Policy Update – Decoupling from Federal Depreciation
Business Privilege Tax / Net Profits Tax
Tax Year 2009

For taxpayers claiming the special first year depreciation allowance on certain property placed in service after December 31, 2008 and before January 1, 2010 pursuant to the *American Recovery and Reinvestment Act of 2009(U.S.P.L. 111-5)*.

Pennsylvania's Act 89 of 2002 (signed by Governor Mark Schweiker on June 29, 2002) provides that the taxable net income subject to the Philadelphia Business Privilege Tax (ñBPTò) shall include the amount of the 50% special allowance deduction for depreciation of qualified property claimed and allowed under section 168(k) of the Internal Revenue Code. That is, the Federal special allowance depreciation is ***not allowed*** as a deduction in determining taxable net income for BPT purposes.

With respect to the decoupling from IRC § 168(k), Section 31.1 of Act 89 links the Philadelphia Business Privilege Tax (ñBPTò) net income add-back adjustment to that made in arriving at taxable net income for Pennsylvania Corporate Net Income Tax (ñCNIò) purposes. **For *corporate* BPT filers using Federal net income (i.e. Method II), the decoupling adjustment made for Pennsylvania CNI purposes will also be made for BPT net income purposes.** (*Note ï Taxpayers reporting net income in accordance with their accounting system (i.e. Method I) must use the depreciation method(s) consistent with the elected accounting system. Under no circumstance can that accounting system avail itself of the Federal bonus depreciation provided under IRC § 168(k)).* Since Section 31.1 of Act 89 does not distinguish a different Philadelphia BPT decoupling treatment for *unincorporated* taxpayers, the same adjustment will still need to be made (despite a CNI return not being filed). The required two - step adjustment as provided by Act 89 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 depreciation.

Historically, Act 89 permitted the recovery of the entire amount of the 30% first year special allowance depreciation originally allowed under the Federal ***Job Creation and Worker Assistance Act of 2002 (U.S.P.L. 107-147)*** by the time the property was fully depreciated for Federal tax purposes. The current mathematical methodology of Act 89 (determined when the Federal first year bonus depreciation was 30%) has not been amended to reflect the 50% bonus depreciation allowance and therefore will prevent a portion of the 50% bonus depreciation from being recovered by the time the asset is fully depreciated for Federal tax purposes. To achieve the full recovery of the entire bonus depreciation, Act 89 permits the continued deduction of any remaining un-recovered bonus depreciation until the total amount has been claimed. In cases where the asset is disposed of prior to the taxpayer recovering the full amount of the disallowed bonus depreciation, the taxpayer may deduct the remaining disallowed bonus depreciation in the year of disposition. (***Refer to the Pennsylvania DOR policy at www.revenue.pa.us/revenue)***.

Note on Net Profits Tax - Act 89 does not specifically address the bonus depreciation as it relates to the Philadelphia Net Profits Tax (ñNPTò). ***However***, for taxpayers who use the Federal Tax accounting method to report their NPT, the bonus depreciation of IRC § 168(k) will ***not*** be allowed as a deduction to arrive at Philadelphia taxable Net Profits. BPT Regulation 403 requires consistency in the accounting method used for BPT Method I and NPT purposes. Since Act 89 prohibits a BPT Method I filer from taking the bonus depreciation, by operation of the regulation it also prevents a NPT filer from taking the bonus depreciation as well.

Example for Decoupling Federal Bonus Depreciation

A calendar year taxpayer acquires MACRS five (5) year property with an original cost basis of $100,000 on October 1, 2009. The allowable ***Federal*** depreciation on the asset (assuming the 200% declining-balance method and the mid-quarter convention) for calendar tax year 2009 is as follows:

Bonus Depreciation ($100,000 x .50)	$50,000
Annual Depreciation ($100,000 ï 50,000) x 40%x 12.5%)	$2,500

(A) Total Federal Depreciation **$ 52,500**

Required BPT / NPT Adjustment to Taxable Net Income

1. **Step 1** ï Add back the Bonus Depreciation taken $50,000

2. **Step 2** - Calculate the BPT/ NPT additional depreciation

(Total Federal Depreciation ï Bonus Depreciation) X 3/7

($52,500 ï 50,000) X 3/7 = <$1,071>

(B) Add back to Federal Taxable Income **$48,929**

(C) Philadelphia BPT / NPT Depreciation **$ 3,571**

Line (A) – Line (B)