Corporate Income Tax

Lecture Materials for Chapter 2

Property Acquisition and Cost Recovery

UNC Charlotte MACC Program

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Big Picture-Learning Objectives

LO 2-1. Explain the concept of basis and adjusted basis and describe the cost recovery methods used under the tax law to recover the cost of personal property, real property, intangible assets, and natural resources.

- Tangible personal and real property (depreciation), intangibles (amortization), and natural resources (depletion) are all subject to cost recovery.
- An asset's basis is the amount that is subject to cost recovery. Generally, an asset's initial basis is its purchase price, plus the cost of any other expenses incurred to get the asset in working condition.
- The taxpayer's basis of assets acquired in a nontaxable exchange is the same basis the taxpayer transferred to acquire the property received.
- Expenditures on an asset are either expensed currently or capitalized as a new asset. Expenditures for routine or general maintenance of the asset are expensed currently. Expenditures that extend the useful life of the asset are capitalized.
- When acquiring a business and purchasing a bundle of property, the basis of each asset is determined as the fair market value of the asset.

LO 2-2. Determine the applicable cost recovery (depreciation) life, method, and convention for tangible personal and real property and calculate the deduction allowable under basic MACRS.

- Tax depreciation is currently calculated under the Modified Accelerated Cost Recovery System (MACRS).
- MACRS for tangible personal property is based upon recovery period (Rev. Proc. 87-56), method (200 percent declining balance, 150 percent declining balance, and straight-line), and convention (half-year or mid-quarter).
- Real property is divided into two groups for tax purposes: residential rental and nonresidential. The recovery period is 27.5 years for residential property and 31.5 years or 39 years for nonresidential property, depending on when the property was placed in service. The depreciation method is straight-line and the convention is mid-month.

LO 2-3. Explain the additional special cost recovery rules (§179, bonus, listed property) and calculate the deduction allowable under these rules.

- §179 allows taxpayers to expense tangible personal property. The expense is limited by the amount of property placed in service and taxable income.
- Bonus depreciation allows taxpayers to immediately expense 50 percent of qualified property in the year of acquisition.
- Listed property includes automobiles, other means of transportation, and computer equipment. Depreciation is limited to the expense multiplied by business-use percentage. Special rules apply if business use is less than 50 percent.
- Additional limitations apply to luxury automobiles.

LO 2-4. Explain the rationale behind amortization, describe the four categories of amortizable intangible assets, and calculate amortization expense.

- Intangible assets (such as patents, goodwill, and trademarks) have their costs recovered through amortization.
- Intangible assets are amortized (straight-line method) using the full-month convention.
- Intangibles are divided into four types (§197 purchased intangibles, start-up costs and organizational expenditures, research and experimentation, and self-created intangibles).

LO 2-5 Explain cost recovery of natural resources and the allowable depletion methods.

- Depletion allows a taxpayer to recover his or her capital investment in natural resources.
- Two methods of depletion are available, and the taxpayer must calculate both and take the one that results in the larger depletion deduction each year.
- Cost depletion allows taxpayers to estimate number of units and then allocate a pro rata share of the basis to each unit extracted during the year.
- Percentage depletion allows the taxpayer to take a statutory determined percentage of gross income as an expense. Deductions are not limited to basis.

Tax legislation in 2015 - section 179 limitations extended

Instructor Note: See Textbook page 2-17. **Textbook: Immediate Expensing** Policy makers created an important tax incentive designed to help small businesses purchasing new or used tangible personal property. This incentive is commonly referred to as the **§179 expense** or *immediate expensing* election. … However, under §179, businesses may elect to immediately expense up to $500,000 of tangible personal property placed in service during 2015 **(assuming the 2014 limits are extended to 2015).**

Instructor Note. The provisions were extended. See underlined words in next paragraph below.

The Protecting Americans from Tax Hikes Act of 2015 (P.L. 114-113), permanently extends the $500,000 dollar limitation and $2,000,000 investment limitation. In tax years beginning after 2015, the limitations will be adjusted annually for inflation. These limitations were scheduled for reduction to $25,000 and $200,000 respectively, in tax years beginning after 2014.

The new law also permanently extends the election to expense qualified real property and eliminates the restriction which limited the amount of qualified real property that could be expensed to $250,000 of the overall $500,000 cap.

