

FURTHER DISCUSSION AND IRS DEFINITION OF DEPRECIATION AND CAPITAL EXPENSES

Depreciation is the annual deduction allowed to recover the cost or other basis of business or investment property having a useful life substantially beyond the tax. However, land is not depreciable. Depreciation starts when you first use the property in your business or for the production of income. It ends when you take the property out of service, deduct all the depreciable cost or other basis, or no longer use the property in your business or for the production of income. convention, you may elect to use the

Capital Expenses

You must capitalize some costs rather than deduct them. These costs are a part of your investment in your business and are called "capital expenses." When you capitalize a cost, you add to the basis of the property to which it relates.

Although you generally cannot take a current deduction for a capital expense, you may be able to take deductions for these costs over a period of years as explained later under *Cost Recovery*.

Kind of Capital Expenses

You must capitalize the following costs.

- *Going into business.* The costs of getting started in business, before you are authorized to start selling your company's products, are capital expenses. These "start up costs" include the cost of exploring different direct-selling opportunities, the cost of any training you must have before becoming a direct seller for your product line, any fees you must pay to the company to become a direct seller, and similar costs. See chapter 9 of Publication 535 for information on how to treat these costs.
- *Business assets.* The cost of any asset (property) that will last substantially beyond the tax year it is placed in service is a capital expense. Examples of business assets include: office furniture, business vehicles, and storage shelves. See *Cost Recovery*, later.
- *Improvements.* The costs of making improvements to a business asset are capital expenses if the improvements add to the value of the asset, appreciably lengthen the time you can use it, or adapt it to a different use. However, normal repair expenses are deducted as current business expenses and are not capitalized. For example, if you have a car you use only for business, maintenance and repair costs, such as tune-ups, new headlights, or brake repairs, are business expenses. The cost of overhauling the engine, however, would be a capital expense.