

**§ 1.167(f)-1**

**26 CFR Ch. I (4-1-02 Edition)**

(d) *Change with respect to section 1250 property.* (1) In respect of his first taxable year beginning after July 24, 1969, a taxpayer may elect, without the consent of the Commissioner, to change the method of depreciation of section 1250 property (as defined in section 1250(c)) from any declining balance method or sum of the years-digits method to the straight line method. With respect to any account (as defined in § 1.167(a)-7) this change may be made notwithstanding any provision to the contrary in an agreement under section 167(d), but such change will constitute (as of the first day of such taxable year) a termination of such agreement as to all property in such account. With respect to any account, this change will be permitted only if applied to all the section 1250 property in the account. The election shall be made by a statement on, or attached to, the return for such taxable year filed on or before the last day prescribed by law, including extensions thereof, for filing such return.

(2) When an election under this paragraph is made in respect of section 1250 property in an account, the unrecovered cost or other basis (less a reasonable estimate for salvage) of all the section 1250 property in the account shall be recovered through annual allowances over the estimated remaining useful life determined in accordance with the circumstances existing at that time. If there is other property in such account, the other property shall be placed in a separate account and depreciated by using the same method as was used before the change permitted by this paragraph, but the estimated useful life of such property shall be redetermined in accordance with § 1.167(b)-2 or § 1.167(b)-3, whichever is applicable. The taxpayer shall maintain records which permit specific identification of the section 1250 property in the account with respect to which the election is made and any other property in such account. The records shall also show for all the property in the account the date of the acquisition, cost or other basis, amounts recovered through depreciation and other allowances, the estimated salvage value, the character of the property, and the estimated remaining use-

ful life of the property. A change to the straight line method under this paragraph must be adhered to for the entire taxable year of the change and for all subsequent taxable years unless, with the consent of the Commissioner, a change to another method is permitted.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 6832, 30 FR 8573, July 7, 1965; T.D. 7166, 37 FR 5245, Mar. 11, 1972]

**§ 1.167(f)-1 Reduction of salvage value taken into account for certain personal property.**

(a) *In general.* For taxable years beginning after December 31, 1961, and ending after October 16, 1962, a taxpayer may reduce the amount taken into account as salvage value in computing the allowance for depreciation under section 167(a) with respect to "personal property" as defined in section 167(f)(2) and paragraph (b) of this section. The reduction may be made in an amount which does not exceed 10 percent of the basis of the property for determining depreciation, as of the time as of which salvage value is required to be determined (or when salvage value is redetermined), taking into account all adjustments under section 1016 other than (1) the adjustment under section 1016(a)(2) for depreciation allowed or allowable to the taxpayer, and (2) the adjustment under section 1016(a)(19) for a credit earned by the taxpayer under section 38, to the extent such adjustment is reflected in the basis for depreciation. See paragraph (c) of § 1.167(a)-1 for the definition of salvage value, the time for making the determination, the redetermination of salvage value, and the general rules with respect to the treatment of salvage value. See also section 167(g) and § 1.167(g)-1 for basis for depreciation. A reduction of the amount taken into account as salvage value with respect to any property shall not be binding with respect to other property. In no event shall an asset (or an account) be depreciated below a reasonable salvage value after taking into account the reduction in salvage value permitted by section 167(f) and this section.

(b) *Definitions and special rules.* The following definitions and special rules

apply for purposes of section 167(f) and this section.

(1) *Personal property.* The term "personal property" shall include only depreciable—

(i) Tangible personal property (as defined in section 48 and the regulations thereunder) and

(ii) Intangible personal property

which has an estimated useful life (determined at the time of acquisition) of 3 years or more and which is acquired after October 16, 1962. Such term shall not include livestock. The term "livestock" includes horses, cattle, hogs, sheep, goats, and mink and other furbearing animals, irrespective of the use to which they are put or the purpose for which they are held. The original use of the property need not commence with the taxpayer so long as he acquired it after October 16, 1962; thus, the property may be new or used. For purposes of determining the estimated useful life, the provisions of paragraph (b) of §1.167(a)-1 shall be applied. For rules determining when property is acquired, see subparagraph (2) of this paragraph. For purposes of determining the types of intangible personal property which are subject to the allowance for depreciation, see §1.167(a)-3.