The election to expense off-the-shelf computer software is permanently extended and, effective for tax years beginning after 2015, the limitation which prevented a taxpayer from expensing portable air conditioning and heating units is revoked. Finally, the provision which allows a taxpayer to make, revoke, or change a Code Sec. 179 election is permanently extended.

Textbook page 2-18: Taxable income limitation. The Code Sec. 179 deduction is limited to the taxpayer's taxable income derived from the active conduct of any trade or business during the tax year, computed without taking into account any Code Sec. 179 deduction, deduction for self-employment taxes, net operating loss carryback or carryover, and deductions suspended under any provision (Code Sec. 179(b)(3); Reg. §1.179-2(c)(1)). Any amount disallowed by this limitation may be carried forward and deducted in subsequent tax years, subject to the maximum dollar and investment limitations, or, if lower, the taxpayer’s taxable income limitation for the carryover year.

Luxury Autos: Material from your textbook on page 2-27

Therefore, … the tax laws generally limit the annual depreciation expense for automobiles. Each year, the IRS provides a maximum depreciation schedule for automobiles placed in service during that particular year. **For 2010 through 2014, taxpayers are allowed to expense $8,000 of bonus depreciation above the otherwise allowable maximum depreciation (maximum depreciation of $11,160 for automobiles placed in service in 2012 through 2014); however, as of press date the bonus depreciation provisions have not been extended to 2015.** Exhibit 2-8 summarizes these schedules for automobiles placed in service for each year from 2015 back to 2012.

Instructor Note: the date range above (underlined words) is now extended for 2015, 2016 and beyond.

More on Bonus Depreciation

For 2015 and 2016, after claiming the Section 179 write-off (which is technically not depreciation expense), a taxpayer may deduct bonus depreciation of 50% of the cost of “new” depreciable personal property (not real estate) acquired in the year.

Procedure: (1) deduct the section 179 deduction if you elect this deduction, (2) take the 50% bonus depreciation, if you elect this, and finally (3) deduct regular depreciation on the basis of the asset after reduction for amounts in (1) and (2).

These extensions will reduce the government’s tax collections by about $100 billion over 10 years.

Cases on Depreciation and Amortization

Except where noted otherwise, each case is independent of the other cases.

Asset Cost: $100, life is 5 years. Bought on March 1. Mid-Year convention applies.
With mid-year convention, you get 1/2 of a full year's depreciation in first year.
Asset bought any time in year -- generally treated as if bought on July 1. (sort of)

Beginning Basis	Depreciable Life	Straight-Line Deprec. Rate	Double Declining Balance Rate	Double Declining Depreciation	Tax Return Depreciation	
$100.00	5	20%	40%	$40	$20.00	Yr. 1, Mid-Yr.
$80.00			40%		$32.00	40% of $80.
$48.00			40%		$19.20	40% of $48.
$28.80			40%		$11.52	Switch to
$17.28			40%		$6.91	Straight-line
$10.37			40%		$4.15	Half-year

Appendix MACRS Tables

TABLE 1 MACRS Half-Year Convention

	Depreciation Rate for R		
Year	3-year	5-year	7-year
1	33.33	20.00	14.29
2	44.45	32.00	24.49
3	14.81	19.20	17.49
4	7.41	11.52	12.49
5		11.52	8.93
6		5.76	8.92
7			8.93
8			4.46

Text Page 2-40

Notes for 5-Year Property

Half-year, in first year

Full-Year of Depreciation

Switch to Straight-line

Half year in sixth year

Note: 5-year property is depreciated over 6 calendar years. First and last year have 1/2 year of depreciation.
Mid-year convention is based on assumption you bought the asset on July 1. (sort of)

1 Buy a machine, compute depreciation. No bonus or Sec. 179 write-off.

Hickory Corporation purchased a machine on July 22, 2015 at a cost of $510,000.
The machine has a recovery period of 5 years. Hickory will NOT claim:
(1) immediate expensing under section 179, or (2) bonus depreciation.
What is Hickory's cost recovery deduction for 2015?

Date of acquistion	**July-22**
Asset	**Machine**
Life	**5.0**
Convention	**Mid-Year**
New machine cost	**$510,000**
MACRS Rate	
MACRS Depreciation	

Proof (with minor rounding error). Page 2-40

New machine cost	$510,000
Life in years	5
Straight-line depreciation - 1 yr.	$102,000
Double-declining balance	$204,000
Mid-year, 50% in first year	

Cost $100/5 Year

$100.00	
0.20	**S.L. Dep. Rate**
20.00	**S.L. Deprec.**
40.00	**DDB**
20.00	**Mid-Year**
20.00%	

2 Buy machine, compute depreciation. Elect Sec. 179. No bonus depreciation

Hickory Corporation purchased machinery on March 1, 2015.
The cost of the machinery was $600,000, and it has a life of 5 years.
Hickory will claim maximum Section 179 write-off. Do not claim bonus depreciation.
Sec. 179 limit is $500,000, less (excess of cost of equipment bought over $2,000,000).

