 in the case of taxable years beginning after 2002 and before 2006)."

(b) INCREASE IN QUALIFYING INVESTMENT AT WHICH PHASEOUT BEGINS.--Paragraph (2) of section 179(b) (relating to reduction in limitation) is amended by inserting "(\$400,000 in the case of taxable years beginning after 2002 and before 2006)" after "\$200,000".

(c) OFF-THE-SHELF COMPUTER SOFTWARE.--Paragraph (1) of section 179(d) (defining section 179 property) is amended to read as follows:

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"(1) SECTION 179 PROPERTY.--For purposes of this section, the term 'section 179 property' means property--

"(A) which is--

"(i) tangible property (to which section 168 applies), or

"(ii) computer software (as defined in section 197(e)(3)(B)) which is described in section 197(e)(3)(A)(i), to which section 167 applies, and which is placed in service in a taxable year beginning after 2002 and before 2006,

"(B) which is section 1245 property (as defined in section 1245(a)(3)), and

"(C) which is acquired by purchase for use in the active conduct of a trade or business.

Such term shall not include any property described in section 50(b) and shall not include air conditioning or heating units."

(d) ADJUSTMENT OF DOLLAR LIMIT AND PHASEOUT THRESHOLD FOR INFLATION.-- Subsection (b) of section 179 (relating to limitations) is amended by adding at the end the following new paragraph:

"(5) INFLATION ADJUSTMENTS.--

"(A) IN GENERAL.--In the case of any taxable year beginning in a calendar year after 2003 and before 2006, the \$100,000 and \$400,000 amounts in paragraphs (1) and (2) shall each be increased by an amount equal to--

"(i) such dollar amount, multiplied by

"(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting 'calendar year 2002' for 'calendar year 1992' in subparagraph (B) thereof.

"(B) ROUNDING.--

"(i) DOLLAR LIMITATION.--If the amount in paragraph (1) as increased under subparagraph (A) is not a multiple of \$1,000, such amount shall be rounded to the nearest multiple of \$1,000.

"(ii) PHASEOUT AMOUNT.--If the amount in paragraph (2) as increased under subparagraph (A) is not a multiple of \$10,000, such amount shall be rounded to the nearest multiple of \$10,000."

(e) REVOCATION OF ELECTION.--Paragraph (2) of section 179(c) (relating to election irrevocable) is amended by adding at the end the following new sentence: "Any such election or specification with respect to any taxable year beginning after 2002 and before 2006 may be revoked by the taxpayer with respect to any property, and such revocation, once made, shall be irrevocable."

(f) EFFECTIVE DATE.--The amendments made by this section shall apply to taxable years beginning after December 31, 2002.



50% Bonus Depreciation Increases Incentive to Purchase Aircraft

The Jobs and Growth Tax Relief Reconciliation Act of 2003 provides increased incentives for the purchase of aircraft. The bonus depreciation provision in particular provides remarkable tax-saving opportunities for those purchasing new aircraft or upgrading aircraft already in service.

Bonus Depreciation for New Aircraft

Under current tax law, a purchaser of a new aircraft can elect to expense 30% of the cost of the aircraft in the year of purchase as bonus depreciation. This deduction is in addition to a deduction for regular depreciation and, possibly, a Section 179 expense deduction as well.

The new tax bill allows up to 50% of the cost of an aircraft purchased after May 5, 2003, to be deducted in the year of purchase. The new tax bill also extends the bonus depreciation provision, which was set to expire September 11, 2004 through December 31, 2004. Remarkably, the combination of the bonus depreciation deduction and first year MACRS depreciation allows up to 60% of the cost of a new aircraft to be written off in the year of purchase.

Tax Incentives Play an Important Role in Aircraft Acquisition Decisions

Taxpayers who could benefit from a substantial write-off in the current year should weigh the differences between the tax treatment of new aircraft and used aircraft. Because bonus depreciation is only applicable to new aircraft, for many taxpayers, the tax savings offered by bonus depreciation may make purchasing a new aircraft more advantageous than purchasing a used one. The following table illustrates the percentage of the cost of an aircraft that can be written off as depreciation in each year of ownership, depending upon whether the aircraft is new or used when acquired.

