

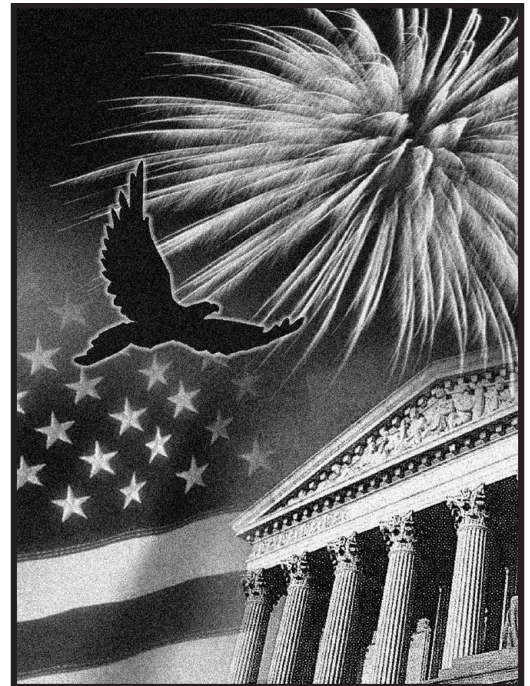
# Publication 946

## How To Depreciate Property

- Section 179 Deduction
- Special Depreciation Allowance
- MACRS
- Listed Property

For use in preparing **2023** Returns

Volume 3 of 6



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Publication 946 (Rev. 2023) Catalog Number 39330R  
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**The mid-month convention.** Use this convention for nonresidential real property, residential rental property, and any railroad grading or tunnel bore.

Under this convention, you treat all property placed in service or disposed of during a month as placed in service or disposed of at the midpoint of the month. This means that a one-half month of depreciation is allowed for the month the property is placed in service or disposed of.

Your use of the midmonth convention is indicated by the "MM" already shown under column (e) in Part III of Form 4562.

**The mid-quarter convention.** Use this convention if the midmonth convention does not apply and the total depreciable bases of MACRS property you placed in service during the last 3 months of the tax year (excluding nonresidential real property, residential rental property, any railroad grading or tunnel bore, property placed in service and disposed of in

the same year, and property that is being depreciated under a method other than MACRS) are more than 40% of the total depreciable bases of all MACRS property you placed in service during the entire year.

Under this convention, you treat all property placed in service or disposed of during any quarter of the tax year as placed in service or disposed of at the midpoint of that quarter. This means that, for a 12month tax year,  $1\frac{1}{2}$  months of depreciation is allowed for the quarter the property is placed in service or disposed of.

If you use this convention, enter “MQ” under column (e) in Part III of Form 4562.



*For purposes of determining whether the mid-quarter convention applies, the depreciable basis of property you placed in service during the tax year reflects the reduction in basis for amounts expensed under section 179 and the part of the basis of property attributable to personal use.*

*However, it does not reflect any reduction in basis for any special depreciation allowance.*

**The half-year convention.** Use this convention if neither the mid-quarter convention nor the midmonth convention applies.

Under this convention, you treat all property placed in service or disposed of during a tax year as placed in service or disposed of at the midpoint of the year. This means that for a 12-month tax year, a one-half year of depreciation is allowed for the year the property is placed in service or disposed of.

If you use this convention, enter "HY" under column (e) in Part III of Form 4562.

See [Figuring the Deduction for a Short Tax Year](#), later, for information on the short tax year rules.

# **Which Depreciation Method Applies?**

## **Terms you may need to know (see Glossary):**

Declining balance method

Listed property

Nonresidential real property

Placed in service

Property class

Recovery period

Residential rental property

Straight line method

Tax exempt

MACRS provides three depreciation methods under GDS and one depreciation method under ADS.

- The 200% declining balance method over a GDS recovery period.
- The 150% declining balance method over a GDS recovery period.
- The straight line method over a GDS recovery period.
- The straight line method over an ADS recovery period.



*For property placed in service before 1999, you could have elected the 150% declining balance method using the ADS recovery periods for certain property classes. If you made this election, continue to use the same method and recovery period for that property.*

[Table 4-1](#) lists the types of property you can depreciate under each method. It also gives a brief explanation of the method, including any benefits that may apply.

## **Depreciation Methods for Farm Property**

If you place personal property in service in a farming business after 1988, and before 2018, you must generally depreciate it under GDS using the 150% declining balance method unless you are a farmer who must depreciate the property under ADS using the straight line method or you elect to depreciate the property under GDS or ADS using the straight line method. You can depreciate real property using the straight line method under either GDS or ADS.

**Note.** For 3, 5, 7, or 10year property used in a farming business and placed in service after 2017, in tax years ending after 2017, the 150% declining balance method is no longer required. However, the 150% declining balance method will continue to apply to any 15 or 20year property used in a farming business to which the straight line method does not apply or to property for which you



elect the use of the 150% declining balance method.

**Fruit or nut trees and vines.** Depreciate trees and vines bearing fruits or nuts under GDS using the straight line method over a recovery period of 10 years.

**ADS required for some farmers.** If you elect not to apply the uniform capitalization rules to any plant produced in your farming business, you must use ADS. You must use ADS for all property you place in service in any year the election is in effect. See the regulations under section 263A of the Internal Revenue Code for information on the uniform capitalization rules that apply to farm property.

## Electing a Different Method

As shown in [Table 4-1](#), you can elect a different method for depreciation for certain types of property. You must make the election by the due date of the return (including extensions) for the year you placed the property in service. However, if you timely filed your return for the year without making the election, you can still make the election by filing an amended return within 6 months of the due date of the return (excluding extensions). Attach the election to the amended return and write “Filed pursuant to section 301.91002” on the election statement. File the amended return at the same address you filed the original return. Once you make the election, you cannot change it.



*If you elect to use a different method for one item in a property class, you must apply the same method to all property in that class placed in service during*

*the year of the election. However, you can make the election on a property-by-property basis for nonresidential real and residential rental property.*

**150% election.** Instead of using the 200% declining balance method over the GDS recovery period for property in the 3, 5, 7, or 10-year property class, you can elect to use the 150% declining balance method. Make the election by entering "150 DB" under column (f) in Part III of Form 4562.

**Straight line election.** Instead of using either the 200% or 150% declining balance method over the GDS recovery period, you can elect to use the straight line method over the GDS recovery period. Make the election by entering "S/L" under column (f) in Part III of Form 4562.

**Election of ADS.** As explained earlier under [Which Depreciation System \(GDS or ADS\) Applies](#), you can elect to use ADS even though your property may come under GDS.

ADS uses the straight line method of depreciation over fixed ADS recovery periods. Most ADS recovery periods are listed in [Appendix B](#), or see the table under [Recovery Periods Under ADS](#), earlier.

Make the election by completing line 20 in Part III of Form 4562.

**15 or 20year farm property.** Instead of using the 150% declining balance method over a GDS recovery period for 15 or 20year property you use in a farming business (other than real property), you can elect to depreciate it using either of the following methods.

- The straight line method over a GDS recovery period.
- The straight line method over an ADS recovery period.