1	Equipment is 5-year property.	Compute	Deduction	
2	Cost of machinery	$600,000		
3	Threshold - Section 179 write-off	2,000,000		
4	Excess (Reduction in 179 limit)	0		
5	Regular Section 179 limit			
6	Adjusted Section 179 limit (5 - 4)			Sec. 179
7	Bonus Depreciation Amount (not claimed)	0		Sec. 168(k)
8	Remaining basis for regular depreciation			
9	Rate for regular depreciation-5 Year			
10	Regular depreciation for first year			Sec. 168
11	Total write-off			
12	Ending book value of machinery			

Note: Amount spent for buildings and other real estate is not relevant here. (Bonus could be $50,000)

3 Buy a machine, compute depreciation. Sec. 179. Income limit applies.

Repeat preceding question. Assume Hickory has a taxable income limit of $80,000.
Section 179 deduction cannot cause a loss.
Taxable income limit is taxable income, taking into account all expenses (including regular depreciation), other than the Sec. 179 deduction.
Section 179 write-off will not be $500,000 as shown above, but will be:

4 Buy a machine, compute depreciation. Sec. 179, Asset acquisition limit

Hickory has net income of $4,000,000, before claiming depreciation.
Hickory Corporation purchased a machine on March 1, 2015.
The cost of the machinery was $2,100,000, and it has a life of 7 years.
Cost of machine exceeds the $2,000,000 limit on asset acquisition, for Sec. 179.
Sec. 179 limit is $500,000, LESS excess of cost of assets bought over $2,000,000.
Take maximimum depreciation (Sec. 179 + Bonus Deprec. + Regular Depreciation).
How much total cost recovery deduction will Hickory take on its tax return.

1	Equipment is 7-year property.	Compute	Deduction
2	Cost of equipment	$2,100,000	
3	Threshold - Sec. 179 write-off	2,000,000	
4	Excess (Reduction in 179 limit)	100,000	
5	Regular Section 179 limit	500,000	
6	Adjusted Sec. 179 limit (5 - 4)	400,000	
7	Cost of equipment	$2,100,000	
8	Remaining basis for depreciation	1,700,000	
9	Bonus Depreciation Rate	50%	
10	Bonus Depreciation Amount	850,000	
11	Remaining basis for depreciation	850,000	
12	Rate for regular depreciation-7 Yr.	14.29%	
13	Regular depreciation		
14	Total write-off		
15	Ending book value		

6 Buy two machines, compute depreciation. Mid-Quarter requirement.

Using mid-year convention, you can buy an asset on Dec. 31 and get a half-year of depreciation.
That is not fair. Mid-quarter convention applies if 40% of acquisitions are in the last quarter.

Hickory has net income of $4,000,000, before claiming depreciation.
Hickory bought two machines: one on March 1, 2015, and one on November 1, 2015.
Each machine cost $600,000 ($1,200,000 total) and has a life of 5 years.
Machine acquired in last quarter was 50% (over 40%) of total acquisitions for year.
Assume the company does not claim Section 179 write-off, or bonus depreciation.
Hickory must use the mid-quarter convention.
Mid-quarter convention: each quarter is a separate computation period.

Asset	Acquired	Cost	% in Quarter	Factor	Depreciation	
Machine 1	March 1	$600,000	50%			Table 2a, page 40
Machine 2	Nov. 1	$600,000	50%			Table 2d, page 41
Totals		$1,200,000	100%			

Full-year depreciation rate is 40% for the Double-Declining balance method and a 5-year life.
For machine 2, depreciation at 5% --- is for half of the last quarter, or 1/8 of 40%.
Now assume the company is going to claim a Sec. 179 write-off of $500,000.
Which asset will be chosen, to have $500,000 of its cost written off under section 179?
Choose Machine no. 2. Why?
The amount written off under Sec. 179 is not considered to be a capital expenditure and is not considered to be depreciation expense. The write-off reduces the amounts used to compute whether at least 40% of asset acquisitions ocurred in the last quarter.
You won't meet 40% test. Mid-quarter convention does not apply. (Acquired $100,000 in Q4)

7 Buy Luxury Auto

Hickory bought a business auto on March 1, 2015, at a cost of $60,000.