	NEW		USED	
	FAR Part 91	FAR Part 135	FAR Part 91	FAR Part 135
Year 1	60.00%	57.15%	20.00%	14.29%
Year 2	16.00%	12.24%	32.00%	24.49%
Year 3	9.60%	8.75%	19.20%	17.49%
Year 4	5.76%	6.25%	11.52%	12.49%
Year 5	5.76%	4.47%	11.52%	8.93%
Year 6	2.88%	4.46%	5.76%	8.92%
Year 7		4.47%		8.93%
Year 8		2.23%		4.46%

Whereas, bonus depreciation offers the greatest benefit to those who purchase new aircraft, it also offers tax-saving opportunities to those purchasing used aircraft or upgrading aircraft they already own. For example, it may be possible to structure a purchase agreement for a used aircraft so that costs for the repair of squawks or the installation of new avionics may be born by the purchaser, rather than the seller, thereby providing bonus depreciation deductions to the new owner.

The Importance of Planning

As beneficial as the new bonus depreciation provision is, its possible benefits for a particular taxpayer can be substantially lessened or even nullified by imprudent purchase and ownership decisions. As is the case with most advantageous tax provisions, bonus depreciation deductions are subject to a morass of conditions and limitations on their usefulness. The context of airplane ownership and operation, with its attendant regulatory and operational complexities, compounds the already daunting pitfalls inherent within the tax laws and regulations.

For instance, an important limitation on bonus depreciation is that, as a business deduction, it is only allowable on an aircraft to the extent that the aircraft is used for business purposes. Accordingly, only two-thirds of the potential depreciation deduction may be claimed on an aircraft used two-thirds of the time for business purposes, and bonus depreciation cannot be claimed at all on an aircraft used only half the time for business. However, by structuring ownership and use of the aircraft properly, aircraft owners can enjoy personal use of their aircraft while benefiting fully from tax deductions that would otherwise have been lost.

Opportunities for Those Purchasing or Upgrading Aircraft

The bonus depreciation provision of last year's tax bill has been a tremendous benefit to those who have purchased new aircraft. The new tax bill's provisions, when coupled with careful tax planning, present the opportunity for tremendous tax savings to those who purchase used aircraft, upgrade an aircraft, or trade up to a more expensive aircraft.

[Advocate Aircraft Taxation Company](#) is in the business of assisting aircraft owners and operators in acquiring, maintaining, and disposing of aircraft in a tax efficient manner. Services include the reduction of sales tax on acquisitions, the maximization of income tax savings, the minimization of exposure for federal excise taxes, and the minimization of imputed income for personal use of aircraft. The firm is comprised of Attorneys and Certified Public Accountants whose practice is limited to the taxation of aircraft.

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New and Used Aircraft Purchases of Less Than \$500,000 Qualify for Expanded Tax Deductions

50% BONUS DEPRECIATION FOR NEW, AND \$100,000 WRITE-OFF FOR NEW & USED QUALIFIED PURCHASES

Congress has now passed The Jobs and Growth Tax Relief Reconciliation Act of 2003, which provides increased incentives for the purchase of new and used aircraft. The bonus depreciation and Section 179 expense deduction provisions can be used by qualified taxpayers to allow the write-off of a substantial portion of the purchase price of aircraft.

Bonus Depreciation for New Aircraft Increases to 50%

Under current law, a purchaser of a new aircraft can elect to expense 30% of the cost of the aircraft in the year of purchase as bonus depreciation. This deduction is in addition to a deduction for regular depreciation and, possibly, a Section 179 expense deduction as well.

The new tax bill allows up to 50% of the cost of a new aircraft purchased after May 5, 2003, to be deducted in the year of purchase. The new tax bill also extends the bonus depreciation provision, which was set to expire September 11, 2004 through December 31, 2004.

\$100,000 Expensing for Qualified New or Used Aircraft

Currently, Section 179 of the Internal Revenue Code allows a qualified purchaser of a new or used aircraft to take an immediate expense deduction of \$25,000 in addition to a regular depreciation deduction in the first year of ownership. However, the Section 179 expense deduction is decreased when a purchaser invests more than \$200,000 in total capital improvements, including his airplane, in any one year; so many purchasers are unable to benefit from the deduction.

The new tax bill provides for a maximum \$100,000 deduction the first year which is available when up to \$400,000 of equipment is placed in service. When a taxpayer adds more than \$400,000 in assets in any one year, the maximum deduction decreases pro rata and is eliminated at \$500,000 in annual capital purchases. The increased Section 179 deduction will apply for tax years 2003 through 2005, so it can be of benefit to those who have already made a purchase this year.