Table 4-1. Depreciation Methods

Note. The declining balance method is abbreviated as DB and the straight line method is abbreviated as SL.		
Method	Type of Property	Benefit
GDS using 200% DB	<ul style="list-style-type: none"><li>• Nonfarm 3-, 5-, 7-, and 10-year property</li><li>• Farm 3-, 5-, 7-, and 10-year property placed in service after 2017, in tax years ending after 2017</li></ul>	<ul style="list-style-type: none"><li>• Provides a greater deduction during the earlier recovery years</li><li>• Changes to SL when that method provides an equal or greater deduction</li></ul>
GDS using 150% DB	<ul style="list-style-type: none"><li>• Farm 3-, 5-, 7-, or 10-year property placed in service before 2018</li><li>• All 15- and 20-year property</li><li>• Nonfarm 3-, 5-, 7-, or 10-year property<sup>2</sup></li><li>• Farm 3-, 5-, 7-, or 10-year property placed in service after 2017<sup>2</sup></li></ul>	<ul style="list-style-type: none"><li>• Provides a greater deduction during the earlier recovery years</li><li>• Changes to SL when that method provides an equal or greater deduction<sup>1</sup></li></ul>
GDS using SL	<ul style="list-style-type: none"><li>• Nonresidential real property</li><li>• Residential rental property</li><li>• Trees or vines bearing fruits or nuts</li><li>• Water utility property</li><li>• All 3-, 5-, 7-, 10-, 15-, and 20-year property<sup>2</sup></li><li>• Property for which you elected section 168(k) (4) of the Internal Revenue Code for a tax year beginning before January 1, 2018</li><li>• Qualified improvement property (as defined in section 168(e)(6) of the Internal Revenue Code) placed in service after 2017</li></ul>	<ul style="list-style-type: none"><li>• Provides for equal yearly deductions (except for the first and last years)</li></ul>
ADS using SL	<ul style="list-style-type: none"><li>• Listed property used 50% or less for business</li><li>• Property used predominantly outside the United States</li><li>• Tax-exempt property</li><li>• Tax-exempt bond-financed property</li><li>• Farm property used when an election not to apply the uniform capitalization rules is in effect</li><li>• Imported property<sup>3</sup></li><li>• Any property for which you elect to use this method<sup>4</sup></li><li>• Any nonresidential real property, residential rental property, or 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)</li><li>• Any property that has a recovery period of 10 years or more under GDS that is held by an electing farming business (as defined in section 163(j)(7)(C) of the Internal Revenue Code)</li></ul>	<ul style="list-style-type: none"><li>• Provides for equal yearly deductions (except for the first and last years)</li></ul>
<sup>1</sup> The MACRS percentage tables in Appendix A have the switch to the straight line method built into their rates. <sup>2</sup> See section 168(b)(5) of the Internal Revenue Code. <sup>3</sup> See section 168(g)(6) of the Internal Revenue Code. <sup>4</sup> See section 168(g)(7) of the Internal Revenue Code.		

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# **How Is the Depreciation Deduction Figured?**

## **Terms you may need to know (see Glossary):**

Adjusted basis

Amortization

Basis

Business/investment use

Convention

Declining balance method

Disposition

Exchange

Nonresidential real property

Placed in service

Property class

Recovery period

## Straight line method

### Unadjusted basis

To figure your depreciation deduction under MACRS, you first determine the depreciation system, property class, placed in service date, basis amount, recovery period, convention, and depreciation method that apply to your property. Then, you are ready to figure your depreciation deduction. You can figure it using a percentage table provided by the IRS, or you can figure it yourself without using the table.

## **Using the MACRS Percentage Tables**

To help you figure your deduction under MACRS, the IRS has established percentage tables that incorporate the applicable convention and depreciation method. These percentage tables are in [Appendix A](#) near the end of this publication.

**Which table to use.** [Appendix A](#) contains the [MACRS Percentage Table Guide](#), which is



designed to help you locate the correct percentage table to use for depreciating your property. The percentage tables immediately follow the guide.

## **Rules Covering the Use of the Tables**

The following rules cover the use of the percentage tables.

1. You must apply the rates in the percentage tables to your property's unadjusted basis.
2. You cannot use the percentage tables for a short tax year. See [Figuring the Deduction for a Short Tax Year](#), later, for information on the short tax year rules.
3. Once you start using the percentage tables for any item of property, you must generally continue to use them for the entire recovery period of the property.

4. You must stop using the tables if you adjust the basis of the property for any reason other than:
  - a. Depreciation allowed or allowable, or
  - b. An addition or improvement to that property that is depreciated as a separate item of property.

Basis adjustments other than those made due to the items listed in (4) include an increase in basis for the recapture of a clean-fuel deduction or credit and a reduction in basis for a casualty loss.

**Basis adjustment due to recapture of clean-fuel vehicle deduction or credit.** If you increase the basis of your property because of the recapture of part or all of a deduction for clean-fuel vehicles or the credit for clean-fuel vehicle refueling property placed in service before January 1, 2006, you cannot continue to use the percentage tables.

For the year of the adjustment and the remaining recovery period, you must figure the depreciation deduction yourself using the property's adjusted basis at the end of the year. See [\*Figuring the Deduction Without Using the Tables\*](#), later.

**Basis adjustment due to casualty loss.** If you reduce the basis of your property because of a casualty, you cannot continue to use the percentage tables. For the year of the adjustment and the remaining recovery period, you must figure the depreciation yourself using the property's adjusted basis at the end of the year. See [\*Figuring the Deduction Without Using the Tables\*](#), later.

**Example.** On October 26, 2022, Sandra and Frank Elm, calendar year taxpayers, bought and placed in service in their business a new item of 7-year property. It cost \$39,000 and they elected a section 179 deduction of \$24,000. They also made an election under section 168(k) (7) not to deduct the special

depreciation allowance for 7-year property placed in service in 2022. Their unadjusted basis after the section 179 deduction was \$15,000 (\$39,000 – \$24,000). They figured their MACRS depreciation deduction using the percentage tables. For 2022, their MACRS depreciation deduction was \$536.

In July 2023, the property was vandalized and they had a deductible casualty loss of \$3,000. Sandra and Frank must adjust the property's basis for the casualty loss, so they can no longer use the percentage tables. Their adjusted basis at the end of 2023, before figuring their 2023 depreciation, is \$11,464. They figure that amount by subtracting the 2022 MACRS depreciation of \$536 and the casualty loss of \$3,000 from the unadjusted basis of \$15,000. They must now figure their depreciation for 2023 without using the percentage tables.

## **Figuring the Unadjusted Basis of Your Property**

You must apply the table rates to your property's unadjusted basis each year of the recovery period. Unadjusted basis is the same basis amount you would use to figure gain on a sale, but you figure it without reducing your original basis by any MACRS depreciation taken in earlier years. However, you do reduce your original basis by other amounts, including the following.

- Any amortization taken on the property.
- Any section 179 deduction claimed.
- Any special depreciation allowance taken on the property.

For business property you purchase during the year, the unadjusted basis is its cost minus these and other applicable adjustments. If you trade property, your unadjusted basis in the property received is

the cash paid plus the adjusted basis of the property traded minus these adjustments.

## **MACRS Worksheet**

You can use this worksheet to help you figure your depreciation deduction using the percentage tables. Use a separate worksheet for each item of property. Then, use the information from this worksheet to prepare Form 4562.



