

# [Aircraft depreciation and taxation](https://assignbuster.com/aircraft-depreciation-and-taxation/)

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The total costs of owning and operating an aircraft are generally divided into four separate categories: cost of acquisition plus capital costs; direct costs of operation, e. g. fuel, repairs and maintenance costs; indirect costs of operation, e. g. insurance, crew salaries as well as benefits, and training costs; and other miscellaneous expenses, e. g. interest and aircraft depreciation.  Depreciation is a deductible expense for taxation purposes.

A company owning an aircraft may depreciate it over a period of five years under accelerated depreciation.  MACRS is the most commonly used method for aircraft depreciation, “ with half-year convention and 5 year recovery (Norris, 2006).”  If, for example, an entity’s federal tax rate is thirty-five percent, aircraft depreciation would allow it to recover thirty-five percent of the original cost of the aircraft through tax reductions during the next five years (Norris).

Aircraft owners can lower their tax burdens by deducting aircraft depreciation as an expense.  However, the Internal Revenue Service only allows aircraft owners to deduct depreciation on their tax forms if their aircrafts are used in business.  In other words, only those aircrafts that are used for business purposes – either in part or in whole – are recognized by the IRS when it is time to deduct expenses on the aircraft owner’s tax forms.

Moreover, small businesses may not be recognized as genuine, existent entities during this process.  It is only the large companies that may easily adopt MACRS to deduct aircraft depreciation on their tax forms (Swirsky & Peabody, 2001).  Swirsky & Peabody describe the various conditions that aircraft owners must be aware of while trying to deduct aircraft depreciation from their tax burdens:

The IRS lists nine factors that it uses to determine the validity of a claimed profit motive:

(1) the manner in which the activity is carried on; (2) the expertise of the taxpayer or his

advisors; (3) the time and effort expended by the taxpayer in carrying on the activity; (4)

expectation that the aircraft or other assets may appreciate in value; (5) the success of the taxpayer in carrying on similar or dissimilar activities; (6) the taxpayer's history of income or loss with respect to the activity; (7) the amount of occasional profits, if any; (8) the financial status of the taxpayer; and (9) elements of personal pleasure or recreation.  None of the foregoing factors is determinative, and the ultimate decision is a “ facts and circumstances” analysis (Swirsky & Peabody).

Even if an aircraft owner meets the above mentioned conditions to qualify for tax deduction for aircraft depreciation, there is a statutory assumption that if an entity’s gross income does not exceed its expenses for three years out of a five year period, it was not established for profit making.  Of course, changing circumstances are taken into account.

But, even if an entity shows the courts that it has made the necessary investments to eventually make a profit, tax deduction in the form of aircraft depreciation is possible to obtain (Swirsky & Peabody).  Regardless of whether an aircraft owner manages to convince the courts that it is a profit making entity – the fact remains that the taxation laws concerning aircraft depreciation were designed to encourage aircraft owners to use their valuable assets (the aircrafts) to boost the economy.

Although it may appear as though the IRS likes to give a tough time to aircraft owners as far as aircraft depreciation is concerned – going as far as suspecting that the aircraft owners’ claims for tax deduction through aircraft depreciation are false – President George W. Bush has already signed the 2008 Economic Stimulus Act to make business easier for aircraft owners that use their aircrafts to help the economy grow.  An unlimited fifty percent bonus depreciation for aircrafts brought into service in 2008 is included in this Act.

Even if an aircraft is purchased this year but delivered the following year – bonus depreciation allows aircraft owners to immediately deduct fifty percent of the aircraft cost, after which they may deduct more under accelerated depreciation.

Additionally, even noncommercial aircraft operators may avail the benefits of the new Act.  These aircraft owners are entitled to subtract sixty percent of aircraft costs during the year of purchase.  The balance would be written off under the accelerated method during the next five years (“ Qualifying for Bonus Depreciation on Aircraft”).

Of course, the 2008 Economic Stimulus Act is meant to offset the problems faced by the United States economy at present.  Noncommercial aircraft owners may avail its benefits for a limited time.  As a matter of fact, “ qualifying assets” described by the Act are only those that are purchased during 2008 (“ Qualifying for Bonus Depreciation on Aircraft”).  If this Act is not extended to cover successive years, noncommercial owners of aircrafts must comply with the IRS rules for aircraft depreciation from 2009 onwards.

If their aircrafts are not at all used for commerce, there is no tax reduction for aircraft depreciation in the years to come.  At present, however, their decision to purchase aircrafts is considered a tool for the growth of the economy.  The country needs to boost its investments, and aircrafts are considered valuable, regardless of whether they are used in trade or not.

References

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