(2) *Acquired.* In determining whether property is acquired after October 16, 1962, property shall be deemed to be acquired when reduced to physical possession, or control. Property which has not been used in the taxpayer's trade or business or held for the production of income and which is thereafter converted by the taxpayer to such use shall be deemed to be acquired on the date of such conversion. In addition, property shall be deemed to be acquired if constructed, reconstructed, or erected by the taxpayer. If construction, reconstruction, or erection by the taxpayer began before October 17, 1962, and was completed after October 16, 1962, section 167(f) and this section apply only to that portion of the basis of the property which is properly attributable to such construction, reconstruction, or erection after October 16, 1962. Property is considered as constructed, reconstructed, or erected by the taxpayer if the work is done for him in accordance with his specifications. The portion of the basis of such

property attributable to construction, reconstruction, or erection after October 16, 1962, consists of all costs of the property allocable to the period after October 16, 1962, including the cost or other basis of materials entering into such work. It is not necessary that such materials be acquired after October 16, 1962, or that they be new in use. If construction or erection by the taxpayer began after October 16, 1962, the entire cost or other basis of such construction or erection qualifies for the reduction provided for by section 167(f) and this section. In the case of reconstruction of property, section 167(f) and this section do not apply to any part of the adjusted basis of such property on October 16, 1962. For purposes of this section, construction, reconstruction, or erection by the taxpayer begins when physical work is started on such construction, reconstruction, or erection.

(c) *Illustrations.* The provisions of paragraphs (a) and (b) of this section may be illustrated by the following examples:

*Example (1).* Taxpayer A purchases a new asset for use in his business on January 1, 1963, for \$10,000. The asset qualifies for the investment credit under section 38 and for the additional first-year depreciation allowance under section 179. A is entitled to an investment credit of \$700 (7%×\$10,000) and elects to take an additional first-year depreciation allowance of \$2,000 (20%×\$10,000). The basis for depreciation (determined in accordance with the provisions of section 167(g) and §1.167(g)-1) is computed as follows:

Purchase price .....	\$10,000
Less: Adjustment required for taxable years beginning before Jan. 1, 1964, under section 1016(a)(19), for the investment credit .....	700
Adjustment required under section 1016(a)(2) for the additional first-year depreciation allowance .....	2,000
	2,700
Basis for depreciation for the taxable year 1963 ....	7,300

However, the basis of the property for determining depreciation as of the time as of which salvage value is required to be determined is \$10,000, the purchase price of the property. A files his income tax returns on a calendar year basis and uses the straight line method of depreciation. A estimates that he will use the asset in his business for 10 years

after which it will have a salvage value of \$500, which is less than \$1,000 (10%×\$10,000, the basis of the property for determining depreciation as of the time as of which salvage value is required to be determined). For the taxable year 1963 A may deduct \$730 as the depreciation allowance. As of January 1, 1964, the basis of the asset is increased by \$700 in accordance with paragraph (d) of § 1.48-7. In computing his total depreciation allowance on the asset, A may reduce the amount taken into account as salvage value to zero and may claim depreciation deductions (including the additional first-year depreciation allowance) totaling \$10,000. See paragraph (d) of § 1.48-7 for the computation of depreciation for taxable years beginning after December 31, 1963, where there is an increase in basis of property subject to the investment credit.

*Example (2).* Assume the same facts as in example (1) except that A in a subsequent taxable year redetermines the estimate of the useful life of the asset and at the same time also redetermines the estimate of salvage value. Assume also that at such time the only reductions reflected in the basis are for depreciation allowed or allowable. Accordingly, the reduction under section 167(f) and this section will be computed with regard to the purchase price and not the unrecovered basis for depreciation at the time of the redetermination.

*Example (3).* Assume the same facts as in example (1) except that A estimates that the asset will have a salvage value of \$1,200 at the end of its useful life. In computing his depreciation for the asset, A may reduce the amount to be taken into account as salvage value to \$200 (\$1,200-\$1,000). Accordingly, A may claim depreciation deductions (including the additional first-year depreciation allowance) totaling \$9,800, i.e., the purchase price of the property (\$10,000) less the amount taken into account as salvage value (\$200).

*Example (4).* Assume the same facts as in example (1) except that the taxpayer had taken into account salvage value of only \$200 but that the estimated salvage value had actually been \$700. The amount of salvage value taken into account by the taxpayer is permissible since the reduction of salvage value by \$500 (\$700-\$200) would be within the limit provided for in section 167 (f), i.e., \$1,000 (10%×\$10,000).

*Example (5).* On January 1, 1963, taxpayer B, a taxicab operator, traded his old taxicab plus cash for a new one, which had an estimated useful life of three years, in a transaction qualifying as a nontaxable exchange. The old taxicab had an adjusted basis of \$2,500. B was allowed \$3,000 for his old taxicab and paid \$1,000 in cash. The basis of the new taxicab for determining depreciation (as determined under section 167(g) and § 1.167(g)-1) is the adjusted basis of the old taxicab at the

time of trade-in (\$2,500) plus the additional cash paid out (\$1,000), or \$3,500. In computing his depreciation allowance on the new taxicab, B may reduce the amount taken into account as salvage value by \$350 (10% of \$3,500).