*Do not use this worksheet for automobiles. Use the Depreciation Worksheet for Passenger Automobiles in chapter 5.*

**MACRS Worksheet**  
*Keep for Your Records*



**Part I**

- 1. MACRS system (GDS or ADS) ..... \_\_\_\_\_
- 2. Property class ..... \_\_\_\_\_
- 3. Date placed in service ..... \_\_\_\_\_
- 4. Recovery period ..... \_\_\_\_\_
- 5. Method and convention ..... \_\_\_\_\_
- 6. Depreciation rate (from tables) ..... \_\_\_\_\_

**Part II**

- 7. Cost or other basis\* ..... \$ \_\_\_\_\_
- 8. Business/investment use ..... % \_\_\_\_\_
- 9. Multiply line 7 by line 8 ..... \$ \_\_\_\_\_
- 10. Total claimed for section 179 deduction and other items ..... \$ \_\_\_\_\_
- 11. Subtract line 10 from line 9. This is your tentative basis for depreciation ..... \$ \_\_\_\_\_
- 12. Multiply line 11 by the applicable percentage if the special depreciation allowance applies. This is your special depreciation allowance. Enter -0- if this is not the year you placed the property in service, the property is not qualified property, or you elected not to claim a special allowance ..... \$ \_\_\_\_\_
- 13. Subtract line 12 from line 11. This is your basis for depreciation ..... \_\_\_\_\_

14. Depreciation rate (from line 6) .....	_____
15. Multiply line 13 by line 14. This is your MACRS depreciation deduction .....	\$ =====
* If real estate, do not include cost (basis) of land.	



The following example shows how to figure your MACRS depreciation deduction using the percentage tables and the MACRS Worksheet.

**Example.** You bought office furniture (7-year property) for \$10,000 and placed it in service on August 11, 2023.

You use the furniture only for business. This is the only property you placed in service this year. You did not elect a section 179 deduction and the property is not qualified property for purposes of claiming a special depreciation allowance, so your property's unadjusted basis is its cost, \$10,000. You use GDS and the half-year convention to figure your depreciation. You refer to the [MACRS Percentage Table Guide](#) in Appendix A and find that you should use Table A-1. Multiply your property's unadjusted basis each year by the percentage for 7-year property given in Table A-1. You figure your depreciation deduction using the MACRS Worksheet as follows.

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# MACRS Worksheet

Keep for Your Records



## Part I

1. MACRS system (GDS or ADS) .....	GDS
2. Property class .....	7-year
3. Date placed in service .....	8/11/23
4. Recovery period .....	7-year
5. Method and convention .....	200%DB/Half-Year
6. Depreciation rate (from tables) .....	0.1429

## Part II

7. Cost or other basis* .....	\$10,000
8. Business/investment use .....	100 %
9. Multiply line 7 by line 8 .....	\$10,000
10. Total claimed for section 179 deduction and other items .....	-0-
11. Subtract line 10 from line 9. This is your tentative basis for depreciation .....	\$10,000
12. Multiply line 11 by the applicable percentage if the special depreciation allowance applies. This is your special depreciation allowance. Enter -0- if this is not the year you placed the property in service, the property is not qualified property, or you elected not to claim a special allowance .....	-0-
13. Subtract line 12 from line 11. This is your basis for depreciation .....	\$10,000
14. Depreciation rate (from line 6) .....	0.1429
15. Multiply line 13 by line 14. This is your MACRS depreciation deduction .....	\$1,429

\* If real estate, do not include cost (basis) of land.

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If there are no adjustments to the basis of the property other than depreciation, your depreciation deduction for each subsequent year of the recovery period will be as follows.

<u>Year</u>	<u>Basis</u>	<u>Percentage</u>	<u>Deduction</u>
2024 .....	\$10,000	24.49%	\$2,449
2025 .....	10,000	17.49	1,749
2026 .....	10,000	12.49	1,249
2027 .....	10,000	8.93	893
2028 .....	10,000	8.92	892
2029 .....	10,000	8.93	893
2030 .....	10,000	4.46	446

## Examples

The following examples are provided to show you how to use the percentage tables. In both examples, assume the following.

- You use the property only for business.
- You use the calendar year as your tax year.
- You use GDS for all the properties.

**Example 1.** You bought a building and land for \$120,000 and placed it in service on March 8. The sales contract showed that the building cost \$100,000 and the land cost \$20,000. It is nonresidential real property. The building's unadjusted basis is its original cost, \$100,000.

You refer to the [MACRS Percentage Table Guide](#) in Appendix A and find that you should use Table A-7a. March is the third month of your tax year, so multiply the building's unadjusted basis, \$100,000, by the percentages for the third month in Table A-7a. Your depreciation deduction for each of the first 3 years is as follows.

<b>Year</b>	<b>Basis</b>	<b>Percentage</b>	<b>Deduction</b>
1st . . . . .	\$100,000	2.033%	\$2,033
2nd . . . . .	100,000	2.564	2,564

3rd . . . . .	100,000	2.564	2,564
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**Example 2.** During the year, you bought a machine (7-year property) for \$4,000, office furniture (7-year property) for \$1,000, and a computer (5-year property) for \$5,000. You placed the machine in service in January, the furniture in September, and the computer in October. You do not elect a section 179 deduction and none of these items is qualified property for purposes of claiming a special depreciation allowance.

You placed property in service during the last 3 months of the year, so you must first determine if you have to use the mid-quarter convention. The total bases of all property you placed in service during the year is \$10,000. The \$5,000 basis of the computer, which you placed in service during the last 3 months (the fourth quarter) of your tax year, is more than 40% of the total bases of all property (\$10,000) you placed in service

during the year. Therefore, you must use the mid-quarter convention for all three items.

You refer to the [MACRS Percentage Table Guide](#) in Appendix A to determine which table you should use under the mid-quarter convention. The machine is 7-year property placed in service in the first quarter, so you use [Table A-2](#) . The furniture is 7-year property placed in service in the third quarter, so you use [Table A-4](#). Finally, because the computer is 5-year property placed in service in the fourth quarter, you use [Table A-5](#). Knowing what table to use for each property, you figure the depreciation for the first 2 years as follows.



<b>Year</b>	<b>Property</b>	<b>Basis</b>	<b>Percentage Deduction</b>	
1st	Machine	\$4,000	25.00	\$1,000
2nd	Machine	4,000	21.43	857
1st	Furniture	1,000	10.71	107
2nd	Furniture	1,000	25.51	255
1st	Computer	5,000	5.00	250
2nd	Computer	5,000	38.00	1,900

## **Sale or Other Disposition Before the Recovery Period Ends**

If you sell or otherwise dispose of your property before the end of its recovery period, your depreciation deduction for the year of the disposition will be only part of the depreciation amount for the full year. You have disposed of your property if you have permanently withdrawn it from use in your business or income-producing activity because of its sale, exchange, retirement, abandonment, involuntary conversion, or destruction. After you figure the full-year depreciation amount, figure the deductible part using the convention that applies to the property.

**Half-year convention used.** For property for which you used a half-year convention, the depreciation deduction for the year of the disposition is half the depreciation determined for the full year.

**Mid-quarter convention used.** For property for which you used the mid-quarter convention, figure your depreciation deduction for the year of the disposition by multiplying a full year of depreciation by the percentage listed below for the quarter in which you disposed of the property.