Acquistion date	Year 1:	March- 2015	
Asset		Auto	
Life		5.0	
Convention		Mid-Year	
New auto cost		$60,000	
Percentage business use		100%	
Business Depreciable base		$60,000	
MACRS Rate		20%	5-year property
MACRS Depreciation		$12,000	
Annual limit of auto deprec.		$3,160	See Pg. 2-27
Percentage business use		100%	
Depreciation			
Add bonus depreciation			
Total			

Note: The provision allowing an extra $8,000 has been extended.

Is the cost of an auto, that will generate depreciation of $3,160.

<u>Straight-line depreciation</u> method is required for buildings.
<u>Mid-month</u> convention is required for buildings. Assume no salvage value.
Deduct 1/2 month's depreciation in month the building is acquired.
Mid-quarter convention: <u>four</u> separate computation periods in the year.
Mid-month convention: <u>twelve</u> separate computation periods in the year.
Building bought in January: deduct the fraction (<u>11.5</u> / <u>12</u>) of a year's deprec.
Residential buildings have 27.5 year depreciable life. Life is 39 years for others.

8 Buy office building

Hickory paid $500,000 for an office building on August 27, 2015.
Hickory allocated $400,000 to the building and $100,000 to the land.
What is Hickory's depreciation deduction on the property in 2015??

Date of acquisition	**Year 1:**	**August 27**	
Asset		**Building**	
Type of asset		**Office**	
Life (non-residential building)		**39.0**	
Convention		**Mid-Month**	
New property cost		$500,000	
Less: allocation to land		($100,000)	
Depreciable base		$400,000	
Deprec. Rate-Year 1	0.963		**Page 2-43**
Depreciation - Year 1			**Table 5**
Deprec. Rate-Year 2	1.605		**Page 2-43**
Depreciation - Year 2			**Table 5**

Instructor Proof

Start with	**$1**
Divide by 39	39
Dep. for 1 yr	0.025641
Divide by 12 mo.	12
Dep. for 1 month	0.00214
Multiply by 4.5	4.5
	$0.0096
	0.9615%

9 Buy Apartment Building

Hickory paid $500,000 for an <u>apartment building</u> on August 27, 2015.
Hickory allocated $400,000 to the building and $100,000 to the land.
What is Hickory's depreciation deduction on the property in 2015?

Date of acquisition.	**Year 1:**	**August 27**	
Asset		**Building**	
Type of asset		**Apartment**	
Life (Residential real estate)		**27.5**	
Convention		**Mid-Month**	
New property cost		$500,000	
Less: allocation to land		($100,000)	
Depreciable base		$400,000	
Deprec. Rate-Year 1	1.364		**Page 2-42**
Depreciation - Year 1			**Table 3**
Deprec. Rate-Year 2	3.636		**Page 2-42**
Depreciation - Year 2			**Table 3**

$1 divided by 27.50 equals =

Instructor Proof

Start with	**$1**
Divide by 27.5	27.5
Dep. for 1 yr	0.036364
Divide by 12	12
Dep. for 1 month	0.00303
Multiply by 4.5	4.5
	$0.0136
	1.3636%

10 Buy a business with covenant not to compete

Hickory bought Sarah's stock in ABC Company on July 1, 2015.
Hickory paid Sarah $30,000 cash for her covenant not to compete or interfere with Hickory's business activities over the next 3 years.
How much deduction can Hickory claim for 2015 for the cost of the covenant?

Cost of covenant not to compete	$30,000	
Amortization Period in years		**Sec. 197**
Amortization for one year		
Months in year	12	
Amortization per month		
Number of months for covenant	6	
Amortization this year		

11 Organization costs

Hickory was organized and began operations on October 1, 2015.
Hickory paid $4,100 for legal fees to obtain a corporate charter.
Hickory elects maximum write-off for its organizational expense.
What amount will Hickory deduct for organizational expenses for 2015?

