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Aircraft Sales and Proposed Tax Legislation: The Tax Cuts and Jobs Act Eliminates Like-Kind Aircraft Exchange

Transportation Legal Update

On November 16, 2017, the House of Representatives narrowly passed the *Tax Cuts and Jobs Act.* This bill would be a major overhaul of the current tax regime, making significant changes. The Senate is considering its own tax overhaul bill, which is currently in committee.

The ultimate fate of the legislation is unknown and changes to each bill are expected. However, provisions in both the House and Senate bills would significantly affect business aircraft owners and operators as well as all those who assist those parties in aircraft transactions. Specifically, if signed into law as written, the *Tax Cuts and Jobs Act* would take away the ability to use the ever-popular tax planning device known as the "like-kind exchange" (commonly short-handed to "LKE") under Section 1031 of the Internal Revenue Code ("Section 1031") in aircraft transactions.

When a taxpayer sells an aircraft, he or she will normally recognize taxable gain if the amount realized from the sale is greater than its adjusted basis (the cost of the aircraft minus the amount of any depreciation taken). Section 1031 currently allows the taxpayer to defer any gain on the sale of an aircraft, if that aircraft is held for productive use in a trade or business or for investment, **and** if it is exchanged solely for another aircraft of a like kind that is also held for productive use in a trade or business or for investment.

The *Tax Cuts and Jobs Act*, however, eliminates the use of an LKE for personal property such as aircraft for transactions started after December 31, 2017. Thereafter, LKEs would be limited to real property exchanges. This means that aircraft owners would no longer be able to rely on Section 1031 to defer any taxable gain on the sale of their aircraft when they upgrade. Instead, aircraft owners will pay income tax on any gains realized on the sale of their aircraft even if the taxpayer replaces that aircraft.

There are other provisions in both the House and Senate versions that might buffer the sting from the elimination of LKEs. The House bill provides for the immediate deduction of 100% of the acquisition cost of new or used business property such as aircraft (rather than depreciation over five years per MACRS); the Senate bill covers only new aircraft. This special expensing provision expires in five years. In addition, both the House bill and the Senate bill increase the amount available for immediate expensing under Section 179 – to $5.0 million under the House bill, and $2.5 million under the Senate bill.

We will continue monitoring the status of the *Tax Cuts and Jobs Act* and the Senate tax bill.