Opportunities for Those Purchasing or Upgrading Aircraft

The bonus depreciation provision in last year's tax bill has been a tremendous benefit to those who have purchased new aircraft. The new tax bill's provisions are of even greater benefit and not just to purchasers of new aircraft. Not only do the new provisions allow the write off of 72% of the purchase price of a new Skylane against current year income, they also promise tremendous tax savings to those who purchase used aircraft, upgrade an aircraft, or trade up to a more expensive aircraft.

An Aircraft Example

To illustrate the effects of the new tax bill, we have calculated the tax savings resulting from the purchase of both a new and used Cessna 182 Turbo under the new tax bill compared with the current law. The example assumes 100% business use.

Cessna 182 Turbo	New Tax Bill		Current Law	
	New	Used	New	Used
Purchase Price	\$330,000	\$300,000	\$330,000	\$300,000
Section 179 Deduction	100,000	100,000	0	0
Bonus Depreciation	115,000	0	99,000	0
MACRS Depreciation	23,000	40,000	46,200	60,000
Total First Year Deduction	\$238,000	\$140,000	\$145,200	\$60,000
% of Purchase Price	72%	47%	44%	20%

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50% Bonus Depreciation on New Aircraft Enhanced by Trade-Ins

The Jobs and Growth Tax Relief Reconciliation Act of 2003 not only increased the bonus depreciation rate from 30% to 50%, but also changed the manner in which the bonus depreciation is calculated. The controlling House Committee states that: “the Committee wishes to clarify that the adjusted basis of qualified property acquired by a taxpayer in a like-kind exchange...is eligible for the additional first year depreciation deduction.” This statement mandates that for purposes of bonus depreciation, a taxpayer will calculate the 50% deduction both on the difference invested as well as the remaining basis of the property used in the exchange. Prior to this announcement, the IRS had issued Notice 2000-4 which states that a taxpayer would continue to depreciate the carry-over basis of any depreciable asset acquired in a like-kind exchange as if the exchange or conversion had not occurred. Although the IRS has not yet released any direct guidance on this issue, it appears that this new provision will provide even greater depreciation when an aircraft owner trades in his old aircraft on a new one.

It has long been a common practice to trade one aircraft on another to avoid depreciation recapture. In accordance with the beforementioned notice, it was generally believed that depreciation should be calculated by treating the difference in purchase price as a new asset and continue to depreciate the trade-in aircraft as though it was owned. This would naturally result in a taxpayer receiving bonus depreciation treatment only on the difference invested, rather than the combination of new investment, as well as the carry-over basis of the traded in aircraft.

Carry-Over Basis of Traded Property Not Considered In Calculation of Section 179 Expense Deduction

A tax law also allows an expensing deduction of up to \$100,000 for taxpayers designated as “small businesses”. A small business is one defined as a business that spends less than \$500,000 in total capital expenditures during the year. However, for purposes of determining both the amount invested and total capital improvements during the year, only the additional investment is considered.

An Aircraft Example

This rather complex tax transaction can perhaps best be illustrated by example. Let us assume that an aircraft owner acquired a Cessna 172 on July 1, 2001, at a price of \$160,000. Because he used the aircraft in his business in 2001 and 2002 he was entitled to 20% depreciation in 2001

and 32% in 2002. His depreciable basis is therefore reduced to \$76,800 or 48% of its original cost. He believes that if he were to sell the aircraft today he would receive \$116,500 for its value and, therefore, be forced to recognize a gain of \$39,700. He has therefore concluded that rather than sell the aircraft, he would prefer to trade it in on a new 182T. The difference between the cost of a new aircraft and the fair market value of the old is \$220,000. The results of the depreciation under the old law and the new law are illustrated below.

Cessna 182T	New Tax Law	Former Law
Purchase Price	\$336,500	\$336,500
New Investment	220,000	220,000
Basis of Trade	76,800	76,800
Section 179 Deduction	100,000	0
Bonus Depreciation	98,400	66,000
MACRS Depreciation-New Investment	12,000	30,800
MACRS Depreciation-Carry Over Basis	15,360	30,720
Total First Year Deduction	\$225,760	\$127,520
Percent of Purchase Price	67.09%	37.90%
Percent of New Investment	102.62%	57.96%

A Planning Opportunity

Due to the new method of calculating bonus depreciation, aircraft owners may find that the tax savings may offset the benefit from attempting to market their old aircraft rather than use it as a trade. However, should an aircraft owner decide to attempt to market the aircraft outside the trade, the tax benefits of a like-kind exchange can still be accomplished through the use of an intermediary. The provisions outlined in this memorandum are rather complex, and presented only in outline form. Before implementing any of the strategies aircraft owners are encouraged to seek professional advice.

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