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Investment Credit

Merlyn M. Dahl
South Dakota State University

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INVESTMENT CREDIT

The Revenue Act of 1971 re-instated investment credit for all qualified property ordered on or after April 1, 1971 or acquired after August 5, 1971, regardless of when it was ordered.

The investment credit implications of a purchase should always be considered because it involves a deduction from the total tax bill, not just from taxable income. Investment credit has the effect of allowing the government to pick up the tab on seven percent of qualified investments. Thus a qualified $1,000 purchase can result in an additional savings of up to $70 on your tax bill.

Qualified Purchases

The property must have a useful life of at least three years for it to qualify for any credit at all and the useful life must be the same as used for depreciation purposes.

In order to qualify for the full seven percent, an item must have a useful life of seven years or longer. Investments with an estimated useful life of five or six years qualify for the credit on only two-thirds of their cost; items with a useful life of three to four years for only one-third of their cost.

Investment credit is not an election. It must be taken (a) in the year the item is placed on a depreciation schedule, or (b) when the item is in a state of readiness to perform the function for which it was purchased.

Eligible Property

Generally, if a purchase is a depreciable item, it will also qualify for investment credit but there are exceptions. Most tangible personal property, on-the-farm improvements, machinery and livestock are the big items to be claimed. Livestock (except horses) purchased for breeding and dairy purposes became qualified property for the first time under the Revenue Act of 1971.

Investment credit generally is not available on buildings and their structural components, such as electrical wiring, plumbing and heating systems. However, there are also exceptions to this ruling. If the equipment and the building are so closely integrated that the structure is considered to be no more than a cover for the equipment, then the entire system could possibly qualify. The possibility is even greater if the building could serve no other useful purpose when the equipment is worn out or if the building would likely be replaced when the equipment is replaced. Unitary livestock and poultry systems would be prime examples because automatic feeding equipment, environmental controls, specifically designed floors and partitions and many other items are part of the entire integrated production system.

Many crop and livestock production items are eligible for investment credit even if not tangible personal property. These could include:

*Fences, gates and corrals for livestock confinement.
*Hard-surfaced feeding floors.
*Livestock water wells (if outside a structure) and irrigation wells.
*Drainage tile, depreciable parts of dams, drainage ways and ponds.
*Grain storage bins and silos if used for bulk storage of fungible (interchangeable) commodities.

Maximum Credit Allowed

Investment credit can be applied to both new and used property. All new equipment qualifies for the credit but is restricted to the individual's tax liability in any one year. Used property is limited to $50,000 annually.

Recapture

If property is disposed of before the end of the useful life originally claimed, the tax in the year of disposal must be increased by the amount of the improperly claimed credit. In other words, the recapture amount is treated as tax due.

Leased Property

Since many farmers lease some equipment instead of buying it outright, the investment credit implications should be closely watched. The owner of the property (lessor) can waive the right to the credit and pass it on to the person leasing the equipment (lessee). This only applies to qualifying new property. A lessor cannot pass credit for used equipment to the lessee.

Summary

This newsletter contains only a brief look at some of the investment credit considerations since it was re-instated after an absence of about two years. For more detailed information, contact your local tax counsellor or the Internal Revenue Service.

Merlyn M. Dahl, Area Farm Management Agent

COOPERATIVE EXTENSION SERVICE
U. S. DEPARTMENT OF AGRICULTURE
SOUTH DAKOTA STATE UNIVERSITY
Brookings, S. D. 57006
OFFICIAL BUSINESS

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