Tax Notes

The Phase-Out of Bonus Depreciation and Its Effect on Your Business

By Valerie Imondi, CPA, Senior Manager

Since 2017 under the Tax Cuts and Jobs Act (the Act), businesses have been benefiting from a provision which has allowed 100% bonus deprecation on qualified assets. This benefit is expected to begin phasing out starting as soon as the end of 2022. With this change on the horizon, it is crucial that these businesses have a tax plan in place to address how this will impact not only the 2022 tax year, but future years and asset purchases going forward.

Observations and Planning Considerations

Under the Act, qualified assets acquired and placed in service after September 27, 2017 and before January 1, 2023 are entitled to take 100% bonus deprecation. After 2023, bonus depreciation available will drop, as follows:

- 80% for property placed in service in 2023
- 60% for property placed in service in 2024
- 40% for property placed in service in 2025
- 20% for property placed in service in 2026
- 0% for property placed in service in 2027 and later years

Businesses will continue to have the benefit of Section 179 which is expected to be fully available in future tax years. The Section 179 deduction allows expensing of many business asset purchases, similar to bonus depreciation. However, unlike bonus depreciation, the Section 179 deduction is limited. The Section 179 deduction limit for businesses in 2022 is $1,080,000 and there is a phase-out of the deduction that starts once qualified assets exceed $2.7 million. Unlike bonus depreciation, Section 179 deductions cannot result in a tax loss and can only be taken to the extent of taxable income.

Regular deprecation will also continue to be available to businesses. Regular deprecation is calculated evenly over a number of years fixed by law for the particular type of item. There are no limits or phase-outs when taking regular deprecation.

The option to elect the *de minimis* safe harbor is also still available to businesses for tax years 2022 and beyond. The *de minimis* rules allow a taxpayer to deduct up to $2,500 for tangible property acquired (increased to $5,000 if applicable financial statements are prepared), regardless of whether the tangible property meets the definition of a purchase that would normally be capitalized.

Look Ahead

The end of bonus depreciation could be a significant change for businesses that have been relying on it for business and tax planning. Modeling of how the future state will affect taxable income annually is imperative. While tax incentives, such as bonus deprecation and Section 179, can be a beneficial tool while tax planning, these provisions should be used only when it makes financial sense for your business. It is important to always consider your cash-flow requirements and overall tax strategy when considering these depreciation provisions.

Contact Us

Determining whether to take bonus depreciation can include many variables and can seem overwhelming. If you have any questions, contact your client service partner or:

Valerie Imondi, CPA
Senior Manager
vimondi@pkfod.com | 845.670.7111

Christopher Migliaccio, JD
Principal
cmigliaccio@pkfod.com | 646.699.2890