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Qualifying for the Expanded \$250,000 Expensing Election

The 2008 stimulus package provides for an immediate deduction of up to \$250,000 for qualified small business taxpayers. The small business taxpayer is one who invests less than \$1,050,000 in total capital purchases during the taxable year.

The expensing election applies to both new and used property, including airplanes and improvements to airplanes. There are three principal qualification requirements.

Investment Threshold. The small business taxpayer is classified as such in the statute based on the level of their capital purchases throughout the year. If the taxpayer invests less than \$800,000, he is entitled to expense the first \$250,000, and then calculate depreciation on the balance. For taxpayers who invest more than \$800,000 during the taxable year, the expensing is phased out on a dollar per dollar basis resulting in complete elimination when the total capital investment exceeds \$1,050,000 per year. The expensing deduction is calculated before depreciation with the non-expensed portion subject to normal depreciation rules.

Taxable Income Limitation. The maximum amount that may be expensed is further limited to the amount of taxable income from any of the taxpayer's active trades or businesses. Taxable income for this purpose is calculated before the expensing deduction itself, net operating loss carrybacks or carry-forwards, and other losses suspended due to basis limitations or passive activity classifications. Any amount suspended under the taxable income limitation is carried over indefinitely. It is important to note that the taxable income limitation is calculated on the taxpayer's combined trade or business income; it is not calculated on a per trade or business basis. Finally, wages paid to a taxpayer constitute trade or business income for the purpose of this calculation.

Asset Qualification. In order to qualify for the expensing election, the asset must constitute property eligible for MACRS depreciation. MACRS depreciation is not available to assets used less than 50% for business and certain leased assets.

Planning Opportunities. The taxable income limitation often limits the opportunity to use stand-alone limited liability companies to hold aircraft interest. Although the limited liability company organization may still be an appropriate vehicle for certain acquisitions, it will generally be necessary to avoid a partnership classification. If the stand-alone limited liability company is a partnership, the taxable income

limitation will be imposed at the partnership level, and the expensing deduction will generally not be available to its owners. It may be possible to avail a limited liability company structure for FAA and sales tax purposes and have it treated as an entity other than a partnership for income tax purposes.

It is also necessary for 50% of the use of the aircraft be for qualified business use. Qualified business use generally excludes related party leasing. With proper planning, it is generally possible to use related party leasing for sales tax purposes, thereby avoiding tax on purchase and having it disregarded for income tax purposes.

AND DON'T FORGET THE BASIS ISSUES

One significant advantage of using a partnership limited liability company over an S corporation is the difference in income tax basis for borrowed funds. An LLC owner's basis includes entity level debt; an S corporation shareholder does not. This problem could be particularly acute when an expensing election generates a deduction significantly in excess of the taxpayer's equity.

The opportunity to expense \$250,000 of the capital purchase is significant. However, qualifying for the expensing election requires extreme care to protect the owner from violating FAA rules, inadvertently subjecting the aircraft to a needless acceleration of sales tax, or failing the taxable income limitation.

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