Organization Costs	**Computations**		**Return**
Amount spent on start-up costs		$4,100	
Threshold		$50,000	
Excess of costs over $50,000		$0	
First-Year write-off amount (limit)	$5,000		
Less: excess expenditure above	$0		
Write-off allowed			
Amount to be amortized		$0	
Amortization period - Years		0	
Amortization period - Months		0	
Amortization per month		$0	
Number of months		12	
Total amortization for year			
Total deduction and amortization			

12 Start-up costs

On 1-1-2015, Hickory Corp. was organized.
In January, Hickory paid $53,000 for startup costs.
Start-up costs are costs incurred after organization, but before fully operational.
New restaurant may <u>pay wait staff in training</u> for first week, before grand opening.
What amount is deducted for start-up costs for 2015?

Start-up costs	Computations		Return	
Amount spent on start-up costs		$53,000		
Threshold		$50,000		
Excess of expenditures over $50,000		$3,000		
First-Year write-off amount (limit)	$5,000			
Less: excess expenditure above	($3,000)			
Write-off				Sec. 195
Amount to be amortized				
Amortization period - Years		15		
Amortization period - Months				
Amortization per month				
Number of months		12		
Total amortization for year				Sec. 195
Total deduction and amortization				

Extra Home work-Chapter 2. The current year is assumed to be 2015.
Note: some of these questions have solutions that were prepared assuming some expiring provisions would not be extended by Congress. Actually, Congress did extend some of those provisions.

1. On January 1, Green Co. bought a warehouse, paying cash of $100,000 and giving a mortgage of $400,000. Green paid back taxes of $5,000 that accrued in the preceding year.
Green will pay $6,000 for taxes that are due for the current year.
What is the total basis of the warehouse and land?

a. $500,000 **b.** $505,000 **c.** $511,000

2. Carol is the business manager for Auto Mart. She bought a new car from the dealership for $30,000. The basis of the car to the dealership was $25,000, and the FMV is $42,000. Auto Mart has a sales policy of posting the price of vehicles and not negotiating sales discounts with customers.
What is Carol's basis in the new car?

a. $ - 0 - **b.** $25,000 **c.** $42,000 **d.** $30,000 **e.** $37,000

3. Ben purchased land and a building by paying cash of $35,000, and assumed the seller's $82,000 mortgage. In addition, Ben paid $3,000 of legal fees related to the purchase. For property tax purposes, the land is valued at $17,000 and the building at $34,000. Ben's basis in the building is

a. $ 17,000 **b.** $ 34,000 **c.** $ 40,000 **d.** $ 80,000 **e.** $120,000

4. Taxpayer bought a business building and land in a single transaction at a bargain.

Description	Amount
Total Cost for both assets	$560,000
Fair Market Value of building	600,000
Fair Market Value of land	100,000

What is the basis of the land?

a. $ 50,000 **b.** $ 70,000 **c.** $80,000 **d.** $560,000 **e.** $700,000

5. Ms. K converted her personal residence to rental property on January 2, 2014.

Transaction	Description	Date	Total	House	Land
Residence converted to rental property	Adj. basis	1-2-2014	$45,000	$40,000	$5,000
	FMV	1-2-2014	$43,000	$38,000	$5,000

What is Ms. K's basis in the house for determining depreciation?

a. $-0- **b.** $38,000 **c.** $40,000 **d.** $43,000 **e.** $45,000

6. Terri owns a truck that cost $40,000 several years ago. After using it personally for two years, she converted the asset to business use when the asset's fair market value was $38,000.
She used the truck in her business and appropriately deducted $5,000 in depreciation on the asset.
Then, she sold the asset for $42,000. What was Terri's realized gain or loss on the sale?

a. No gain or loss **b.** $ 7,000 gain **c.** $27,000 gain **d.** $32,000 gain

7. An individual (Jan) owns an office building with a value of $500,000. The building has a basis after depreciation of $400,000 (cost $600,000 & accumulated depreciation of $200,000).
If Jan sells the building for cash (for it FMV of $500,000) she will recognize a gain of $100,000.
Assume the Jan trades the building for another office building that is also worth $500,000,
Jan has a gain realized on the exchange of $100,000.The gain will not be recognized because this qualifies as a like-kind exchange (rules covered in later chapter). What is the basis of the new building?

a. $ 400,000 **b.** $ 500,000 **c.** $600,000

8. Bob received a gift of art with a value of $10,000, and an adjusted basis of $6,000 to the donor. No gift tax was paid. Bob sold the art for $9,000. What is Bob's gain or (loss) on the sale?

a. $1,000 gain **b.** $3,000 gain **c.** $4,000 gain **d.** $1,000 loss **e.** $3,000 loss

