

**SECTION 14000 LOCAL AGENCY MILITARY BASE RECOVERY AREA
BUSINESS EXPENSE DEDUCTION**

References 17268(a); 17268(d)(4); 17268(e)(1); 24356.8(a); 24356.8(d)(1)

For each taxable year beginning on or after January 1, 1995, a person or entity (other than an estate or trust) engaged in a trade or business within a Local Agency Military Base Recovery Area (LAMBRA) may elect to treat 40% of the eligible cost of qualified property as a business expense rather than a capital expense.

The deduction is allowed for the taxable year in which the property is placed in service.

EDAM 14100	GEOGRAPHIC BOUNDARIES AND DESIGNATION DATES
EDAM 14200	"TAXPAYER" DEFINED
EDAM 14300	QUALIFIED PROPERTY
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EDAM 14500	MAKING THE ELECTION
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EDAM 14800	RECAPTURE

14100 Geographic Boundaries and Designation Dates

For a listing of LAMBRAs, refer to EDAM 1320. To verify an address, refer to EDAM 1300.

14200 "Taxpayer" Defined

References 17268(e)(2); 24356.8(d)(2)

EDAM 14210 Allowance of the LAMBRA Business Expense Deduction
EDAM 14220 Estates and Trusts
EDAM 14230 Pass-Through Entities

A "taxpayer" is a person or entity engaged in a trade or business within a LAMBRA and, for the first two taxable years, has a net increase in jobs (defined as 2,000 paid hours per employee per year) of one or more employees in the LAMBRA.

14210 Allowance of the LAMBRA Business Expense Deduction

Taxpayers engaged in operations within a LAMBRA are allowed to utilize the LAMBRA business expense deduction beginning in the first year of operations within the LAMBRA even though they cannot fulfill the definition of a qualified taxpayer before the close of the second year of operations in the LAMBRA when the net increase in jobs is computed. If at the end of the second year the taxpayer does not meet the definition of a "qualified taxpayer", the LAMBRA business expense deduction previously utilized must be recaptured.

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14220 Estates and Trusts

References 17268(d)(4)

Estates and trusts are not allowed to take the business expense deduction.

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14230 Pass-Through Entities

The determination of whether a taxpayer is a qualified taxpayer is made at the entity level. The term "pass-through entity" means any partnership or S corporation. The business expense deduction is allowed to the pass-through entity and passed through to the partners or shareholders.

14300 Qualified Property

References 17268(d); 17268(g); 24356.8(c); 24356.8(g)

EDAM 14310 Leased Property
EDAM 14320 Property Not Qualified

Qualified property is IRC § 1245 property (as defined in Section 1245(a)(3) of the Internal Revenue Code) purchased and placed in service for exclusive use in a trade or business conducted within a LAMBRA. The property must also be purchased and placed in service before the date the LAMBRA designation expires, is no longer binding, or becomes inoperative.

Qualified property under IRC § 1245 includes, but is not limited to, tangible personal property (excluding buildings and inventory) that is subject to the allowance for depreciation. This includes most equipment and furnishings purchased for *exclusive use* within a LAMBRA. Office supplies and other small non-depreciable items are not included.

14310 Leased Property

Taxpayers who acquire property by lease arrangement may be able to take the business expense deduction. The structure of the leasing arrangement itself is critical. Lease arrangements structured using a financial (conditional sales) contract generally will qualify the taxpayer to take the business expense deduction. For reference sources to determine if a lease qualifies as a purchase rather than a lease arrangement, refer to IRS Revenue Ruling 55-540, 1955-2 C.B. 39, and [FTB Legal Ruling 94-2](#), March 23, 1994.

14320 Property Not Qualified

References 17268(d); 24356.8(c)

The business expense deduction is not allowed if the property:

- Was transferred between members of an affiliated group;
- Was acquired as a gift or inherited;
- Was traded for other property;
- Is property for which the taxpayer may not make an election under IRC § 179 due to the provisions of IRC § 179(d);
- Was received from a personal or business relation as defined by IRC § 267, as modified by CR&TC § 17268(d)(2)(A) and 24356.8(c)(2)(A) for a LAMBRA;
- Was received from a personal or business relation as defined by IRC § 707(b); or
- Is described in IRC § 168(f).