*Example (6).* Taxpayer C purchases a new asset for use in his business on January 1, 1963, for \$10,000. At the time of purchase, the asset has an estimated useful life of 10 years and an estimated salvage value of \$1,500. C elects to compute his depreciation allowance for the asset by the declining balance method of depreciation, using a rate of 20% which is twice the normal straight line rate of 10% (without adjustment for salvage value). C files his income tax returns on a calendar year basis. In computing his depreciation allowance for the year 1966, C changes his method of determining the depreciation allowance for the asset from the declining balance method to the straight line method (in which salvage value is accounted for in determining the annual depreciation allowances) in accordance with the provisions of section 167(e) and paragraph (b) of § 1.167(e)-1. He also wishes to reduce the amount of salvage value taken into account in accordance with the provisions of section 167(f) and this section. At the close of the year 1966, the only reductions reflected in the basis of the asset are for depreciation allowances. Thus, C may reduce the amount of salvage value taken into account by \$1,000 (10%×\$10,000, the basis of the asset when it was acquired), and, therefore, will account for salvage value of only \$500 in computing his depreciation allowance for the asset in 1966 and subsequent years.

*Example (7).* Taxpayer D purchases a station wagon for his personal use on January 1, 1962, for \$4,500. On January 1, 1963, D converts the use of the station wagon to his business, and at that time it has an estimated useful life of 4 years, an estimated salvage value of \$500, and a basis of \$3,000 (as determined under section 167 (g) and § 1.167 (g)-1). Thus, for purposes of section 167 (f) and this section, D is deemed to have acquired the station wagon on January 1, 1963. D elects the straight line method of depreciation in computing the depreciation allowance for the station wagon and also wishes to reduce the amount of salvage value taken into account in accordance with the provisions of section 167(f) and this section. Accordingly, D may reduce the amount of salvage value taken into account by \$300 (10% of \$3,000). D files his income tax returns on a calendar year basis. His depreciation allowance for the year 1963 would be computed as follows:

Basis for depreciation .....	\$3,000
Less:	
Salvage value .....	\$500 .....

Reduction permitted by section 167(f) .....	300 .....	
	<hr/>	200
Amount to be depreciated over the useful life .....		2,800

D's depreciation allowance on the station wagon for the year 1963 would be \$700 (\$2,800 divided by 4, the remaining useful life).

[T.D. 6712, 29 FR 3654, Mar. 24, 1964, as amended by T.D. 6838, 30 FR 9064, July 20, 1965]

**§ 1.167(g)-1 Basis for depreciation.**

The basis upon which the allowance for depreciation is to be computed with respect to any property shall be the adjusted basis provided in section 1011 for the purpose of determining gain on the sale or other disposition of such property. In the case of property which has not been used in the trade or business or held for the production of income and which is thereafter converted to such use, the fair market value on the date of such conversion, if less than the adjusted basis of the property at that time, is the basis for computing depreciation.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960. Redesignated, T.D. 6712, 29 FR 3653, Mar. 24, 1964]

**§ 1.167(h)-1 Life tenants and beneficiaries of trusts and estates.**

(a) *Life tenants.* In the case of property held by one person for life with remainder to another person, the deduction for depreciation shall be computed as if the life tenant were the absolute owner of the property so that he will be entitled to the deduction during his life, and thereafter the deduction, if any, shall be allowed to the remainderman.

(b) *Trusts.* If property is held in trust, the allowable deduction is to be apportioned between the income beneficiaries and the trustee on the basis of the trust income allocable to each, unless the governing instrument (or local law) requires or permits the trustee to maintain a reserve for depreciation in any amount. In the latter case, the deduction is first allocated to the trustee to the extent that income is set aside for a depreciation reserve, and any part of the deduction in excess of the income set aside for the reserve shall be

apportioned between the income beneficiaries and the trustee on the basis of the trust income (in excess of the income set aside for the reserve) allocable to each. For example:

(1) If under the trust instrument or local law the income of a trust computed without regard to depreciation is to be distributed to a named beneficiary, the beneficiary is entitled to the deduction to the exclusion of the trustee.

(2) If under the trust instrument or local law the income of a trust is to be distributed to a named beneficiary, but the trustee is directed to maintain a reserve for depreciation in any amount, the deduction is allowed to the trustee (except to the extent that income set aside for the reserve is less than the allowable deduction). The same result would follow if the trustee sets aside income for a depreciation reserve pursuant to discretionary authority to do so in the governing instrument.

No effect shall be given to any allocation of the depreciation deduction which gives any beneficiary or the trustee a share of such deduction greater than his pro rata share of the trust income, irrespective of any provisions in the trust instrument except as otherwise provided in this paragraph when the trust instrument or local law requires or permits the trustee to maintain a reserve for depreciation.

(c) *Estates.* In the case of an estate the allowable deduction shall be apportioned between the estate and the heirs legatees, and devisees on the basis of income of the estate which is allocable to each.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960. Redesignated, T.D. 6712, 29 FR 3653, Mar. 24, 1964]

**§ 1.167(i)-1 Depreciation of improvements in the case of mines, etc.**

Property used in the trade or business or held for the production of income which is subject to the allowance for depreciation provided in section 611 shall be treated for all purposes of the Code as if it were property subject to the allowance for depreciation under section 167. The preceding sentence