9. Willis received a gift of art valued at $7,000. The donor's basis was $11,000. No gift tax was paid. Willis sold the books to a professional collector for $8,000. What is Willis's gain or (loss) on the sale?

a. $0 gain, $0 loss **b.** $1,000 gain **c.** $4,000 gain **d.** $1,000 loss **e.** $3,000 loss

10. Valerie received a ring as a gift from her aunt. The ring is valued at $12,000 on the date of the gift. Valerie's aunt's basis in the ring is $13,000. Three years later Valerie sold the ring for $14,000. What is the amount of gain or (loss) realized by Valerie on the sale?

a. $ - 0 - **b** $1,000 gain **c.** $2,000 gain **d.** Other

11. Larry gave stock to his son. The stock had a basis of $60,000 and a FMV of $100,000. Larry paid gift tax of $20,000 on this gift. What is the basis of this stock for his son?

a. $-0- **b.** $60,000 **c.** $68,000 **d.** $80,000 **e.** $100,000

12. Sue is a successful executive. She has no current need for the assets she will receive from her elderly parents. Her parents are discussing whether to leave all of their property to Sue in the will, or give her some of the assets now. The assets are substantial and they are worth much more than their basis. Sue would prefer to receive the assets:

a. Now as gifts **b.** Later as an inheritance **c.** Either

13. It is necessary to estimate the useful life of the asset if depreciation is being computed for:

a. Financial Statements **b.** Tax return **c.** Both

14. An accountant is preparing a 2015 income tax return and is computing depreciation for an asset acquired in 2009. The depreciation should be computed using the tax law in effect for:

a. 2009 **b.** 2015 **c.** Either year

15. What is the MACRS recovery period for an office desk?

a. 3 years. **b.** 5 years. **c.** 6 years. **d.** 7 years **e.** 10 years

16. MACRS requires the use of one of three conventions.
For personal property, the general and most common convention is

a. mid-life **b.** mid-quarter. **c.** mid-month. **d.** mid-year.

17. Teton Company purchased a machine on July 22 at a cost of $510,000, which has a recovery period of 7 years. [Page 2-9] The company will NOT claim: (1) bonus depreciation [Pg. 2-22)] or (2) immediate expensing under section 179 [Page 2-17]. What is Teton's cost recovery deduction?

a. $ 72,879 **b.** $ 65,714 **c.** $ 88,459 **d.** $42,086 **e.** $55,500

18. Teton Company purchased a used delivery truck [weighing 8,000 pounds – Pg 28 luxury auto rules not applicable] on July 22 at a cost of $15,000, which has a recovery period of 5 years. (Page 2-9). The company will NOT claim: (1) bonus depreciation [pg. 22, expired] or (2) immediate expensing under section 179 [Page 2-17]. What is Teton's cost recovery deduction?

a. $ 0 **b.** $3,000 **c.** $5,000 **d.** $15,000 **e.** Other

19. Assume Teton Company bought the used delivery truck in the preceding question on December 22. This was the only asset acquisition in the year. This means the asset(s) placed in service in the fourth quarter exceeds 40% of the cost of all assets placed in service in the year. The mid-quarter rules apply in this case. What is Teton's cost recovery deduction? (Page 10+)

a. \$ 750 **b.** \$3,000 **c.** \$5,000 **d.** \$15,000 **e.** Other

20. Steven bought a new truck (5-year MACRS property, weighing 8,000 pounds) to use in his landscaping business on May 13, at a cost of \$18,000. On November 5, Steven took advantage of an end of the season clearance sale to purchase various landscaping equipment (7-year MACRS property) costing \$34,000. Steven does not wish to immediately expense any of the cost of the property purchased this year. What is his current maximum allowable cost recovery deduction?

a. \$ 2,114 **b.** \$ 5,714 **c.** \$ 8,459 **d.** \$12,086 **e.** \$15,500

21. Witt Processing Corporation placed \$2,125,000 of Section 179 property in service for use in its business. What is the amount of Witt Processing's maximum Section 179 deduction for 2015?

a. \$350,000 **b.** \$100,000 **c.** \$375,000 **d.** \$400,000 **e.** Other

22. Henry purchased \$40,000 of equipment. The taxable income of the business is \$20,000 [before sec. 179 deduction]. What is Henry's maximum Section 179 deduction for the current year?

a. \$ 20,000 **b.** \$ 30,000 **c.** \$25,000 **d.** \$40,000 **e.** Other

23. Keith wishes to maximize his total cost recovery deduction for his fixed asset purchases.

On September 15, 2014, he purchases 5-year MACRS property costing \$300,000.