<u>Quarter</u>	<u>Percentage</u>
First . . . . .	12.5%
Second . . . . .	37.5
Third . . . . .	62.5
Fourth . . . . .	87.5

**Example.** On December 2, 2020, you placed in service an item of 5-year property costing \$10,000. You did not claim a section 179 deduction and the property does not qualify for a special depreciation allowance. Your unadjusted basis for the property was \$10,000. You used the mid-quarter convention because this was the only item of business property you placed in service in 2020 and it was placed in service during the

last 3 months of your tax year. Your property is in the 5-year property class, so you used [Table A-5](#) to figure your depreciation deduction. Your deductions for 2020, 2021, and 2022 were \$500 (5% of \$10,000), \$3,800 (38% of \$10,000), and \$2,280 (22.80% of \$10,000), respectively. You disposed of the property on April 6, 2023. To determine your depreciation deduction for 2023, first figure the deduction for the full year. This is \$1,368 (13.68% of \$10,000). April is in the second quarter of the year, so you multiply \$1,368 by 37.5% (0.375) to get your depreciation deduction of \$513 for 2023.

**Mid-month convention used.** If you dispose of residential rental or nonresidential real property, figure your depreciation deduction for the year of the disposition by multiplying a full year of depreciation by a fraction. The numerator of the fraction is the number of months (including partial months) in the year

that the property is considered in service. The denominator is 12.

**Example.** On July 2, 2021, you purchased and placed in service residential rental property. The property cost \$100,000, not including the cost of land. You used [Table A-6](#) to figure your MACRS depreciation for this property. You sold the property on March 2, 2023. You file your tax return based on the calendar year.

A full year of depreciation for 2023 is \$3,636. This is \$100,000 multiplied by 0.03636 (the percentage for the seventh month of the third recovery year) from [Table A-6](#). You then apply the mid-month convention for the 2 1/2 months of use in 2023. Treat the month of disposition as one-half month of use. Multiply \$3,636 by the fraction, 2.5 over 12, to get your 2023 depreciation deduction of \$757.50.

## Figuring the Deduction Without Using the Tables

Instead of using the rates in the percentage tables to figure your depreciation deduction, you can figure it yourself. Before making the computation each year, you must reduce your adjusted basis in the property by the depreciation claimed the previous year(s).



*Figuring MACRS deductions without using the tables will generally result in a slightly different amount than using the tables.*

### Declining Balance Method

When using a declining balance method, you apply the same depreciation rate each year to the adjusted basis of your property. You must use the applicable convention for the first tax year and you must switch to the straight line method beginning in the first year for which it will give an equal or greater deduction. The straight line method is explained later.

You figure depreciation for the year you place property in service as follows.

1. Multiply your adjusted basis in the property by the declining balance rate.
2. Apply the applicable convention.

You figure depreciation for all other years (before the year you switch to the straight line method) as follows.

1. Reduce your adjusted basis in the property by the depreciation allowed or allowable in earlier years.
2. Multiply this new adjusted basis by the same declining balance rate used in earlier years.

If you dispose of property before the end of its recovery period, see [Using the Applicable Convention](#), later, for information on how to figure depreciation for the year you dispose of it.

Figuring depreciation under the declining balance method and switching to the straight line method is illustrated in [Example 1](#), later, under *Examples*.

**Declining balance rate.** You figure your declining balance rate by dividing the specified declining balance percentage (150% or 200% changed to a decimal) by the number of years in the property's recovery period. For example, for 3year property depreciated using the 200% declining balance method, divide 2.00 (200%) by 3 to get 0.6667, or a 66.67% declining balance rate. For 15year property depreciated using the 150% declining balance method, divide 1.50 (150%) by 15 to get 0.10, or a 10% declining balance rate.

The following table shows the declining balance rate for each property class and the first year for which the straight line method gives an equal or greater deduction.



<b>Property Class</b>	<b>Method</b>	<b>Declining Balance Rate</b>	<b>Year</b>
3-year	200% DB	66.667%	3rd
5-year	200% DB	40.0	4th
7-year	200% DB	28.571	5th
10-year	200% DB	20.0	7th
15-year	150% DB	10.0	7th
20-year	150% DB	7.5	9th

## **Straight Line Method**

When using the straight line method, you apply a different depreciation rate each year to the adjusted basis of your property. You must use the applicable convention in the

year you place the property in service and the year you dispose of the property.

You figure depreciation for the year you place property in service as follows.

1. Multiply your adjusted basis in the property by the straight line rate.
2. Apply the applicable convention.

You figure depreciation for all other years (including the year you switch from the declining balance method to the straight line method) as follows.

1. Reduce your adjusted basis in the property by the depreciation allowed or allowable in earlier years (under any method).
2. Determine the depreciation rate for the year.
3. Multiply the adjusted basis figured in (1) by the depreciation rate figured in (2).

If you dispose of property before the end of its recovery period, see [Using the Applicable Convention](#), later, for information on how to figure depreciation for the year you dispose of it.

**Straight line rate.** You determine the straight line depreciation rate for any tax year by dividing the number 1 by the years remaining in the recovery period at the beginning of that year. When figuring the number of years remaining, you must take into account the convention used in the year you placed the property in service. If the number of years remaining is less than 1, the depreciation rate for that tax year is 1.0 (100%).

## **Using the Applicable Convention**

The applicable convention (discussed earlier under [Which Convention Applies](#)) affects how you figure your depreciation deduction for the year you place your property in service and for the year you dispose of it. It determines

how each year, so it also affects the depreciation rate for property you depreciate under the straight line method. See [\*Straight line rate\*](#) in the previous discussion. Use the applicable convention, as explained in the following discussions.

**Half-year convention.** If this convention applies, you deduct a half-year of depreciation for the first year and the last year that you depreciate the property. You deduct a full year of depreciation for any other year during the recovery period.

Figure your depreciation deduction for the year you place the property in service by dividing the depreciation for a full year by 2. If you dispose of the property before the end of the recovery period, figure your depreciation deduction for the year of the disposition the same way. If you hold the property for the entire recovery period, your depreciation deduction for the year that includes the final 6 months of the recovery

period is the amount of your unrecovered basis in the property.

**Mid-quarter convention.** If this convention applies, the depreciation you can deduct for the first year you depreciate the property depends on the quarter in which you place the property in service.

A quarter of a full 12month tax year is a period of 3 months. The first quarter in a year begins on the first day of the tax year. The second quarter begins on the first day of the fourth month of the tax year. The third quarter begins on the first day of the seventh month of the tax year. The fourth quarter begins on the first day of the tenth month of the tax year. A calendar year is divided into the following quarters.

<b>Quarter</b>	<b>Months</b>
First.....	January, February, March
Second.....	April, May, June
Third.....	July, August, September
Fourth.....	October, November, December

Figure your depreciation deduction for the year you place the property in service by multiplying the depreciation for a full year by the percentage listed below for the quarter you place the property in service.

<b>Quarter</b>	<b>Percentage</b>
First.....	87.5%
Second.....	62.5
Third.....	37.5
Fourth.....	12.5

If you dispose of the property before the end of the recovery period, figure your depreciation deduction for the year of the disposition by multiplying a full year of depreciation by the percentage listed below for the quarter you dispose of the property.

<b>Quarter</b>	<b>Percentage</b>
First.....	12.5%

Second.....	37.5
Third.....	62.5
Fourth.....	87.5

If you hold the property for the entire recovery period, your depreciation deduction for the year that includes the final quarter of the recovery period is the amount of your unrecovered basis in the property.

**Mid-month convention.** If this convention applies, the depreciation you can deduct for the first year that you depreciate the property depends on the month in which you place the property in service. Figure your depreciation deduction for the year you place the property in service by multiplying the depreciation for a full year by a fraction. The numerator of the fraction is the number of full months in the year that the property is in service plus  $\frac{1}{2}$  (or 0.5). The denominator is 12.



