PacificCPE

COURSE
34602A

Figuring Depreciation Under MACRS

Mastering MACRS is essential for accurately calculating depreciation on business assets. This course walks through the Modified Accelerated Cost Recovery System in detail, covering recovery periods, depreciation methods, and the conventions that determine how much depreciation a taxpayer can claim each year. Designed for CPAs and tax professionals who want to move beyond the basics, this course builds the technical confidence needed to handle MACRS calculations correctly across a wide range of client situations.

CREDIT HOURS 2 | FIELD OF STUDY TAXES | EXAM QUESTIONS 10

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Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Recognize the different MACRS depreciation systems and the information required to properly calculate the allowable depreciation and potential recapture.

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Chapter 1: FIGURING DEPRECIATION UNDER MACRS

Chapter Objective

After completing this chapter, you should be able to:

- Recognize the different MACRS depreciation systems and the information required to properly calculate the allowable depreciation and potential recapture.

Introduction

The Modified Accelerated Cost Recovery System (MACRS) is used to recover the basis of most business and investment property placed in service after 1986. MACRS consists of two depreciation systems, the General Depreciation System (GDS) and the Alternative Depreciation System (ADS). Generally, these systems provide different methods and recovery periods to use in figuring depreciation deductions.

This chapter explains how to determine which MACRS depreciation system applies to your property. It also discusses other information you need to know before you can figure depreciation under MACRS. This information includes the property's recovery class, placed in service date, and basis, as well as the applicable recovery period, convention, and depreciation method. It explains how to use this information to figure your depreciation deduction and how to use a general asset account to depreciate a group of properties. Finally, it explains when and how to recapture MACRS depreciation.

WHICH DEPRECIATION SYSTEM (GDS OR ADS) APPLIES?

Your use of either the General Depreciation System (GDS) or the Alternative Depreciation System (ADS) to depreciate property under MACRS determines what depreciation method and recovery period you use. You generally must use GDS unless you are specifically required by law to use ADS or you elect to use ADS.

If you placed your property in service in 2025, complete Part III of Form 4562 to report depreciation using MACRS. Complete section B of Part III to report depreciation using GDS, and complete section C of Part III to report depreciation using ADS. If you placed your property in service before 2025 and are required to file Form 4562, report depreciation using either GDS or ADS on line 17 in Part III.

Required use of ADS. You must use ADS for the following property.

- Nonresidential real property, residential real property, and qualified improvement property held by an electing real property trade or business (as defined in section 163(j)(7)(B) of the Internal Revenue Code).
- Any property with a recovery period of 10 years or more under the GDS held by an electing farming business (as defined in section 163(j)(7)(C) of the Internal Revenue Code).
- Any tax-exempt use property.
- Any tax-exempt bond-financed property.
- All property used predominantly in a farming business and placed in service in any tax year during which an election not to apply the uniform capitalization rules to certain farming costs is in effect.
- Any property imported from a foreign country for which an Executive Order is in effect because the country maintains trade restrictions or engages in other discriminatory acts.
- Any tangible property used predominantly outside the United States during the tax year.
- Any listed property used 50% or less in a qualified business use during the tax year (discussed later in Chapter 1 of course 34603A).

Caution!

If you are required to use ADS to depreciate your property, you cannot claim any special depreciation allowance (discussed in Chapter 3 of course 34601A) for the property.

Electing ADS. Although your property may qualify for GDS, you can elect to use ADS. The election generally must cover all property in the same property class that you placed in service during the year. However, the election for residential rental property and nonresidential real property can be made on a property-by-property basis. Once you make this election, you can never revoke it.

You make the election by completing Form 4562, Part III, line 20.

WHICH PROPERTY CLASS APPLIES UNDER GDS?

The following is a list of the nine property classifications under GDS and examples of the types of property included in each class. These property classes are also listed under column (a) in section B, Part III, of Form 4562.

1. **3-year property.**

   a) Tractor units for over-the-road use.

   b) Any race horse over 2 years old when placed in service.

   c) Any other horse (other than a race horse) over 12 years old when placed in service.

d) Qualified rent-to-own property (defined later).

