Decoupling Federal Bonus Depreciation

For taxpayers claiming the special first year depreciation allowance for certain property acquired after September 10, 2001 and before September 11, 2004 pursuant to the Federal *Job Creation and Worker Assistance Act of 2002* *(P.L. 107-147).*

Pennsylvania's Act 89 of 2002 has decoupled the City of Philadelphia from the bonus depreciation of IRC 168(k). The taxable net income subject to the Philadelphia Business Privilege Tax ("BPT") and Net Profits Tax ("NPT") shall include the amount of the 30% special allowance deductions for depreciation of qualified property claimed and allowed under section 168(k) of the the Internal Revenue Code. **That is, the Federal 30% special allowance depreciation is *not allowed* as a deduction in determining taxable net income for BPT and NPT purposes.**

The required two (2) - step adjustment for BPT/NPT is as follows:

1. The amount of any IRC § 168(k) bonus depreciation for the qualified property ***must*** be added back to net income.

2. After the amount of the IRC § 168(k) bonus depreciation is added back, an additional deduction for depreciation is allowed for the qualified property. The additional deduction is equal to 3/7 of the Federal deduction allowed for depreciation of the qualified property (net of the bonus depreciation of IRC § 168(k) for the tax year). In effect, the ***non***-bonus portion of the allowed Federal depreciation is multiplied by 3/7 to arrive at the additional CNI/BPT/NPT depreciation.

The effect of this two-step adjustment is to ultimately allow a depreciation deduction for the tax year that is consistent with the Internal Revenue Code of 1986 (absent the bonus depreciation provision).

With respect to qualified property that is sold or otherwise disposed of during a tax year, where the bonus depreciation was previously included for BPT/NPT net income, an additional deduction shall be allowed from taxable income to the extent that the depreciation claimed under IRC § 168(k) on the qualified property has not been recovered by the additional deductions provided in step 2 above. That is, the taxpayer will get an additional depreciation deduction in the year of sale or disposal equal to the difference between the IRC § 168(k) bonus depreciation and the cumulative Philadelphia BPT/NPT additional depreciation taken on the qualified property. This will adjust the Philadelphia basis in the asset to be equal to the Federal adjusted basis in the year of sale or disposition.

Please refer to the Department's web site at **www.phila.gov/revenue** for information on filing amended BPT and NPT returns as a result of decoupling.

Example for Decoupling Federal Bonus Depreciation

A calendar year taxpayer acquires a MACRS five (5) year property with an original cost basis of $100,000 on October 1, 2001. The allowable ***Federal*** depreciation on the asset (assuming the 200% declining-balance method and the mid-quarter convention) for calendar tax year 2001 is as follows:

Bonus Depreciation ($100,000 x .30)	$30,000
Annual Depreciation ($100,000 - 30,000) x 40% x 12.5%	$3,500
Total Federal Depreciation	**$33,500**

Required BPT/NPT Adjustment to Taxable Net Income

Step 1 - Add back the Bonus Depreciation taken	$30,000
Step 2 - Calculate the BPT/NPT additional depreciation (Total Federal Depreciation - Bonus Depreciation) x 3/7 ($33,500 - 30,000) x 3/7 =	<$1,500>
Add back to Federal Taxable Income	**$28,500**
Philadelphia BPT/NPT Depreciation	**$5,000**

Note: *The Philadelphia BPT/NPT Depreciation is 5% of the original basis of $100,000. The 5% rate or $5,000 is what a Federal taxpayer using the 200% declining-balance mid-quarter convention would be allowed absent the bonus depreciation provied by IRC § 168(k).*