Quickfinder®

Depreciation
Quickfinder® Handbook
(2022 Tax Year)

Updates for December 2022 Legislation and Other Recent Guidance

Instructions: This packet contains “marked up” changes to the pages in the *Depreciation Quickfinder® Handbook* that were affected by December 2022 legislation, which was enacted after the *Handbook* was published. Additionally, changes were made based on other guidance issued after the Handbook was published. To update your *Handbook*, you can make the same changes in your *Handbook* or print the revised page and paste over the original page.

Plug-In Electric Drive Motor Vehicle Credit

Taxpayers can claim a credit for each new qualifying vehicle purchased for use or for lease, but not for resale. The credit amount ranges from $2,500 to $7,500. The portion of the credit attributable to the vehicle's business-use percentage is treated as part of the taxpayer's general business credit. The remainder is a nonrefundable personal credit that can offset both regular tax and AMT (IRC Sec. 30D).

Qualifying vehicles. These are new four-wheeled plug-in electric vehicles manufactured primarily for use on public streets, roads, and highways that meet certain technical requirements and the original use of the vehicle began with the taxpayer.

However, the following do not qualify:

1) Vehicles manufactured primarily for off-road use (such as golf carts).
2) Vehicles weighing 14,000 pounds or more.
3) Low-speed vehicles.

Manufacturer's certification. The IRS will acknowledge a manufacturer's (or in the case of a foreign vehicle manufacturer, its domestic distributor's) certification that a vehicle meets the standards to qualify for the credit. Taxpayers may rely on such a certification (Notice 2009-89).

Phase-out based on vehicle sales. The credit begins to phase out for a manufacturer's vehicles when at least 200,000 qualifying vehicles manufactured by that manufacturer have been sold for use in the U.S. (determined cumulatively for sales after 2009). For General Motors, LLC and Tesla, Inc. the phaseout period began in 2019. For Toyota Motor North America, Inc. vehicles, the phase-out begins October 1, 2022. For the latest information on the phase out amounts, see the IRS website at **www.irs.gov/businesses/irc-30d-new-qualified-plug-in-electric-drive-motor-vehicle-credit**.

Note: A vehicle is considered acquired on the date when title to that vehicle passes under state law (Notice 2009-89).

Law Change Alert: To qualify for the credit, the Inflation Reduction Act of 2022 requires that final assembly of qualifying electric vehicles sold after August 16, 2022 occurs in North America. If a taxpayer purchased (or entered into a written binding contract to purchase) an otherwise-qualifying vehicle after 2021 and before August 16, 2022, but didn't place the vehicle into service until on or after August 16, 2022, the taxpayer may elect to treat the vehicle as placed in service on August 15, 2022 and not be subject to the final assembly requirement. See *New Clean Vehicle Credit* on Page 6-11.

Reporting

The credit for plug-in electric drive motor vehicles is claimed on Form 8936. The portion of the credit attributable to business/investment use of the vehicle is part of the general business credit. The remainder is a personal nonrefundable credit that can offset regular tax and AMT. It is reported on Form 1040, Schedule 3, line 6f. Any part of the personal-use portion of the credit that cannot be used is lost. It cannot be carried over to other years.

Line 4b of Form 8936 is used for GM, Tesla, and Toyota vehicles that are subject to the credit phaseout.

New Clean Vehicle Credit

The Inflation Reduction Act of 2022 (the Act) made several changes to the qualified plug-in electric drive motor vehicle credit (IRC Sec. 30D), mostly for vehicles placed in service after 2022. However, see the Law Change Alert under *Plug-In Electric Drive Motor Vehicle Credit* on Page 6-11 for one change that applies to vehicles purchased after August 16, 2022. The Act also made credits available for some vehicles that didn't qualify in the past.

New final assembly requirement. Vehicles sold after August 16, 2022 only qualify for this credit if their final assembly occurs in North America.

Note: For a list of vehicles whose final assembly occurs in North America and that should qualify for the credit if purchased after August 16, 2022 and before 2023 see the table *Electric Vehicles Assembled in North America* on Page 6-15.

Transition rule. The final assembly requirement does not apply to a vehicle purchased under a *written binding contract* entered into before August 16, 2022, when the taxpayer does not take possession of it until on or after August 16, 2022 (for example, because the vehicle was not delivered immediately). The taxpayer can claim the credit based on the rules in effect before the Act.

Generally, a written contract is binding if it is enforceable under state law and doesn't limit damages to a specified amount (for example, under a liquidated damages provision or the forfeiture of a deposit). Making a significant (at least 5% of the total purchase price) nonrefundable deposit or down payment is an indication of a binding contract. A contract is binding even if subject to a condition, as long as the condition is not within either party's control and continues to be binding if the parties make insubstantial changes to its terms and conditions.