On September 15, 2014, he purchases 7-year MACRS property costing \$400,000.

What will his total cost recovery deduction be on the properties purchased in 2014?

a. \$540,000 **b.** \$505,725 **c.** \$600,000 **d.** \$580,000 **e.** Other

24. Residential rental real estate placed in service on July 17 of the current year is depreciated over:

a. 39 years, straight-line method, mid-month convention.
b. 40 years, straight-line method, mid-month convention.
c. 27.5 years, 150%-declining-balance method, mid-year convention.
d. 27.5 years, straight-line method, mid-month convention.
e. 31.5 years, 200%-declining-balance method, mid-year convention.

25. Nonresidential commercial realty placed in service on March 2, of current year, is depreciated over:

a. 27.5 years, 200%-declining-balance method, mid-year convention.
b. 31.5 years, straight-line method, mid-month convention.
c. 31.5 years, 200%-declining-balance method, mid-year convention
d. 39 years, straight-line method, mid-month convention.
e. 40 years, straight-line method, mid-month convention.

26. Shirley pays \$170,000 for an **office building** on August 27, to use in her consulting business. She properly allocates \$150,000 to the building and \$20,000 to the land.
What is Shirley's depreciation deduction on the property in the second year of ownership?

a. \$1,124 **b.** \$1,443 **c.** \$1,923 **d.** \$3,846 **e.** \$5,454

27. Anderson bought an apartment building on March 27, 2003, at a cost of $2,000,000 (exclusive of the cost allocated to land). He sold the building on November 3, 2015. What is Anderson's cost recovery deduction on the building in 2015, if he wants to take the maximum deduction allowable on the building?

a. $51,510 **b.** $63,630 **c.** $66,660 **d.** $69,690 **e.** $72,720

28. Pet Guard Co. bought and placed into service a company auto costing $60,000 in April, 2015. The auto is used 100% for business travel. What is the depreciation deduction for 2015 on the auto?

a. $ 1,530 **b.** $ 2,900 **c.** $ 3,160 **d.** $ 4,350 **e.** $10,960

29. In **June of 2015**, Chase purchased a new car for $28,000. He used the car 75% for business purposes. What is Chase's maximum depreciation deduction for the car in the current year?

a. $ 2,220 **b.** $ 3,060 **c.** $ 4,200 **d.** $ 2,370 **e.** Other

30. **[Pg. 3-32]** Local Corporation was organized and began operations on October 1, 2015.
It incurs $4,100 in legal fees to obtain the corporate charter. The corporation elects to expense its organizational costs over the shortest allowable period. What amount will Local Corp. report for organizational expenses for 2015?

a. $ 2,050 **b.** $ 4,100 **c.** $ 5,000 **d.** $ 5,600 **e.** $41,000

31. On 1-1-2015, Bell Corp. was organized. On that date, Bell paid $23,000 for startup costs for the corporation. What amount is deducted for 2015?

a. $6,000 b. $5,120 c. $6,200 d. $23,000 e. Other

32. Rose owns a mine, which cost her $460,000 several years ago. In prior years she had claimed depletion in the amount of $140,000. It is estimated that 800,000 tons of minerals remained in the mine at the beginning of the year. During the current year, Rose mined and sold 180,000 tons. What is the amount of Rose's cost depletion deduction for the current year?

a. $ 56,000 **b.** $ 72,000 **c.** $ 80,500 **d.** $103,500 **e.** $180,000

33. Scott bought Franklin's ownership interest in ABC Company on July 1 of current year. Scott paid Franklin $30,000 cash not to compete or interfere with Scott's business activities over the next 3 years. How much cost recovery can Scott claim in the current year because of the covenant not to compete?

a. $ 1,000 **b.** $ 2,000 **c.** $ 3,000 **d.** $ 6,000 **e.** $30,000

34. Jason paid $24,000 for a patent. The patent has 8 years of legal life remaining from date of purchase.

I. If patent is the only asset Jason purchased, he must amortize the patent over 15 years.
II. If patent was part of a purchase of all assets of a business, he must amortize the patent over 15 years.

a. Only statement I is correct. **b.** Only statement II is correct.
c. Both statements are correct. **d.** Neither statement is correct.