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## IRS Saves Many Vehicles from the TCJA Bonus Depreciation Debacle

Imagine this: In 2018, you buy and place in service a \$60,000 business car that you use 100 percent for business.

You don't ELECT OUT of bonus depreciation, and you don't choose Section 179 expensing (always worthless on luxury limited vehicles, as we explain below).

Without the new IRS rescue, your business car depreciation deductions would have looked like this.<sup>1</sup>

Year	Deductions
2018	\$18,000
2019	\$0
2020	\$0
2021	\$0
2022	\$0
2023	\$0
2024	\$5,760
2025	\$5,760
2026	\$5,760
2027	\$5,760
2028	\$5,760
and beyond	until depreciated

### Outraged

If this happened to you, you would be outraged. The IRS says it this way: "To mitigate the anomalous result ... the IRS provides a safe harbor ..."

You will like the safe harbor, but first you have to love the IRS's use of the word "anomalous."

It's a great description for this new law's unintended consequences. Merriam-Webster's dictionary defines "anomalous" as "irregular, unusual, paradoxical, contradictory, and inconsistent with the expected."<sup>2</sup>

### Results with the Safe Harbor

To first see how good the safe harbor is, look at the table below. It shows you the deductions for that \$60,000 business car using the safe harbor.<sup>3</sup>

Year	Deductions
2018	\$18,000
2019	\$13,440
2020	\$8,064
2021	\$4,838
2022	\$4,838
2023	\$2,419
2024	\$5,760
2025	\$2,641
<b>Total</b>	<b>\$60,000</b>

As you can see, the IRS has truly come to the rescue with its safe harbor.

### Calculation Observations

1. The IRS reduces the original basis by the full first-year depreciation deduction when computing the MACRS depreciation for years 2019 through 2023 ( $\$60,000 - \$18,000 = \$42,000$ ). The 2019 depreciation under this method is  $\$13,440$  ( $\$42,000 \times 32$  percent). For the techies, this is

different from what you are used to. For example, with 50 percent bonus depreciation on a \$100,000 asset, you deduct \$50,000 and then commence a regular depreciation schedule on the remaining \$50,000.

2. Moving further down the above table, the lower 2023 depreciation amount of \$2,419 reflects the 50 percent half-year MACRS depreciation convention in year six of the asset's life.
3. In 2024, the MACRS' life is over. You write off the remaining undepreciated basis at an amount not to exceed \$5,760 per year.<sup>4</sup>
4. In 2025, your remaining basis is \$2,641, and you write that off in full because it is less than \$5,760.

### ***Don't Claim Section 179***

You can claim a Section 179 deduction on a business vehicle that's subject to the luxury limits, but you don't get even one additional dollar of benefit more than you would get with depreciation. That's a zero-sum game to start with, but it gets much worse.

Say, on the car above, you elect \$18,000 in Section 179 expensing, which matches what you could deduct using MACRS and bonus depreciation in the first year. If you make this mistake, your miserable deductions are as shown in the table below.<sup>5</sup>

Year	Deductions
2018	\$18,000
2019	\$0
2020	\$0
2021	\$0
2022	\$0
2023	\$0
2024	\$5,760
2025	\$5,760
2026	\$5,760
2027	\$5,760
2028 and beyond	\$5,760 until depreciated

### ***Electing Out of Bonus Depreciation***

First, a reminder. Under the TCJA tax reform, bonus depreciation applies to both new and used assets.<sup>6</sup>

You can elect out of bonus depreciation, but you must do that on an asset class basis.<sup>7</sup> Vehicles are in the five-year class. To elect out of bonus depreciation on a vehicle, you have to elect out of bonus depreciation on all assets in the five-year classification.

Note that you have to ELECT OUT. This is unusual, because for most tax options, you need to elect the treatment (opt in).

Let's return to the \$60,000 business car with 100 percent business use, but this time let's both (a) elect out of bonus depreciation and (b) avoid the dreaded Section 179 luxury vehicle deduction mistake. With no bonus depreciation and no 179 deduction, your depreciation deductions on that \$60,000 car are as follows.<sup>8</sup>

Year	Deductions
2018	\$10,000
2019	\$16,000
2020	\$9,600
2021	\$5,760
2022	\$5,760
2023	\$3,456
2024	\$5,760
2025	\$3,664

The 2023 MACRS calculation uses the half-year convention, and that's less than the \$5,760 luxury limit for that year. Thus, we use the lower amount of \$3,456 (\$60,000 x 5.76 percent).

## Luxury Vehicle

You have a vehicle that's subject to the luxury vehicle depreciation limits when you buy and place in service a new or used<sup>9</sup>

- automobile with a curb weight (no people or cargo) of 6,000 pounds or less, or
- pickup truck, van, or crossover vehicle with a gross vehicle weight rating (GVWR) of 6,000 pounds or less. (The manufacturer finds the GVWR using the government's method. You don't get to find a personal GVWR using people you select or your own cargo weights.)

## Electing Out

Remember, bonus depreciation is the default depreciation method. If you don't want to use bonus depreciation, you must elect out. To elect out, attach a statement to your tax return that states something such as the following.<sup>10</sup>

### Election Out of Additional First-Year Depreciation Under IRC Section 168(k)(7)

Taxpayer name and taxpayer ID number  
Taxpayer address  
Tax year ending

Taxpayer elects under IRC Section 168(k)(7) to not claim the additional first-year bonus depreciation deduction for five-year property placed in service during the tax year ended December 31, 2018.

## Takeaways

If you bought a 2018 or 2019 luxury limited vehicle, the first thing you need to look at is your five-year property and how much of it you placed in service in 2018 or will place in service in 2019. You can elect out of bonus depreciation for all your five-year property, but you may not pick and choose assets.

Remember, for bonus depreciation in a property class, you are either all in or all out. In other words, you use bonus depreciation either on all assets in the class or on none of the assets in the class.

And if you want out, you need to elect out by attaching a statement to your tax return. You can use the sample statement above as a guide.

If you are in on the bonus depreciation of a vehicle that's subject to the luxury auto limits, make certain that you don't claim Section 179 expensing for that amount. As you saw above, that would give zero depreciation for each of the five years following your mistake.

And finally, you have to thank the IRS for its luxury auto bonus depreciation safe harbor because without it, you could claim bonus depreciation this year and then be surprised by no depreciation for the next five years. Had this happened to you, you likely would have been outraged by such an anomalous result.

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<sup>1</sup> Rev. Proc. 2019-13, Section 4.01.

<sup>2</sup> Merriam-Webster's Collegiate Dictionary, Eleventh Edition, p. 51.

<sup>3</sup> Rev. Proc. 2019-13, Section 4.04(1).

<sup>4</sup> IRC Section 280F(a)(1)(B)(ii) 2018.

<sup>5</sup> Rev. Proc. 2019-13, Section 4.04(2).

<sup>6</sup> IRC Section 168(k)(2)(A)(ii).

<sup>7</sup> IRC Section 168(k)(7) 2018.

<sup>8</sup> Rev. Proc. 2018-25.

<sup>9</sup> IRC Section 280F(d)(5)(A)(ii) 2018.

<sup>10</sup> Reg. Section 1.168(k)-1(e)(3)(ii) refers you to IRS Form 4562 for the election, and this form then sends you to IRS Publication 946. When you get off this merry-go-round, you find no help from the IRS and need to create your own election, such as the one in this article.