

depreciation deduction (assuming all other requirements are met).

With respect to the election out of the additional first year depreciation deduction, a taxpayer may elect out of the 30-percent additional first year depreciation deduction for any class of qualified property. For any class of 50-percent bonus depreciation property, a taxpayer may elect either to deduct the 30-percent, instead of the 50-percent, additional first year depreciation deduction or to deduct no additional first year depreciation deduction. The regulations provide the rules for making these elections and also define what is a class of property for purposes of the elections.

#### *Original Use*

Pursuant to section 168(k)(2)(A)(ii), the regulations provide that qualified property is property the original use of which commences with the taxpayer after September 10, 2001. Further, pursuant to section 168(k)(4)(B)(i), the regulations provide that 50-percent bonus depreciation property is property the original use of which commences with the taxpayer after May 5, 2003. The regulations provide that the original use generally means the first use to which the property is put, whether or not that use corresponds to the use of the property by the taxpayer. Thus, new property initially used by a taxpayer for personal use and then subsequently converted by the taxpayer for use in its trade or business satisfies the original use requirement. However, new property acquired by a taxpayer for personal use and then subsequently acquired by a different taxpayer for use in its trade or business does not satisfy the original use requirement.

Likewise, additional capital expenditures incurred by a taxpayer to recondition or rebuild property acquired or owned by the taxpayer satisfies the original use requirement. However, the cost of reconditioned or rebuilt property acquired by the taxpayer does not satisfy the original use requirement. The question of whether property is reconditioned or rebuilt property is a question of fact. The regulations provide a safe harbor that property containing used parts will not be treated as reconditioned or rebuilt if the cost of the used parts is not more than 20 percent of the total cost of the property. *See Rev. Rul. 68-111 (1968-1 C.B. 29).*

The regulations also provide special rules for certain sale-leaseback transactions and syndication transactions. If qualified property is originally placed in service after September 10, 2001, or 50-percent bonus depreciation property is

originally placed in service after May 5, 2003, by a person and the property is involved in a sale-leaseback transaction described in section 168(k)(2)(D)(ii), the taxpayer-lessor is considered the original user of the property. Likewise, if qualified property is originally placed in service by a lessor after September 10, 2001, or 50-percent bonus depreciation property is originally placed in service by a lessor after May 5, 2003, and is sold by the lessor or any subsequent purchaser within three months after the date the property was originally placed in service by the lessor, and the user of the property does not change during this three-month period, the purchaser of the property in the last sale is considered the original user of the property.

The regulations also provide that if in the ordinary course of its business a taxpayer sells fractional interests in qualified property or 50-percent bonus depreciation property to unrelated third parties, each first fractional owner of the property is considered as the original user of its proportionate share of the property. Furthermore, if a taxpayer uses the qualified property or the 50-percent bonus depreciation property before all of the fractional interests are sold and the property continues to be held primarily for sale by the taxpayer, the original use of any fractional interest sold to an unrelated third party subsequent to the taxpayer's use begins with the first purchaser of that interest.

#### *Acquisition of Property*

Pursuant to section 168(k)(2)(A)(iii), the regulations provide that qualified property is property: (1) Acquired by the taxpayer after September 10, 2001, and before January 1, 2005, but only if no written binding contract for the acquisition of the property was in effect before September 11, 2001; or (2) acquired by the taxpayer pursuant to a written binding contract that was entered into after September 10, 2001, and before January 1, 2005. Further, pursuant to section 168(k)(4)(B)(ii), the regulations provide that 50-percent bonus depreciation property is property acquired by the taxpayer after May 5, 2003, and before January 1, 2005, but only if no written binding contract for the acquisition of the property was in effect before May 6, 2003.

The regulations define a binding contract as any contract that is enforceable under State law against the taxpayer or a predecessor, and does not limit damages to a specified amount. However, a contractual provision that limits damages to an amount equal to at least 5 percent of the total contract price will not be treated as limiting damages

to a specified amount. Further, the fact that there will be little or no damages because the contract price does not significantly differ from the fair market value will not be taken into account in determining whether a contract limits damages.

The regulations also provide that a contract is binding even if the contract is subject to a condition, as long as the condition is not within the control of either one of the parties or a predecessor. Further, an option to either acquire or sell property is not treated as a binding contract.

The regulations also provide that a binding contract does not include a supply agreement or similar agreement, if the amount and design specifications of the property to be purchased have not been specified. In this case, the contract is not treated as a binding contract until both the amount and design specifications are specified.

With respect to self-constructed property, the regulations provide that the property acquisition requirement is met if a taxpayer manufactures, constructs, or produces qualified property or 50-percent bonus depreciation property for its own use and such manufacturing, construction, or production began after, respectively, September 10, 2001, or May 5, 2003, and before January 1, 2005. Further, property that is manufactured, constructed, or produced for the taxpayer by another person under a written binding contract that is entered into before the manufacture, construction, or production of the property begins is considered to be manufactured, constructed, or produced by the taxpayer.

The regulations also define when construction begins. Construction of qualified property or 50-percent bonus depreciation property begins when physical work of a significant nature begins. Physical work does not include preliminary activities such as planning or designing, securing financing, exploring, or researching. The determination of when physical work of a significant nature has begun depends on the facts and circumstances. The regulations, however, provide a safe harbor that physical work of a significant nature has begun when the taxpayer incurs or pays more than 10 percent of the total cost of the property (excluding the cost of any land and preliminary activities).

The regulations also provide rules for a contract to acquire, or for the manufacture, construction, or production of, a component of the larger self-constructed property. If a binding contract to acquire a component was in