Vehicles purchased and delivered from August 17, 2022 through December 31, 2022. For a taxpayer that buys and takes possession of a qualifying vehicle after August 16, 2022 and before 2023, in addition to the final assembly requirement, the rules in effect before the enactment of the Act apply (including those involving the manufacturing caps on vehicles sold). This means that the limits on the credit due to the vehicle's price or for individuals the taxpayer's modified AGI, discussed later, don't come into play. Also see *Manufacturer's limit eliminated* on Page 6-12).

Vehicles that qualify for the credit after 2022. In addition to the final assembly requirement, vehicles placed in service after 2022 must have a minimum battery capacity of seven kilowatt hours (up from a four-hour minimum under the previous rules). Also, the credit will be based on meeting one or both of two new requirements. Vehicles that meet a *critical minerals* requirement will be eligible for a $3,750 credit. Vehicles that meet a *battery component* requirement also qualify for a $3,750 credit. Vehicles that meet both requirements will qualify for a $7,500 credit. These requirements are designed to ensure that the vehicles meet certain standards regarding the minerals used in their batteries and that a certain percentage of the vehicle's battery is manufactured or assembled in North America. Under the Act, the IRS must issue proposed guidance on the critical minerals and battery component requirements~~ by December 31, 2022~~. This change in the credit calculation will apply to vehicles placed in service after the date the IRS issues that guidance. The IRS announced that it will release proposed regulations on the credit (expected in March 2023) and has released guidance to clarify definitions related to vehicles that may qualify for the credit. See Notice 2023-1 for these definitions. Also, FAQs were released in December 2022 in Fact Sheet 2022-42 at **www.irs.gov/newsroom/fact-sheets**. For a list of vehicles that may qualify for the credit in 2023, see **www.irs.gov/credits-deductions/manufacturers-and-models-for-new-qualified-clean-vehicles-purchased-in-2023-or-after**.

Note: Many of the electric vehicles available in 2022 won't meet these new standards. So, until more manufacturers begin producing vehicles that qualify for the Clean Vehicle credit, there may not be a lot of qualifying vehicles on the market, at least in the short term.

New documentation requirement. The Clean Vehicle credit will only be available for vehicles placed in service after 2022 if the seller furnishes a report to the IRS and to the buyer that contains the:

1) buyer's name and taxpayer identification number,
2) Vehicle Identification Number (VIN), unless the vehicle is not assigned a VIN,

Continued on the next page

Research and Experimental Expenditures

What Costs Are Included?

Research and experimental (R&E) expenditures are costs incurred in a trade or business for activities intended to provide information that would eliminate uncertainty about the development or improvement of a product (Reg. 1.174-2). For this purpose, a product includes any formula, invention, patent, pilot model, process, technique or similar property. The term *product* also includes products used in the taxpayer's trade or business or held for sale, lease or license. Uncertainty exists if the information available does not establish how to develop or improve a product or the appropriate design of a product.

Caution: Although the costs of obtaining a patent, including attorneys' fees paid or incurred in making and perfecting a patent application, are R&E costs, any costs to obtain someone else's patent are not.

Costs not included. R&E costs do not include expenses for any of the following activities:

- Advertising or promotions.
- Consumer surveys.
- Efficiency surveys.
- Management studies.
- Quality control testing.
- Research in connection with literary, historical or similar projects.
- The acquisition of another's patent, model, production or process.

Deducting the costs. Research and experimental costs are deducted in one of the following ways:

1) Deduct as a current business expense (but see *Specified R&E expenditures* on Page 11-10 for required capitalization and amortization beginning in 2022).
2) Elect to amortize over 60 months.
3) 10-year optional write-off.

Making the elections. To elect the optional write-off method or amortization of research costs, fill out Part VI of Form 4562 and attach to either a timely filed return (including extensions) or an amended return within six months of the original due date of the return (excluding extensions). If electing the optional write-off method, a statement must also be included with the taxpayer's name and address, taxpayer number, and the type of research cost and specific amount of the research cost for the election.

Claiming the Incremental Research Credit

Taxpayers may elect to claim a research credit (RC) for R&E costs rather than expensing them. Not all costs that are R&E costs will qualify for the RC. See *Qualified research expenditures* on Page 11-9. Eligible small businesses ($50 million or less in gross receipts) may claim the credit against alternative minimum tax (AMT) [IRC Sec. 38(c)] and the credit can be utilized by certain (qualified) small businesses against employer payroll tax liability. [For a definition of *qualified small businesses*, see IRC Sec. 41(h). For information on claiming the credit against employer payroll tax liability, see IRC Sec. 3111(f).]

