



New deduction for QPP can save significant taxes for manufacturers and similar businesses

The One Big Beautiful Bill Act (OBBBA) allows 100% first-year depreciation for nonresidential real estate that's classified as qualified production property (QPP). This new break is different from the first-year bonus depreciation that's available for assets such as tangible property with a recovery period of 20 years or less and qualified improvement property with a 15-year recovery period. Normally, nonresidential buildings must be depreciated over 39 years.

What is QPP?

The statutory definition of QPP is a bit complicated:

- *QPP* is the portion of any nonresidential real estate that's used by the taxpayer (your business) as an integral part of a *qualified production activity*.
- A *qualified production activity* is the manufacturing, production or refining of a *qualified product*.
- A *qualified product* is any tangible personal property that isn't a food or beverage prepared in the same building as a retail establishment in which the property is sold. (So a restaurant building can't be QPP.)

In addition, an activity doesn't constitute manufacturing, production or refining of a qualified product unless the activity results in a substantial transformation of the property comprising the product.

To sum up these rules, QPP generally means factory buildings. But additional rules apply.

Meeting the placed-in-service rules

QPP 100% first-year depreciation is available for property whose construction begins after January 19, 2025, and before 2029. The property generally must be placed in service in the United States or a U.S. possession before 2031. In addition, the original use of the property generally must commence with the taxpayer.

There's an exception to the original-use rule. The QPP deduction can be claimed for a previously used nonresidential building that:

1. Is acquired by the taxpayer after January 19, 2025, and before 2029,
2. Wasn't used in a qualified production activity between January 1, 2021, and May 12, 2025,
3. Wasn't used by the taxpayer before being acquired,
4. Is used by the taxpayer as an integral part of a qualified production activity, and
5. Is placed in service in the United States or a U.S. possession before 2031.

Also, the IRS can extend the before-2031 placed-in-service deadline for property that otherwise meets the requirements to be QPP if an Act of God (as defined) prevents the taxpayer from placing the property in service before the deadline.

Pitfalls to watch out for

While potentially valuable, 100% first-year depreciation for QPP isn't without pitfalls:

Leased-out buildings. To be QPP, the building must be used by the taxpayer for a qualified production activity. So, if you're the lessor of a building, you can't treat it as QPP even if it's used by a lessee for a qualified production activity.

Nonqualified activities. You can't treat as QPP any area of a building that's used for offices, administrative services, lodging, parking, sales activities, research activities, software development, engineering activities or other functions unrelated to the manufacturing, production or refining of tangible personal property.

Ordinary income recapture rule. If at any time during the 10-year period beginning on the date that QPP is placed in service the property ceases to be used for a qualified production activity, an ordinary income depreciation recapture rule will apply.

IRS guidance expected

QPP 100% first-year depreciation can be a valuable tax break if you have eligible property. However, it could be challenging to identify and allocate costs to portions of buildings that are used only for nonqualifying activities or for several activities, not all of which are qualifying activities. Also, once made, the election can't be revoked without IRS consent. IRS guidance on this new deduction is expected. Contact us with questions and to learn about the latest developments.

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