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TCJA: Convert Personal Vehicle to Business and Deduct up to 100%

You probably like your personal vehicle just as it is.

But wouldn't you like it far better if it were producing tax deductions? Perhaps big deductions, immediately. And the Tax Cuts and Jobs Act (TCJA) gives you the tax reform road map on how to do this.

Of course, to make this happen, you need to strip your personal vehicle of its personal status and re-dress it as a business vehicle. This is not difficult, as you will learn in this article.

In its new business dress, your former personal vehicle can qualify for up to 100 percent bonus depreciation.

Example. Sam has a personal vehicle with a tax basis for depreciation of $31,000. With 70 percent business use on this 100 percent bonus depreciation qualifying vehicle, Sam has a new $21,700 tax deduction for this year ($31,000 x 70 percent).

Let's examine what you would need to do to make this work for you and how much you could write off this year.

Depreciating a Former Personal Vehicle

When you convert a personal vehicle to business use, the law sees you as placing the item in service in your business at that time. That means you can begin depreciating the asset and claiming your tax deductions.[1]

To determine the basis to use for depreciation, use the *lesser* of[2]

- fair market value on the date of conversion from personal to business use; or
- adjusted basis of the property (generally the amount you paid for the asset plus the cost of any improvements).

Example. Sam bought the personal vehicle for $43,000. Today, it has a fair market value of $31,000. Upon converting the vehicle to use in his business, Sam uses the lower $31,000 fair market value as his beginning basis.

Bonus Depreciation and Section 179 Expensing

You may not use Section 179 expensing on assets that you convert from personal to business use.[3]

But you may use bonus depreciation. Bonus depreciation, as explained below, is a different and likely more beneficial story.

Bonus Depreciation Rule You Must Know

The law makes bonus depreciation your method of depreciation if you don't elect OUT of it on your tax return.[4] This is unusual. Generally, to qualify for an additional tax break, you must take action. But with bonus depreciation, you are in for the tax break if you don't elect out of it.

And beware: when you "don't elect out" of bonus depreciation, the 100 percent deduction applies to all assets in the class.

Example. You place in service a vehicle that's in the five-year class, and also seven other non-vehicle five-year-class assets. You must claim bonus depreciation on either (a) all eight assets or (b) none. To get to the "none," you must elect out of bonus depreciation for this class of assets on your tax return.

Purchased after September 27, 2017

The bonus depreciation deduction for most qualifying assets[5] purchased after September 27, 2017, and before January 1, 2023, is

- 100 percent;[6]
- 50 percent (if you elect to substitute 50 percent for 100 percent during the first taxable year ending after September 27, 2017[7]); or
- if restricted by the luxury vehicle rules, limited to your business-use percentage of $8,000.[8]

For a calendar-year taxpayer who is not going to use the IRS optional mileage rates for his or her business vehicle, the post–September 27, 2017, acquisition of a personal vehicle and subsequent conversion to business use this year (2018) will trigger for the business use one of the following:

- a 100 percent bonus depreciation deduction;

- a bonus depreciation deduction limited by the $8,000 luxury limit as explained in Tax Reform Allows Bigger, Faster Business Car Deductions; or
- if you or your corporation or partnership elected out of bonus depreciation for this class of asset, MACRS depreciation.

Example. John bought a personal SUV on October 1, 2017, for $40,000. Today, when the SUV has a fair market value of $30,000, John converts it to business use and claims 80 percent business use. The SUV has a gross vehicle weight rating (GVWR) greater than 6,000 pounds, so it is not classified as a luxury vehicle.[9]

John does not “elect out” of bonus depreciation and does not elect IRS mileage rates. John’s 2018 bonus depreciation deduction is $24,000 on this previously personal vehicle ($30,000 x 80 percent).

Yes, you read that right! John’s previously personal vehicle created a $24,000 tax deduction this year.

Purchased before September 28, 2017

For bonus depreciation property acquired before September 28, 2017, the 100 percent bonus depreciation is replaced with[10]

- 50 percent for property placed in service *before* January 1, 2018, and certain long aircraft, film, and water property placed in service *during* 2018;
- 40 percent for property placed in service in 2018 and certain long aircraft, film, and water property placed in service during 2019;
- 30 percent for property placed in service in 2019 and certain long aircraft, film, and water property placed in service during 2020; and
- zero for property placed in service in 2020 and certain long aircraft, film, and water property placed in service after 2020.

Example. Mary bought her personal SUV in 2016. The SUV has a GVWR of 6,050 pounds, so it’s not subject to the luxury limits. Today, the vehicle has a fair market value of $44,000. Mary uses the vehicle 90 percent for business, so her business basis is $39,600. Her 2018 depreciation deductions are $20,592, computed as follows:

- $15,840 in bonus depreciation ($39,600 x 40 percent), plus

$4,752 in MACRS depreciation ($39,600 - $15,840 x 20 percent).

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Luxury Limits on Bonus Depreciation for Passenger Autos Acquired before September 28, 2017

In the case of a passenger automobile subject to the tax law defined luxury limits, acquired before September 28, 2017, and placed in service[11]

- after September 27, 2017, but before 2018, the tax code limits your bonus depreciation to $8,000;
- during 2018, the tax code reduces the bonus depreciation to a $6,400 limit; and
- during 2019, the tax code reduces the bonus depreciation to a $4,800 limit.

Basis When You Sell

There's a trick to basis when you sell property that you converted from personal to business—you use a different rule for calculating losses than you do for calculating gains:

- **Losses.** To calculate losses, use your adjusted basis (conversion basis as discussed above minus depreciation).[12]
- **Gains.** To calculate gains, use original cost basis minus post-conversion depreciation. In most cases, original cost gives you a higher basis and thus less tax on your gains.[13] So don't accidentally use adjusted basis.

Planning note. Most vehicles don't appreciate, but classic and antique vehicles do. Using a classic vehicle in business can produce great financial results. For how this works, see Tax Deduction for Classic Car Used in Business.

Takeaways

When it comes to your taxes, most personal assets other than your home suck:

- You pay taxes on the gains.
- You may not deduct the losses.

But when you convert a personal vehicle or other personal asset to business use, you create tax deductions. And you create these new tax deductions without spending any new money.

Now, say thank you to tax reform. The TCJA reinstated 100 percent bonus depreciation. Take a look at that personal vehicle. How much could it produce in immediate tax deductions for you?

Client Letter on This Article for Use by Tax Pros. Click Here.

1 Reg. Section 1.168(i)-4(b)(1).
2 Reg. Section 1.167(g)-1.
3 Rev. Rul. 77-448.
4 IRC Section 168(k)(7) 2018; Reg. Section 1.168(k)-1(e).
5 IRC Section 168(k)(2)(A)(iii) 2018.
6 IRC Section 168(k)(6)(A)(i) 2018.
7 IRC Section 168(k)(10) 2018.
8 IRC Section 168(k)(2)(F)(i) 2018.
9 IRC Section 280F(d)(5).
10 IRC Section 168(k)(8) 2018.
11 IRC Section 168(k)(2)(F)(iii) 2018.
12 Reg. Section 1.165-9(b).
13 See IRC Section 1011; Reg. Section 1.167(g)-1.