Caution: If a taxpayer elects to claim the RC for certain costs, those same costs cannot be expensed or capitalized and amortized. In other words, taxpayers cannot get a double tax benefit from the same costs.

Qualified research expenditures. The RC can be claimed for qualified research expenditures (QREs) conducted as part of a taxpayer's trade or business. QREs are the sum of in-house research expenses and contract research expenses [IRC Sec. 41(b)(1) and Reg. 1.41-4].

In-house research expenses are:

1) Wages paid to an employee engaged in qualified research or in the direct supervision of qualified research.
2) Amounts paid for supplies used to conduct qualified research.
3) Amounts paid for the use of computers to conduct qualified research.

Contract research expenses are 65% of amounts paid to persons other than employees for qualified research. The limit is increased to 75% for payments made to a *qualified research consortium*, which is an organization that has the following characteristics:

1) It is a Section 501(c)(3) or 501(c)(6) organization and is exempt from tax under IRC Sec. 501(a).
2) It is organized and operated primarily to conduct scientific research.
3) It is not a private foundation.

Payments made to a qualified research consortium are made on behalf of the taxpayer and one or more unrelated taxpayers.

Qualified research must meet the following tests [IRC Sec. 41(d)]:

1) The expenditures must be expenses described at *What Costs Are Included?* on Page 11-9.
2) The research must be of a technological nature (for example, it must be related to the physical, biological, engineering, or computer sciences).
3) Substantially all of the research must be related to a new or improved function, performance, reliability, or quality.
4) The application of the research is intended to be useful in the development of a new or improved business component of the taxpayer.

Expenses related to efficiency surveys, management studies, market research, routine data collection and quality control testing do not qualify for the RC.

Note: To provide an efficient approach to determine the correct amount of QREs the IRS issued a directive to Large Business and International (LB&I) examiners to accept as sufficient evidence the Adjusted ASC 730 Financial Statement R&D amount as the amount of QREs used to compute the RC. This directive applies to original

Deducting Research and Experimental Expenditures

Method	Description	Pros and Cons
Current Business Expense [IRC Sec. 174(a)]	Research and experimental costs that are ordinary and necessary business expenses can be deducted in the current year as *Other Business Expenses*. The taxpayer must adopt this method in the first year that such expenditures are paid or incurred. Occasionally, the taxpayer may adopt this method in a later year with IRS consent.	• *Advantages:* Immediate deduction and simplicity. • *Disadvantage:* Amounts expensed by individuals are subject to 10-year amortization for AMT, unless taxpayer materially participates in the activity [IRC Sec. 56(b)(2)].
Elect to Amortize [IRC Sec. 174(b)]	Amortization period begins with the month an economic benefit from the expenditures is first received. Costs are amortized ratably over a period of 60 months or more. This is a one-time election that applies to all expenditures in the year of election and all subsequent years and can be revoked only with IRS consent.	• *Advantages:* No AMT adjustment. Sixty-month amortization allows faster recovery than 10-year write off. • *Disadvantages:* Amortization does not begin until economic benefit realized. Once election is made, it applies to all later years, unless permission to revoke obtained from IRS.
Optional Write-Off Method [IRC Sec. 59(e)]	Research and experimental costs are deducted, if elected, ratably over a 10-year period beginning with the tax year the costs are incurred. The election applies only to current-year expenditures and is not binding in future years.	• *Advantages:* No AMT adjustment required for costs written off over 10 years. This is also a flexible method. Taxpayer can choose each year the amount of costs that will be written off over 10 years (allowing taxpayer to reduce or avoid AMT). • *Disadvantage:* May provide for longer write-off in many cases.

returns timely filed (including extensions) after September 11, 2017 and to taxpayers that:
1) Have assets of $10 million or more.
2) Have U.S. GAAP-based certified audited financial statements.
3) Comply with certain certification requirements provided in the directive.

For more information, search **www.irs.gov** for "News Release and Fact Sheet Archive", then access IR-2017-158 in the 2017, September section.

Computing the credit. The RC equals the sum of [IRC Sec. 41(a)]:
1) 20% of the QREs for the current tax year exceeding the base amount for that year, plus
2) 20% of the basic research payments over the qualified organization base period amount, plus
3) 20% of amounts paid to an energy research consortium.