2. **5-year property.**

a) Automobiles, taxis, buses, helicopters, and trucks.

b) Non-commercial (that is not used in commercial or contract carrying of passengers or freight).

c) Any qualified technological equipment.

d) Office machinery (such as typewriters, calculators, and copiers).

e) Any property used in research and experimentation.

f) Breeding cattle and dairy cattle.

g) Appliances, carpets, furniture, etc., used in a residential rental real estate activity.

h) Certain geothermal property.

i) Any machinery equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) used in a farming business and placed in service after 2017, in tax years ending after 2017. The original use of the property must begin with you after 2017.

j) Any qualified facility (as defined in section 45Y(b)(1)(A)) of the Internal Revenue Code, any qualified property (as defined in subsection (b)(2) of section 48E of the Internal Revenue Code) which is a qualified investment (as defined in subsection (b)(1) of such section), or any energy storage technology (as defined in subsection (c)(2) of such section).

3. **7-year property.**

a) Office furniture and fixtures (such as desks, files, and safes).

b) Used agricultural machinery and equipment placed in service after 2017, grain bins, cotton ginning assets, or fences used in a farming business (but no other land improvements).

c) Railroad track.

d) Any property that does not have a class life and has not been designated by law as being in any other class.

e) Certain motorsports entertainment complex property (defined later) .

f) Any natural gas gathering line placed in service after April 11, 2005.

4. **10-year property.**

a) Vessels, barges, tugs, and similar water transportation equipment.

b) Any single-purpose agricultural or horticultural structure.

c) Any tree or vine bearing fruits or nuts.

d) Qualified small electric meter and qualified smart electric grid system (defined later) placed in service on or after October 3, 2008.

5. **15-year property.**

a) Certain improvements made directly to land or added to it (such as shrubbery, fences, roads, sidewalks, and bridges).

b) Any retail motor fuels outlet (defined later), such as a convenience store.

c) Any municipal wastewater treatment plant.

d) Initial clearing and grading land improvements for gas utility property.

e) Electric transmission property (that is section 1245 property) used in the transmission at 69 or more kilovolts of electricity placed in service after April 11, 2005.

f) Any natural gas distribution line placed in service after April 11, 2005, and before January 1, 2011.

g) Any telephone distribution plant and comparable equipment used for 2-way exchange of voice and data communications.

h) Qualified improvement property (defined later) placed in service after 2017.

6. **20-year property.**

a) Farm buildings (other than single purpose agricultural or horticultural structures).

b) Municipal sewers not classified as 25-year property.

c) Initial clearing and grading land improvements for electric utility transmission and distribution plants.

7. **25-year property.** This class is water utility property, which is either of the following.

a) Property that is an integral part of the gathering, treatment, or commercial distribution of water, and that, without regard to this provision, would be 20-year property.

b) Municipal sewers other than property placed in service under a binding contract in effect at all times since June 9, 1996.

8. **Residential rental property.** This is any building or structure, such as a rental home (including a mobile home), if 80% or more of its gross rental income for the tax year is from dwelling units. A dwelling unit is a house or apartment used to provide living accommodations in a building or structure. It does not include a unit in a hotel, motel, or other establishment where more than half the units are used on a transient basis. If you occupy any part of the building or structure for personal use, its gross rental income includes the fair rental value of the part you occupy.

9. **Nonresidential real property.** This is section 1250 property, such as an office building, store, or warehouse, that is neither residential rental property nor property with a class life of less than 27.5 years.

Qualified rent-to-own property. Qualified rent-to-own property is property held by a rent-to-own dealer for purposes of being subject to a rent-to-own contract. It is tangible personal property generally used in the home for personal use. It includes computers and peripheral equipment, televisions, videocassette recorders, stereos, camcorders, appliances, furniture, washing machines and dryers, refrigerators, and other similar consumer durable property. Consumer durable property does not include real property, aircraft, boats, motor vehicles, or trailers.

If some of the property you rent to others under a rent-to-own agreement is of a type that may be used by the renters for either personal or business purposes, you still can treat this property as qualified property as long as it does not represent a significant portion of your leasing property. However, if this dual-use property does represent a significant portion of your leasing property, you must prove that this property is qualified rent-to-own property.

Rent-to-own dealer. You are a rent-to-own dealer if you meet all the following requirements.

- You regularly enter into rent-to-own contracts (defined below) in the ordinary course of your business for the use of consumer property.
- A substantial portion of these contracts end with the customer returning the property before making all the payments required to transfer ownership.
- The property is tangible personal property of a type generally used within the home for personal use.

