

Leases, Conditional Sales, Personal Property Tax

Nebraska Legislative Update

By Denny Rasmussen

Lots of things going on, but I wanted to clarify a few things on leases, conditional sales and depreciable property.

Leases

Net Book Value is calculated using the owner's (lessor's) Nebraska adjusted basis and date of acquisition. (NOTE: The amount of the lease payments and the date of the lease are NOT used in calculating the net book value.)

Property may be reported by either lessor or lessee, but always based on the owner's basis and date of acquisition.

Taxes may be paid by either lessor or lessee. This is between the two parties, typically spelled out in the lease agreement.

Leases with a purchase option at the end of the lease period are treated as any other lease, until the buy-out option is exercised. When the lessee exercised his buy-out option, he is then the **owner** of the property and the net book value is then determined by using his basis (buy-out price) and date of acquisition (buy-out date).

Example: A farmer leases a combine for five years beginning in March, 1992. The lease contains a buy-out option at the end of the lease. In March, 1997, the farmer exercises his buy-out option and purchases the combine for \$12,000.

For tax years 1993-1997, the combine's net book value is determined using the lessor's (owner's) basis and date of acquisition (not the lease date).

Beginning tax year 1998, the combine's net book value is determined using the farmer's (owner) basis (\$12,000) and the date of acquisition (March, 1997).

Conditional Sales

Conditional sales (see Revenue Ruling 41-89-3) are essentially financing agreements, not true leases. In a conditional sale, the ownership of the property is deemed to rest with the "lessee" at the inception of the lease and it is also the "lessee" not the "lessor" who is able to take federal depreciation of the property. Therefore, in a conditional sale, the "lessee's" basis and the date of acquisition is used to determine the net book value as they are considered the owner. (When in doubt whether a lease agreement is in fact a true lease or a conditional sale, find out which party is able to take the federal depreciation. Whoever

is able to take the federal depreciation is considered the owner and their basis and date of acquisition is used in determining net book value.)

Personal Property Tax

All depreciable tangible personal property is taxable. This includes property which is eligible for depreciation but for which the owner chooses not to depreciate. This may also include property which is "fully depreciated" for federal income tax purposes (when the recovery period for property tax purposes is longer than the actual recovery period chose for federal depreciation). If you purchase property with a recovery period of seven years, but depreciate it fully in five years, the property will still be taxed for seven years.

Depreciable property which is leased is also taxable. In a true lease agreement, the lessor is able to depreciate the property. If the lessee is unable to determine the lessor's Nebraska net book value of leased property, they must provide the name and address of the lessor so this information can be obtained. The lessor must list and determine the net book value of all leased property for which the lessee has not provided the net book value.

Review Revenue Ruling 41-89-3 dealing with conditional sales. When a conditional sale exists, the ownership of the property is deemed to rest with the lessee and the lessee may depreciate the property. In these situations, the lessee should be able to provide the net book value, as it will most likely show up on their depreciation worksheet.