If you dispose of the property before the end of the recovery period, figure your depreciation deduction for the year of the disposition the same way. If you hold the property for the entire recovery period, your depreciation deduction for the year that includes the final month of the recovery period is the amount of your unrecovered basis in the property.

**Example.** You use the calendar year and place nonresidential real property in service in August. The property is in service 4 full months (September, October, November, and December). Your numerator is 4.5 (4 full months plus 0.5). You multiply the depreciation for a full year by  $4.5/12$ , or 0.375.

## **Examples**

The following examples show how to figure depreciation under MACRS without using the percentage tables. Figures are rounded for purposes of the examples. Assume for all the

examples that you use a calendar year as your tax year.

***Example 1—200% DB method and half-year convention.*** In February, you placed in service depreciable property with a 5-year recovery period and a basis of \$1,000. You do not elect to take the section 179 deduction and the property does not qualify for a special depreciation allowance. You use GDS and the 200% DB method to figure your depreciation. When the SL method results in an equal or larger deduction, you switch to the SL method. You did not place any property in service in the last 3 months of the year, so you must use the half-year convention.

***First year.*** You figure the depreciation rate under the 200% DB method by dividing 2 (200%) by 5 (the number of years in the recovery period). The result is 40%. You multiply the adjusted basis of the property (\$1,000) by the 40% DB rate. You apply the half-year convention by dividing the result

(\$400) by 2. Depreciation for the first year under the 200% DB method is \$200.

You figure the depreciation rate under the SL method by dividing 1 by 5, the number of years in the recovery period. The result is 20%. You multiply the adjusted basis of the property (\$1,000) by the 20% SL rate. You apply the half-year convention by dividing the result (\$200) by 2. Depreciation for the first year under the SL method is \$100.

The DB method provides a larger deduction, so you deduct the \$200 figured under the 200% DB method.

***Second year.*** You reduce the adjusted basis (\$1,000) by the depreciation claimed in the first year (\$200). You multiply the result (\$800) by the DB rate (40%). Depreciation for the second year under the 200% DB method is \$320.

You figure the SL depreciation rate by dividing 1 by 4.5, the number of years remaining in

the recovery period. (Based on the half-year convention, you used only half a year of the recovery period in the first year.) You multiply the reduced adjusted basis (\$800) by the result (22.22%). Depreciation under the SL method for the second year is \$178.

The DB method provides a larger deduction, so you deduct the \$320 figured under the 200% DB method.

***Third year.*** You reduce the adjusted basis (\$800) by the depreciation claimed in the second year (\$320). You multiply the result (\$480) by the DB rate (40%). Depreciation for the third year under the 200% DB method is \$192.

You figure the SL depreciation rate by dividing 1 by 3.5. You multiply the reduced adjusted basis (\$480) by the result (28.57%). Depreciation under the SL method for the third year is \$137.

The DB method provides a larger deduction, so you deduct the \$192 figured under the 200% DB method.

***Fourth year.*** You reduce the adjusted basis (\$480) by the depreciation claimed in the third year (\$192). You multiply the result (\$288) by the DB rate (40%). Depreciation for the fourth year under the 200% DB method is \$115.

You figure the SL depreciation rate by dividing 1 by 2.5. You multiply the reduced adjusted basis (\$288) by the result (40%). Depreciation under the SL method for the fourth year is \$115.

The SL method provides an equal deduction, so you switch to the SL method and deduct the \$115.

***Fifth year.*** You reduce the adjusted basis (\$288) by the depreciation claimed in the fourth year (\$115) to get the reduced adjusted basis of \$173. You figure the SL

depreciation rate by dividing 1 by 1.5. You multiply the reduced adjusted basis (\$173) by the result (66.67%). Depreciation under the SL method for the fifth year is \$115.

***Sixth year.*** You reduce the adjusted basis (\$173) by the depreciation claimed in the fifth year (\$115) to get the reduced adjusted basis of \$58. There is less than 1 year remaining in the recovery period, so the SL depreciation rate for the sixth year is 100%. You multiply the reduced adjusted basis (\$58) by 100% to arrive at the depreciation deduction for the sixth year (\$58).

***Example 2—SL method and midmonth convention.*** In January, you bought and placed in service a building for \$100,000 that is nonresidential real property with a recovery period of 39 years. The adjusted basis of the building is its cost of \$100,000. You use GDS, the SL method, and the midmonth convention to figure your depreciation.

**First year.** You figure the SL depreciation rate for the building by dividing 1 by 39 years. The result is 0.02564. The depreciation for a full year is \$2,564 ( $\$100,000 \times 0.02564$ ). Under the midmonth convention, you treat the property as placed in service in the middle of January. You get 11.5 months of depreciation for the year. Expressed as a decimal, the fraction of 11.5 months divided by 12 months is 0.958. Your first-year depreciation for the building is \$2,456 ( $\$2,564 \times 0.958$ ).

**Second year.** You subtract \$2,456 from \$100,000 to get your adjusted basis of \$97,544 for the second year. The SL rate is 0.02629. This is 1 divided by the remaining recovery period of 38.042 years (39 years reduced by 11.5 months or 0.958). Your depreciation for the building for the second year is \$2,564 ( $\$97,544 \times 0.02629$ ).

**Third year.** The adjusted basis is \$94,980 ( $\$97,544 - \$2,564$ ). The SL rate is 0.027 (1

divided by 37.042 remaining years). Your depreciation for the third year is \$2,564 ( $\$94,980 \times 0.027$ ).

***Example 3—200% DB method and mid-quarter convention.*** During the year, you bought and placed in service in your business the following items.

<b>Item</b>	<b>Month Placed in Service</b>	<b>Cost</b>
Safe	January	\$4,000
Office furniture	September	1,000
Computer	October	5,000

You do not elect a section 179 deduction and these items do not qualify for a special depreciation allowance. You use GDS and the



200% DB method to figure the depreciation. The total bases of all property you placed in service this year is \$10,000. The basis of the computer (\$5,000) is more than 40% of the total bases of all property placed in service during the year (\$10,000), so you must use the mid-quarter convention. This convention applies to all three items of property. The safe and office furniture are 7-year property and the computer is 5-year property.

***First and second-year depreciation for safe.*** The 200% DB rate for 7-year property is 0.28571. You determine this by dividing 2.00 (200%) by 7 years. The depreciation for the safe for a full year is \$1,143 ( $\$4,000 \times 0.28571$ ). You placed the safe in service in the first quarter of your tax year, so you multiply \$1,143 by 87.5% (the mid-quarter percentage for the first quarter). The result, \$1,000, is your deduction for depreciation on the safe for the first year.

For the second year, the adjusted basis of the safe is \$3,000. You figure this by subtracting the first year's depreciation (\$1,000) from the basis of the safe (\$4,000). Your depreciation deduction for the second year is \$857( $\$3,000 \times 0.28571$ ).

***First and second-year depreciation for furniture.*** The furniture is also 7-year property, so you use the same 200% DB rate of 0.28571. You multiply the basis of the furniture (\$1,000) by 0.28571 to get the depreciation of \$286 for the full year. You placed the furniture in service in the third quarter of your tax year, so you multiply \$286 by 37.5% (the mid-quarter percentage for the third quarter). The result, \$107, is your deduction for depreciation on the furniture for the first year.

For the second year, the adjusted basis of the furniture is \$893. You figure this by subtracting the first year's depreciation (\$107) from the basis of the furniture

(\$1,000). Your depreciation for the second year is \$255 ( $\$893 \times 0.28571$ ).