The *base amount* equals the fixed base percentage [as defined in IRC Sec. 41(c)(3)] multiplied by the average annual gross receipts of the taxpayer for the four tax years preceding the tax year for which the credit is being determined [IRC Sec. 41(c)]. However, the base amount cannot be less than 50% of its QREs for the year. This means no more than half of the current year's QREs can qualify for the RC.

Basic research payments are cash payments made to qualified organizations such as educational institutions and certain scientific research organizations if the basic research is to be performed by the organization. Cash payments to scientific tax-exempt organizations and certain grant organizations also qualify, but these organizations do not have to perform the research directly.

Alternative Simplified Credit (ASC). Taxpayers may elect to take the Section 41(c)(4) Alternative Simplified Credit (ASC). This is equal to 14% (12% before 2009) of the excess of the qualified research expenses for the tax year over 50% of the average qualified research expenses for the three preceding tax years. A taxpayer may make an ASC election on an amended return (Reg. 1.41-9). A taxpayer who is a member of a controlled group in a tax year may not make an election under IRC Sec. 41(c)(4) for that tax year on an amended return if any member of the controlled group for that year claimed the credit using a method other than the ASC.

Reduction of expenses. Any deductions for R&E claimed under IRC Sec. 174 must be reduced by the amount of the RC [IRC Sec. 280C(c)(1)]. For capitalized research expenditures, the amount chargeable to a capital account is reduced by the excess of the RC over the amount of QREs allowable as a deduction for the year. The taxpayer may avoid these reductions by electing a reduced credit. Under the election, the credit is reduced by an amount equal to the top corporate income tax rate multiplied by the full credit.

Reporting requirements. Form 6765, *Credit for Increasing Research Activities*, is filed to claim the RC. The taxpayer may elect to reduce the credit by completing the appropriate lines on Form 6765. If the taxpayer does not elect a reduced credit, a statement must be attached to Form 6765 showing the QREs reduced by the research credit.

Controlled groups. The credit is allocated to a member of a controlled group on a proportionate basis consistent with its share of total QREs and other factors [IRC Sec. 41(f)(1)(A) and Reg. 1.41-6].

Specified R&E expenditures. The TCJA requires capitalization and amortization (over 60 months beginning at the midpoint of the year) for specified R&E expenditures, which are R&E costs paid or incurred, in tax years beginning after 2021, by the taxpayer in connection with the taxpayer's trade or business. Presumably specified R&E expenditures are defined the same as pre-TCJA by Reg. 1.174-2. Practitioners should watch for IRS guidance on this matter. R&E expenditures attributable to foreign research will be amortized over a 180-month period beginning at the midpoint of the year.

Specified R&E expenditures do not include costs incurred for:
- Land.
- Depreciable or depletable property (but they do include the depreciation or depletion allowed on such property).
- Exploration of mineral (including oil and gas) or ore deposits.

Note: Research and experimental property disposed of, retired or abandoned during its amortization period is not allowed immediate expensing of the unamortized balance. Instead amortization continues over the remaining amortization period.

Change in accounting method. Applying this new rule is a change in accounting method treated as initiated by the taxpayer, made with IRS's consent and applied on a cut-off basis. Therefore, there is no IRC Sec. 481(a) adjustment. See Rev. Proc. 2023-11 and *Requesting an Accounting Method Change* on Page 10-2.

Income Forecast Method

The income forecast method uses an estimate of income to recover the cost of certain assets. Under this method, each year's deduction is equal to:

$$(\text{Cost} - \text{Salvage Value}) \times \frac{\text{Current Year Net Income From Property}}{\text{Estimated Total Income From Property}}$$

The denominator is the total income anticipated from the property through the end of the 10th tax year following the tax year the property is placed in service [IRC Sec. 167(g)].

Look-back calculation. Taxpayers who use the income forecast method for property with a cost of more than $100,000 are subject to a look-back calculation that may result in the receipt or payment of interest if actual income differs from anticipated income. Any interest computed under the look-back method is reported on Form 8866, *Interest Computation Under the Look-Back Method for Property Depreciated Under the Income Forecast Method.*

Eligible assets. The following intangibles can be amortized under either the straight-line method or the income forecast method:
1) Motion picture films or video tapes.
2) Sound recordings.
3) Copyrights.
4) Books.
5) Patents.
6) Other property to be specified in regulations.

Caution: The income forecast method cannot be used for Section 197 intangibles. Thus, to the extent any of the intangibles listed above is a Section 197 intangible (because it was acquired in connection with acquiring assets making up a trade or business), it cannot be amortized under the income forecast method.

Example: Easygoing Inc. produces a new record for a cost of $250,000. Salvage value of the recording at the end of 10 years is expected to be $10,000. Expected net income for the first 11 years of sales is $500,000. The record generates $150,000 of net income in the first year of sales.