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14400 Deduction Amount

References 17268(f); 24356.8(f)

- EDAM 14410 Pass-Through Entities
- EDAM 14420 Personal Income Tax Taxpayers-Married Filing Separate
- EDAM 14430 Basis reduction / Depreciation
- EDAM 14440 Interaction with the Manufacturer's Investment Credit

For taxable years beginning on or after January 1, 1999, the *maximum* deduction the taxpayer may claim in any taxable year is determined by the number of years that have elapsed since the area was designated, as follows:

Taxable Years	Maximum Aggregate Cost	Maximum Deduction
Taxable year of designation and 1 st year thereafter	\$100,000	\$40,000
2 nd and 3 rd taxable year thereafter	\$75,000	\$30,000
Each taxable year thereafter	\$50,000	\$20,000

For taxable years beginning before January 1, 1999, the maximum *deduction* the taxpayer may claim in any taxable year is determined by the number of years that have elapsed since the area was designated, as follows:

Taxable Years	Maximum Deduction
Taxable year of designation and 1 st year thereafter	\$5,000
2 nd and 3 rd taxable year thereafter	\$ 7,500
Each taxable year thereafter	\$10,000

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14410 Pass-Through Entities

References 17268(d)(6); 24356.8(c)(8)

In the case of pass-through entities, the percentage limitation (40%), of the aggregate cost of all qualified property, shall apply at the entity level and at the partner/shareholder level.

14420 Personal Income Tax Taxpayers-Married Filing Separate

References 17268(b)

In the case of a husband and wife filing separate returns for a taxable year, the applicable deduction is equal to one-half (50%) of the otherwise allowable deduction.

14430 Basis reduction / Depreciation

The basis (cost for depreciation purposes) of the property is reduced by the amount allowed as a deduction. Depreciation of the cost of the property, less the amount deducted, may be claimed using any method of depreciation normally allowed. **NOTE:** Depreciation will start with the taxable year following the year in which the property is placed in service. The depreciation is calculated on the remaining basis *after* reduction for the business expense deduction.

Taxpayers electing to take the business expense deduction cannot claim the additional first year depreciation (IRC § 179 or CR&TC § 24356) for the same property.

14440 Interaction with the Manufacturer's Investment Credit

References 17053.49(b)(1)(C); 23649(b)(1)(C)

Taxpayers claiming the business expense deduction and the Manufacturers' Investment Credit (MIC) for the same property must reduce MIC qualified costs by the amount of the business expense deduction before computing the MIC. Taxpayers that elect to take the business expense deduction are not allowed to capitalize the expensed amount.

14500 Making the Election

References 17268(a); 17268(c); 24356.8(a); 24356.8(b)

EDAM 14510 Members of an Affiliated Group

The taxpayer must make an election to treat the cost of qualified property as a business expense, on the original return filed for the taxable year the property is first placed in service. The election must specify the items to which the election applies and the portion of the cost taken into account for purposes of determining the deduction amount. The election may not be revoked, unless the taxpayer has obtained the consent of the Franchise Tax Board.

The taxpayer makes the election by using:

- [Form FTB 3807](#) – Local Agency Military Base Recovery Area Deduction and Credit Summary.

14510 Members of an Affiliated Group

References 24356.8(c)(5)-(6)

For purposes of electing the business expense deduction, all members of an affiliated group are treated as one taxpayer. The maximum deduction amount is properly apportioned among the members of the affiliated group.

An affiliated group is defined in IRC § 1504 as modified by the California Revenue & Taxation Code, to replace "at least 80%" with "more than 50%" each place it appears in IRC § 1504(a).

14600 Creating a Net Operating Loss

Unlike IRC § 179, there is *no* statutory prohibition on the amount of business expense deduction amount that may create a net operating loss.

14700 Alternative Minimum Tax

References 17062; 23457

The business expense deduction is *not* listed as a tax preference item.

14800 Recapture

References 17268(h); 24356.8(h): See also Cal. Code Regs. (CCR) §17267.2-1(a); 24356.7-1

EDAM 14810 Special LAMBRA Recapture

The business expense deduction is subject to recapture (added back to income) if, before the *close of the second taxable year after* the property is placed in service, the property is sold, disposed of, or is no longer used exclusively within the LAMBRA trade or business. The taxpayer is required to recapture the amount previously expensed for that item and include the amount as income for the taxable year in which the property ceases to be used. The basis of the property is increased as of the first day of the taxable year in which the recapture event occurs.

To recapture the amount deducted, add to the current year income, the amount previously deducted for that property.

Example: Corp. A purchases property on June 1, 1998 that qualifies Corp. A to take the LAMBRA business expense deduction. Corp. A's income year ends December 31 of each year. Corp. A disposes of the property August 5, 2000. The previous deduction is added to income in the 2000 tax year because the property was disposed of before the close of the second taxable year after the property was placed in service (12/31/2000). The basis in the asset would be increased by the recaptured amount effective January 1, 2000.

NOTE: The State Board of Equalization in an unpublished and (uncitable) decision agreed that the statute requires the closure of two taxable years after the end of the taxable year in which the property is placed in service and the election to claim the deduction on the original return is made. *Appeal of Accurate Metal Fabricators, Inc. 32552, Cal. St. Bd. Of Equal., July 3, 2000.*

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14810 Special LAMBRA Recapture

References 17268(h); 17268(e)(2); 24356.8(h); 24356.8(d)(2)

See EDAM 12625.