***First and second-year depreciation for computer.*** The 200% DB rate for 5-year property is 0.40. You determine this by dividing 2.00 (200%) by 5 years. The depreciation for the computer for a full year is \$2,000 ( $\$5,000 \times 0.40$ ). You placed the computer in service in the fourth quarter of your tax year, so you multiply the \$2,000 by 12.5% (the mid-quarter percentage for the fourth quarter). The result, \$250, is your deduction for depreciation on the computer for the first year.

For the second year, the adjusted basis of the computer is \$4,750. You figure this by subtracting the first year's depreciation (\$250) from the basis of the computer (\$5,000). Your depreciation deduction for the second year is \$1,900 ( $\$4,750 \times 0.40$ ).

***Example 4—200% DB method and half-year convention.*** Last year, in July, you

bought and placed in service in your business a new item of 7-year property. This was the only item of property you placed in service last year. The property cost \$39,000 and you elected a \$24,000 section 179 deduction. You also made an election under section 168(k)(7) not to deduct the special depreciation allowance for 7-year property placed in service last year. Your unadjusted basis for the property is \$15,000. Because you did not place any property in service in the last 3 months of your tax year, you used the half-year convention. You figured your deduction using the percentages in [Table A-1](#) for 7-year property. Last year, your depreciation was \$2,144 ( $\$15,000 \times 14.29\%$  (0.1429)).

In July of this year, your property was vandalized. You had a deductible casualty loss of \$3,000. You spent \$3,500 to put the property back in operational order. Your adjusted basis at the end of this year is

\$13,356. You figured this by first subtracting the first year's depreciation (\$2,144) and the casualty loss (\$3,000) from the unadjusted basis of \$15,000. To this amount (\$9,856), you then added the \$3,500 repair cost.

You cannot use the table percentages to figure your depreciation for this property for this year because of the adjustments to basis. You must figure the deduction yourself. You determine the DB rate by dividing 2.00 (200%) by 7 years. The result is 0.28571 or 28.571%. You multiply the adjusted basis of your property (\$13,356) by the DB rate of 0.28571 to get your depreciation deduction of \$3,816 for this year.

## **Figuring the Deduction for Property Acquired in a Nontaxable Exchange**

If your property has a carryover basis because you acquired it in a nontaxable transfer such as a like-kind exchange or involuntary conversion, you must generally

figure depreciation for the property as if the transfer had not occurred. However, see [Like-kind exchanges and involuntary conversions](#), earlier, in chapter 3 under [How Much Can You Deduct](#); and [Property Acquired in a Like-kind Exchange or Involuntary Conversion](#) next.

## **Property Acquired in a Like-kind Exchange or Involuntary Conversion**

You must generally depreciate the carryover basis of property acquired in a like-kind exchange or involuntary conversion over the remaining recovery period of the property exchanged or involuntarily converted. You also generally continue to use the same depreciation method and convention used for the exchanged or involuntarily converted property. This applies only to acquired property with the same or a shorter recovery period and the same or more accelerated depreciation method than the property exchanged or involuntarily converted. The excess basis (the part of the acquired

property's basis that exceeds its carryover basis), if any, of the acquired property is treated as newly placed in service property.

For acquired property that has a longer recovery period or less accelerated depreciation method than the exchanged or involuntarily converted property, you must generally depreciate the carryover basis of the acquired property as if it were placed in service in the same tax year as the exchanged or involuntarily converted property. You also generally continue to use the longer recovery period and less accelerated depreciation method of the acquired property.

If the MACRS property you acquired in the exchange or involuntary conversion is qualified property, discussed earlier in chapter 3 under [What Is Qualified Property](#), you can claim a special depreciation allowance on the carryover basis. Special rules apply to vehicles acquired in a trade-in. For

information on how to figure depreciation for a vehicle acquired in a trade-in that is subject to the passenger automobile limits, see [\*Deductions For Passenger Automobiles Acquired in a Trade-in\*](#) under [\*Do the Passenger Automobile Limits Apply?\*](#) in chapter 5.



*Like-kind exchanges completed after December 31, 2017, are generally limited to exchanges of real property not held primarily for sale.*

***Election out.*** Instead of using the above rules, you can elect, for depreciation purposes, to treat the adjusted basis of the exchanged or involuntarily converted property as if disposed of at the time of the exchange or involuntary conversion. Treat the carryover basis and excess basis, if any, for the acquired property as if placed in service the later of the date you acquired it or the time of the disposition of the exchanged or involuntarily converted property.



The depreciable basis of the new property is the adjusted basis of the exchanged or involuntarily converted property plus any additional amount you paid for it. The election, if made, applies to both the acquired property and the exchanged or involuntarily converted property. This election does not affect the amount of gain or loss recognized on the exchange or involuntary conversion.

***When to make the election.*** You must make the election on a timely filed return (including extensions) for the year of replacement. The election must be made separately by each person acquiring replacement property. In the case of a partnership, S corporation, or consolidated group, the election is made by the partnership, by the S corporation, or by the common parent of a consolidated group, respectively. Once made, the election may not be revoked without IRS consent.

For more information and special rules, see the Instructions for Form 4562.

## **Property Acquired in a Nontaxable Transfer**

You must depreciate MACRS property acquired by a corporation or partnership in certain nontaxable transfers over the property's remaining recovery period in the transferor's hands, as if the transfer had not occurred. You must continue to use the same depreciation method and convention as the transferor. You can depreciate the part of the property's basis that exceeds its carryover basis (the transferor's adjusted basis in the property) as newly purchased MACRS property.

The nontaxable transfers covered by this rule include the following.

- A distribution in complete liquidation of a subsidiary.

- A transfer to a corporation controlled by the transferor.
- An exchange of property solely for corporate stock or securities in a reorganization.
- A contribution of property to a partnership in exchange for a partnership interest.
- A partnership distribution of property to a partner.

## **Figuring the Deduction for a Short Tax Year**

You cannot use the MACRS percentage tables to determine depreciation for a short tax year. A short tax year is any tax year with less than 12 full months. This section discusses the rules for determining the depreciation deduction for property you place in service or dispose of in a short tax year. It also discusses the rules for determining depreciation when you have a short tax year

during the recovery period (other than the year the property is placed in service or disposed of).

For more information on figuring depreciation for a short tax year, see Revenue Procedure 89-15, 1989-1 C.B. 816.

### **Using the Applicable Convention in a Short Tax Year**

The applicable convention establishes the date property is treated as placed in service and disposed of. Depreciation is allowable only for that part of the tax year the property is treated as in service. The recovery period begins on the placed in service date determined by applying the convention. The remaining recovery period at the beginning of the next tax year is the full recovery period less the part for which depreciation was allowable in the first tax year.

The following discussions explain how to use the applicable convention in a short tax year.

**Mid-month convention.** Under the mid-month convention, you always treat your property as placed in service or disposed of on the midpoint of the month it is placed in service or disposed of. You apply this rule without regard to your tax year.

**Half-year convention.** Under the half-year convention, you treat property as placed in service or disposed of on the midpoint of the tax year it is placed in service or disposed of.

***First or last day of month.*** For a short tax year beginning on the first day of a month or ending on the last day of a month, the tax year consists of the number of months in the tax year. If the short tax year includes part of a month, you generally include the full month in the number of months in the tax year. You determine the midpoint of the tax year by dividing the number of months in the tax year by 2. For the half-year convention, you treat property as placed in service or disposed of

on either the first day or the midpoint of a month.