Current year amortization is $72,000 [($250,000 – $10,000) × $150,000 ÷ $500,000].

Participations and Residuals

Participations and residuals are costs that, by contract, vary with the amount of income earned in connection with the property. The participations and residuals that relate to income to be derived from the property before the end of the tenth tax year after the property is placed in service are eligible for two optional tax treatments [IRC Sec. 167(g)(7)]:
- The participations and residuals can be included in the property's adjusted basis for calculating the amortization deduction for the year.
- The participations and residuals can be deducted in the tax year they are paid.

Reporting Income Forecast Method Deductions

Expense for assets depreciated under the income forecast method is reported on Form 4562, line 16, *Other depreciation (including ACRS)*.

— End of Tab 11 —

What's New and Glossary

Tab 13 Topics

Recent Tax Legislation

The Inflation Reduction Act of 2022 was signed into law on August 16, 2022. The Act includes new taxes on corporations, and many new credits, among other things. See the table *Inflation Reduction Act of 2022* on Page 13-2 for changes impacting this *Handbook*.

Certain tax provisions impacting this *Handbook* expired on December 31, 2021. See *Tax Provisions That Expired on December 31, 2021* below. Tax professionals should watch for possible extender legislation and check for updates to this *Handbook*. See *Quickfinder Updates* in the next column.

Quickfinder Updates. See the *Handbook Updates* section of the Quickfinder website (**tax.thomsonreuters.com/quickfinder**) for potential late-breaking developments impacting 2022 tax returns.

Tax Legislation History

The following table identifies selected tax legislation enacted beginning in 2015 that may impact 2022 and later tax returns.

Name of Act	Public Law Number	Date of Enactment
Protecting Americans From Tax Hikes Act of 2015 (PATH Act)	PL 114-113	12/18/15
Disaster Tax Relief and Airport and Airway Extension Act of 2017	PL 115-63	9/29/17
Tax Cuts and Jobs Act (TCJA)	PL 115-97	12/22/17
Bipartisan Budget Act of 2018 (BBA)	PL 115-123	2/9/18
Consolidated Appropriations Act, 2018	PL 115-141	3/23/18
Consolidated Appropriations Act, 2020	PL 116-93	12/20/19
Further Consolidated Appropriations Act, 2020	PL 116-94	12/20/19
Coronavirus Aid, Relief, and Economic Security (CARES) Act	PL 116-136	3/27/20
Consolidated Appropriations Act, 2021	PL 116-260	12/27/20
American Rescue Plan Act of 2021	PL 117-2	3/11/21
Inflation Reduction Act of 2022	PL 117-169	8/16/22
Consolidated Appropriations Act, 2023	PL 117-328	12/29/22

Tax Provisions That Expired on December 31, 2021

Not Available in 2022 (Unless Extended By Legislation)

Note. This table summarizes significant tax provisions impacting this *Handbook* that expired on December 31, 2021. It's possible that Congress will extend some or all of them to 2022, but it had not done so at the date of this publication. Tax professionals should watch for developments.

Item	*IRC Sec.*	*Handbook Pages*	*Provision in Effect for 2022*	*Provision in Effect for 2021*
Alternative Motor Vehicle Credit	30B	6-10	Credit expired for vehicles purchased after 12/31/21. However, taxpayers who purchased the vehicle in 2021, but placed it in service during 2022, may still be able to claim the credit for 2022. See *Inflation Reduction Act of 2022* on Page 13-2 for information on the new Clean Vehicle Credit for which fuel cell motor vehicles placed in service after 2022 may qualify.	The credit for vehicles propelled by chemically combining oxygen with hydrogen and creating electricity ("fuel cell motor vehicles") was available.
Two-Wheeled Plug-In Electric Vehicles Credit	30D	6-15	Credit expired for vehicles acquired after 12/31/21. However, taxpayers who acquired the vehicle in 2021, but placed it in service during 2022, may still be able to claim the credit for 2022.	The credit for electric motorcycles acquired in 2021 was available.
Racehorses—3-Year Property	168(e)(3)	1-20, 2-3, 2-4, 2-11, 4-3	No provision. Shorter recovery period expired for such property placed in service after 2021.	A racehorse, regardless of age when placed in service, was treated as three-year property.
Qualified Indian Reservation Property	168(j)(9)	2-5, 4-2, 4-3, 4-8, 4-10, 4-12, 4-14, 4-16, 4-31, 4-32	Accelerated cost recovery expired for such property placed in service after 2021.	Accelerated cost recovery was available for qualified Indian reservation property placed in service during 2021.