Rent-to-own contract. This is any lease for the use of consumer property between a rent-to-own dealer and a customer who is an individual, which meets all of the following requirements.

- Is titled “Rent-to-Own Agreement,” “Lease Agreement with Ownership Option,” or other similar language.
- Provides a beginning date and a maximum period of time, not to exceed 156 weeks or 36 months from the beginning date, for which the contract can be in effect (including renewals or options to extend).
- Provides for regular periodic (weekly or monthly) payments that can be either level or decreasing. If the payments are decreasing, no payment can be less than 40% of the largest payment.
- Provides for total payments that generally exceed the normal retail price of the property plus interest.
- Provides for total payments that do not exceed $10,000 for each item of property.

- Provides that the customer has no legal obligation to make all payments outlined in the contract and that, at the end of each weekly or monthly payment period, the customer can either continue to use the property by making the next payment or return the property in good working order with no further obligations and no entitlement to a return of any prior payments.
- Provides that legal title to the property remains with the rent-to-own dealer until the customer makes either all the required payments or the early purchase payments required under the contract to acquire legal title.
- Provides that the customer has no right to sell, sublease, mortgage, pawn, pledge, or otherwise dispose of the property until all contract payments have been made.

Motorsports entertainment complex. This is a racing track facility permanently situated on land that hosts one or more racing events for automobiles, trucks, or motorcycles during the 36-month period after the first day of the month in which the facility is placed in service. The events must be open to the public for the price of admission.

Qualified smart electric grid system. A qualified smart electric grid system means any smart grid property used as part of a system for electric distribution grid communications, monitoring, and management placed in service after October 3, 2008, by a taxpayer who is a supplier of electrical energy or a provider of electrical energy services. Smart grid property includes electronics and related equipment that is capable of:

- Sensing, collecting, and monitoring data of or from all portions of a utility's electric distribution grid,
- Providing real-time, two-way communications to monitor or to manage the grid, and
- Providing real-time analysis of an event prediction based on collected data that can be used to provide electric distribution system reliability, quality, and performance.

Retail motor fuels outlet. Real property is a retail motor fuels outlet if it is used to a substantial extent in the retail marketing of petroleum or petroleum products (whether or not it is also used to sell food or other convenience items) and meets any one of the following three tests.

- It is not larger than 1,400 square feet.
- 50% or more of the gross revenues generated from the property are derived from petroleum sales.
- 50% or more of the floor space in the property is devoted to petroleum marketing sales.

A retail motor fuels outlet does not include any facility related to petroleum and natural gas trunk pipelines.

Qualified improvement property. Generally, this is any improvement to an interior part of a building that is nonresidential real property, and the improvement is section 1250 property and is placed in service by you after 2017 and after the date the building was first placed in service by any person.

However, a qualified improvement does not include any improvement for which the expenditure is attributable to any of the following.

- The enlargement of the building.
- Any elevator or escalator.
- The internal structural framework of the building.

Qualified smart electric meter. A qualified smart electric meter is any time-based meter and related communication equipment which is placed in service by a supplier of electric energy or a provider of electric energy services and which is capable of being used by you as part of a system that meets all of the following requirements.

- Measures and records electricity usage data on a time-differentiated basis in at least 24 separate time segments per day.
- Provides for the exchange of information between the supplier or provider and the customer's smart electric meter in support of time-based rates or other forms of demand response.
- Provides data to the supplier or provider so that the supplier or provider can provide energy usage information to customers electronically.
- Provides all commercial and residential customers of such supplier or provider with net metering. Net metering means allowing a customer a credit, if any, as complies with applicable federal and state laws and regulations for providing electricity to the supplier or provider.

Natural gas gathering line and electric transmission property. Any natural gas gathering line placed in service after April 11, 2005, is treated as 7-year property, and electric transmission property (that is section 1245 property) used in the transmission at 69 or more kilovolts of electricity and any natural gas distribution line placed in service after April 11, 2005, are treated as 15-year property, if the following requirements are met.

- The original use of the property must have begun with you after April 11, 2005. Original use means the first use to which the property is put, whether or not by you. Therefore, property used by any person before April 12, 2005, is not original use. Original use includes additional capital expenditures you incurred to recondition or rebuild your property. However, original use does not include the cost of reconditioned or rebuilt property you acquired. Property containing used parts will not be treated as