For example, a short tax year that begins on June 20 and ends on December 31 consists of 7 months. You use only full months for this determination, so you treat the tax year as beginning on June 1 instead of June 20. The midpoint of the tax year is the middle of September ( $3\frac{1}{2}$  months from the beginning of the tax year). You treat property as placed in service or disposed of on this midpoint.

**Example.** Tara Corporation, a calendar year taxpayer, was incorporated on March 15. For purposes of the half-year convention, it has a short tax year of 10 months, ending on December 31, 2023. During the short tax year, Tara placed property in service for which it uses the half-year convention. Tara treats this property as placed in service on the first day of the sixth month of the short tax year, or August 1, 2023.

***Not on first or last day of month.*** For a short tax year not beginning on the first day of a month and not ending on the last day of a month, the tax year consists of the number of days in the tax year. You determine the midpoint of the tax year by dividing the number of days in the tax year by 2. For the half-year convention, you treat property as placed in service or disposed of on either the first day or the midpoint of a month. If the result of dividing the number of days in the tax year by 2 is not the first day or the midpoint of a month, you treat the property as placed in service or disposed of on the nearest preceding first day or midpoint of a month.

**Mid-quarter convention.** To determine if you must use the mid-quarter convention, compare the basis of property you place in service in the last 3 months of your tax year to that of property you place in service during the full tax year. The length of your tax year

does not matter. If you have a short tax year of 3 months or less, use the mid-quarter convention for all applicable property you place in service during that tax year.

You treat property under the mid-quarter convention as placed in service or disposed of on the midpoint of the quarter of the tax year in which it is placed in service or disposed of. Divide a short tax year into 4 quarters and determine the midpoint of each quarter.

For a short tax year of 4 or 8 full calendar months, determine quarters on the basis of whole months. The midpoint of each quarter is either the first day or the midpoint of a month. Treat property as placed in service or disposed of on this midpoint.

To determine the midpoint of a quarter for a short tax year of other than 4 or 8 full calendar months, complete the following steps.



1. Determine the number of days in your short tax year.
2. Determine the number of days in each quarter by dividing the number of days in your short tax year by 4.
3. Determine the midpoint of each quarter by dividing the number of days in each quarter by 2.

If the result of (3) gives you a midpoint of a quarter that is on a day other than the first day or midpoint of a month, treat the property as placed in service or disposed of on the nearest preceding first day or midpoint of that month.

**Example.** Tara Corporation, a calendar year taxpayer, was incorporated and began business on March 15. It has a short tax year of 9 1/2 months, ending on December 31. During December, it placed property in service for which it must use the mid-quarter convention. This is a short tax year of other

than 4 or 8 full calendar months, so it must determine the midpoint of each quarter.

1. First, it determines that its short tax year beginning March 15 and ending December 31 consists of 292 days.
2. Next, it divides 292 by 4 to determine the length of each quarter, 73 days.
3. Finally, it divides 73 by 2 to determine the midpoint of each quarter, the 37th day.

The following table shows the quarters of Tara Corporation's short tax year, the midpoint of each quarter, and the date in each quarter that Tara must treat its property as placed in service.

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<b>Quarter</b>	<b>Midpoint</b>	<b>Placed in Service</b>
3/15 – 5/26	4/20	4/15

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5/27 – 8/07	7/02	7/01
8/08 – 10/19	9/13	9/01
10/20 – 12/31	11/25	11/15

The last quarter of the short tax year begins on October 20, which is 73 days from December 31, the end of the tax year. The 37th day of the last quarter is November 25, which is the midpoint of the quarter.

November 25 is not the first day or the midpoint of November, so Tara Corporation must treat the property as placed in service in the middle of November (the nearest preceding first day or midpoint of that month).

## **Property Placed in Service in a Short Tax Year**

To figure your MACRS depreciation deduction for the short tax year, you must first determine the depreciation for a full tax year.

You do this by multiplying your basis in the property by the applicable depreciation rate. Then, determine the depreciation for the short tax year. Do this by multiplying the depreciation for a full tax year by a fraction. The numerator (top number) of the fraction is the number of months (including parts of a month) the property is treated as in service during the tax year (applying the applicable convention). The denominator (bottom number) is 12. See [Depreciation After a Short Tax Year](#), later, for information on how to figure depreciation in later years.

***Example 1—half-year convention.*** Tara Corporation, with a short tax year beginning March 15 and ending December 31, placed in service on March 16 an item of 5-year property with a basis of \$1,000. This is the only property the corporation placed in service during the short tax year. Tara does not elect to claim a section 179 deduction and the property does not qualify for a special

depreciation allowance. The depreciation method for this property is the 200% declining balance method. The depreciation rate is 40% and Tara applies the half-year convention.

Tara treats the property as placed in service on August 1. The determination of this August 1 date is explained in the example illustrating the half-year convention under [Using the Applicable Convention in a Short Tax Year](#), earlier. Tara is allowed 5 months of depreciation for the short tax year that consists of 10 months. The corporation first multiplies the basis (\$1,000) by 40% (the declining balance rate) to get the depreciation for a full tax year of \$400. The corporation then multiplies \$400 by  $\frac{5}{12}$  to get the short tax year depreciation of \$167.

***Example 2—mid-quarter convention.*** Tara Corporation, with a short tax year beginning March 15 and ending December 31, placed in service on October 16 an item of 5-year

property with a basis of \$1,000. Tara does not elect to claim a section 179 deduction and the property does not qualify for a special depreciation allowance. The depreciation method for this property is the 200% declining balance method. The depreciation rate is 40%. The corporation must apply the mid-quarter convention because the property was the only item placed in service that year and it was placed in service in the last 3 months of the tax year.

Tara treats the property as placed in service on September 1. This date is shown in the table provided in the example illustrating the mid-quarter convention under [Using the Applicable Convention in a Short Tax Year](#), earlier, for property that Tara Corporation placed in service during the quarter that begins on August 8 and ends on October 19. Under MACRS, Tara is allowed 4 months of depreciation for the short tax year that consists of 10 months. The corporation first

multiplies the basis (\$1,000) by 40% to get the depreciation for a full tax year of \$400. The corporation then multiplies \$400 by  $\frac{4}{12}$  to get the short tax year depreciation of \$133.

## **Property Placed in Service Before a Short Tax Year**

If you have a short tax year after the tax year in which you began depreciating property, you must change the way you figure depreciation for that property. If you were using the percentage tables, you can no longer use them. You must figure depreciation for the short tax year and each later tax year as explained next.

## **Depreciation After a Short Tax Year**

You can use either of the following methods to figure the depreciation for years after a short tax year.

- The simplified method.
- The allocation method.

You must use the method you choose consistently.

**Using the simplified method for a 12-month year.** Under the simplified method, you figure the depreciation for a later 12-month year in the recovery period by multiplying the adjusted basis of your property at the beginning of the year by the applicable depreciation rate.

**Example.** Assume the same facts as in *Example 1* under [Property Placed in Service in a Short Tax Year](#), earlier. The Tara Corporation claimed depreciation of \$167 for its short tax year. The adjusted basis on January 1 of the next year is \$833 (\$1,000 – \$167). Tara's depreciation for that next year is 40% of \$833, or \$333.

**Using the simplified method for a short tax year.** If a later tax year in the recovery period is a short tax year, you figure depreciation for that year by multiplying the



adjusted basis of the property at the beginning of the tax year by the applicable depreciation rate, and then by a fraction. The fraction's numerator is the number of months (including parts of a month) in the tax year. Its denominator is 12.

