

Qualified Production Property

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OBBB: Qualified Production Property – New 100% Bonus-eligible Asset Type

- The OBBB introduced a new tax incentive under Section 168(n), allowing 100% bonus depreciation on the adjusted basis of QPP. This provision is designed to promote domestic investment by enabling taxpayers to fully expense the cost of eligible nonresidential real property. Taxpayers must make an irrevocable election to apply this special depreciation.



QPP Defined

- QPP is nonresidential real property that:
 - Is used by the taxpayer as an integral part of a qualified production activity;
 - Is located in the U.S.;
 - Has original use beginning with the taxpayer;
 - Begins construction after Jan. 19, 2025, and before Jan. 1, 2029; and
 - Placed in service by Jan. 1, 2031.



Qualified Production Activity Defined

- “Is used by the taxpayer as an integral part of a qualified production activity:”
 - Qualified Production Activity includes manufacturing, production, or refining of a qualified product.
 - “Production” in the above sentence specifically means agriculture or chemical production activities only
 - “Manufacturing” is not defined
 - “Refining” is not defined
 - “Qualified Product” means any tangible personal property if such property is not a food or beverage prepared in the same building as the retail establishment in which the property is sold

Qualified Production Activity Defined (cont'd)

- “Is used by the taxpayer as an integral part of a qualified production activity:”
 - The activities of any taxpayer do not constitute manufacturing, production, or refining of a qualified product unless the activities of such taxpayer result in a substantial transformation of the property *comprising the product*
 - Note – there is no further clarification or further elaboration as to what “substantial transformation” means

Qualified Production Activity - Exclusions

- QPA does not include any portion of the building used for non-production purposes, such as:
 - Office space
 - Administrative function areas
 - Lodging
 - Parking
 - Sales / R&D
 - Software Development / Engineering
- *Note – cost seg methodologies will likely be appropriate/necessary to isolate the assets located in excluded areas*

Qualified Production Activity - Landlords

- The rules also clarify that if the taxpayer is the lessor, and the lessee is the party involved in the QPA, the taxpayer (lessor) is precluded from claiming deductions for QPP.
- Tax planning tip: Structure the deal so that the entity that owns the real estate is the entity involved in the qualified production activity (where applicable avoid propco/opco setup if the real estate owner would like to claim deductions for QPP).

Original Use Requirement – Acquired/Used Property

- The bill text says the original use of the QPP must lie with the taxpayer. It clarifies that used property will satisfy the original use requirement if:
 - The property was acquired after January 19, 2025 and before January 1, 2029
 - Written binding contract rules apply here
 - The property was not used in a qualified production activity by any person at any time during the period beginning on January 1, 2021 and ending on May 12, 2025.

Original Use Requirement – Acquired/Used Property (cont'd)

- The bill text says the original use of the QPP must lie with the taxpayer. It clarifies that used property will satisfy the original use requirement if:
 - The property was not used by the taxpayer at any time prior to such acquisition
 - The property was not acquired by the taxpayer in a related party transaction

QPP – Other notes

- QPP does NOT include any property where ADS is required (tax-exempt-use property will never be QPP)
- Section 1245 depreciation recapture applies if at any time within 10 years of placing the QPP in service the property fails to meet the definition of QPP (converted to a non-qualifying use)

QPP – Other notes

- Making the election:
 - The election must specify the nonresidential real property that is QPP
 - What will “specifying” entail exactly (how detailed will this need to be)?
 - The election must be made in the year the qualifying property is first placed into service
 - Irrevocable (unless the Secretary provides consent)
 - Further administrative details about making the election will be provided via regulations

QPP – Additional Thoughts / Considerations

- Key terms left undefined:
 - Manufacturing
 - Refining
 - Substantial transformation

QPP – Additional Thoughts / Considerations

- Where will the line be drawn for determining what 1250 property is QPP that exists inside of, bordering, or adjacent to “qualifying activity areas?”
 - Poured concrete floors
 - Foundation components
 - Exterior walls/roofs enclosing qualifying areas
 - HVAC equipment that services/conditions qualified areas but that do not physical exist in those spaces
 - Primary MEP distribution elements that might also concurrently service other “non-qualifying areas?”

QPP – Additional Thoughts / Considerations

- The IRS may look to past or existing frameworks – such as the uniform capitalization rules under Section 263A or the former Section 199 manufacturing deduction – to define manufacturing and production for purposes of QPP

QPP – Additional Thoughts / Considerations

- Interaction of QPP and QIP – is one “better”, or more inclusive than the other?
 - Generally the applicability/eligibility of QIP is much broader than QPP
 - For a renovation of an existing building, or TI for qualifying activities, QPP might include more structural components (like structural beams/girders/columns, exterior walls, etc.) that might be excluded from QIP
 - 163(j) – QIP must be ADS with this election, but QPP can still be MACRS (probably)
 - State / local tax differences?

QPP – Final Thoughts

- How applicable is QPP to your client base?
- WE NEED REGULATIONS!!!