**Using the simplified method for an early disposition.** If you dispose of property in a later tax year before the end of the recovery period, determine the depreciation for the year of disposition by multiplying the adjusted basis of the property at the beginning of the tax year by the applicable depreciation rate and then multiplying the result by a fraction. The fraction's numerator is the number of months (including parts of a month) the property is treated as in service during the tax year (applying the applicable convention). Its denominator is 12.

**Using the allocation method for a 12-month or short tax year.** Under the allocation method, you figure the depreciation

for each later tax year by allocating to that year the depreciation attributable to the parts of the recovery years that fall within that year. Whether your tax year is a 12-month or short tax year, you figure the depreciation by determining which recovery years are included in that year. For each recovery year included, multiply the depreciation attributable to that recovery year by a fraction. The fraction's numerator is the number of months (including parts of a month) that are included in both the tax year and the recovery year. Its denominator is 12. The allowable depreciation for the tax year is the sum of the depreciation figured for each recovery year.

**Example.** Assume the same facts as in *Example 1* under [Property Placed in Service in a Short Tax Year](#), earlier. The Tara Corporation's first tax year after the short tax year is a full year of 12 months, beginning January 1 and ending December 31. The first

recovery year for the 5-year property placed in service during the short tax year extends from August 1 to July 31. Tara deducted 5 months of the first recovery year on its short-year tax return. Seven months of the first recovery year and 5 months of the second recovery year fall within the next tax year. The depreciation for the next tax year is \$333, which is the sum of the following.

- \$233—The depreciation for the first recovery year ( $\$400 \times 7/12$ ).
- \$100—The depreciation for the second recovery year. This is figured by multiplying the adjusted basis of \$600 ( $\$1,000 - \$400$ ) by 40% (0.40), then multiplying the \$240 result by 5/12.

**Using the allocation method for an early disposition.** If you dispose of property before the end of the recovery period in a later tax year, determine the depreciation for the year of disposition by multiplying the depreciation figured for each recovery year (or part of a

recovery year) included in the tax year by a fraction. The numerator of the fraction is the number of months (including parts of months) the property is treated as in service in the tax year (applying the applicable convention). The denominator is 12. If there is more than one recovery year in the tax year, you add together the depreciation for each recovery year.

## **How Do You Use General Asset Accounts?**

### **Terms you may need to know (see Glossary):**

Adjusted basis

Amortization

Amount realized

Basis

Convention

Disposition  
Exchange  
Placed in service  
Recovery period  
Section 1245 property  
Unadjusted basis

To make it easier to figure MACRS depreciation, you can group separate properties into one or more general asset accounts (GAAs). You can then depreciate all the properties in each account as a single item of property.

**Property you cannot include.** You cannot include property in a GAA if you use it in both a personal activity and a trade or business (or for the production of income) in the year in which you first place it in service. If property you included in a GAA is later used in a personal activity, see [Terminating GAA Treatment](#), later.

## **Property generating foreign source**

**income.** For information on the GAA treatment of property that generates foreign source income, see sections 1.168(i)-1(c)(1)(ii) and (f) of the regulations.

**Change in use.** Special rules apply to figuring depreciation for property in a GAA for which the use changes during the tax year.

Examples include a change in use resulting in a shorter recovery period and/or a more accelerated depreciation method or a change in use resulting in a longer recovery period and/or a less accelerated depreciation method. See sections 1.168(i)-1(h) and 1.168(i)-4 of the regulations.

## **Grouping Property**

Each GAA must include only property you placed in service in the same tax year and that has the following in common.

- Recovery period.

- Depreciation method.
- Convention.

The following rules also apply when you establish a GAA.

- ***Mid-quarter convention.*** Property subject to the mid-quarter convention can only be grouped into a GAA with property placed in service in the same quarter of the tax year.
- ***Mid-month convention.*** Property subject to the mid-month convention can only be grouped into a GAA with property placed in service in the same month of the tax year.
- ***Passenger automobiles.*** Passenger automobiles subject to the limits on passenger automobile depreciation must be grouped into a separate GAA.

See section 1.168(i)-1(c)(2)(ii) of the regulations for additional rules that apply when you establish a GAA.

## **Figuring Depreciation for a GAA**

After you have set up a GAA, you generally figure the MACRS depreciation for it by using the applicable depreciation method, recovery period, and convention for the property in the GAA. For each GAA, record the depreciation allowance in a separate depreciation reserve account.

**Example.** Make & Sell, a calendar year corporation, set up a GAA for 10 machines. The machines cost a total of \$10,000 and were placed in service in June 2023. One of the machines cost \$8,200 and the rest cost a total of \$1,800. This GAA is depreciated under the 200% declining balance method with a 5-year recovery period and a half-year convention. Make & Sell did not claim the section 179 deduction on the machines and



the machines did not qualify for a special depreciation allowance. The depreciation allowance for 2023 is \$2,000  $[(\$10,000 \times 40\% (0.40)) \div 2]$ . As of January 1, 2024, the depreciation reserve account is \$2,000.

**Passenger automobiles.** To figure depreciation on passenger automobiles in a GAA, apply the deduction limits discussed in chapter 5 under [\*Do the Passenger Automobile Limits Apply\*](#). Multiply the amount determined using these limits by the number of automobiles originally included in the account, reduced by the total number of automobiles removed from the GAA, as discussed under [\*Terminating GAA Treatment\*](#), later.

## **Disposing of GAA Property**

When you dispose of property included in a GAA, the following rules generally apply.

- Neither the unadjusted depreciable basis (defined later) nor the depreciation

reserve account of the GAA is affected. You continue to depreciate the account as if the disposition had not occurred.

- The property is treated as having an adjusted basis of zero, so you cannot realize a loss on the disposition. If the property is transferred to a supplies, scrap, or similar account, its basis in that account is zero.
- Any amount realized on the disposition is treated as ordinary income, up to the limit discussed later under [Treatment of amount realized](#).

However, these rules do not apply to any disposition described later under [Terminating GAA Treatment](#).

**Disposition.** Property in a GAA is considered disposed of when you do any of the following.

- Permanently withdraw it from use in your trade or business or from the production of income.
- Transfer it to a supplies, scrap, or similar account.
- Sell, exchange, retire, physically abandon, or destroy it.

The retirement of a structural component of real property is not a disposition unless it is a partial disposition. See section 1.168(i)-1(e)(1) of the regulations.

**Treatment of amount realized.** When you dispose of property in a GAA, you must recognize any amount realized from the disposition as ordinary income, up to a limit. The limit is:

- 1.** The unadjusted depreciable basis of the GAA, **plus**
- 2.** Any expensed costs for property in the GAA that are subject to recapture as

depreciation (not including any expensed costs for property that you removed from the GAA under the rules discussed later under [Terminating GAA Treatment](#)), **minus**

3. Any amount previously recognized as ordinary income upon the disposition of other property from the GAA.

***Unadjusted depreciable basis.*** The unadjusted depreciable basis of a GAA is the total of the unadjusted depreciable bases of all the property in the GAA. The unadjusted depreciable basis of an item of property in a GAA is the amount you would use to figure gain or loss on its sale, but figured without reducing your original basis by any depreciation allowed or allowable in earlier years. However, you do reduce your original basis by other amounts, including any amortization deduction, section 179 deduction, special depreciation allowance, and electric vehicle credit.