Maximizing Deductions for Business-Use Vehicles

How would you like to squeeze more time out of your busy week, cut down on record-keeping duties, and reduce piles of paperwork and old receipts? The optional standard mileage rates for business vehicles can help you do just that. Businesses that operate up to four vehicles at the same time can deduct this standard mileage rate rather than keeping track of depreciation, gas, and repairs.

The standard business mileage rate for 2023 is 65.5 cents-per-mile. The business rate reflects, among other things, gasoline, depreciation, and maintenance costs each year. The standard business mileage rate for 2022 was 62.5 cents-per-mile for miles driven on or after July 1, 2022 and 58.5 cents for travel between January 1 and June 30, 2022.

Four or more vehicles. Businesses using no more than four vehicles for business purposes can use the business standard mileage rate. Generally, the IRS prohibits taxpayers from using the business standard mileage rate to compute the deductible expenses of five or more vehicles the taxpayer owns or leases and uses simultaneously, such as in a fleet operation.

Depreciation. The depreciation component of the business standard mileage rate is 28 cents-per-mile for 2023 and 26 cents-per-mile for 2022 and 2021. Businesses that use the standard mileage rate are not allowed to take actual depreciation deduction amounts, even if they are higher than the depreciation component. Before deciding to use the standard mileage rate, a look at whether you will do better under the actual expense method, which includes actual depreciation, should be considered. Especially for circumstances in which Code Section 179 expensing and/or bonus depreciation is available; taking actual expenses, including actual depreciation, may be worth the effort.

Luxury vehicle caps. If depreciation is taken on a business vehicle, Congress wanted to be sure that vehicles selling above a certain price point did not enable their owners to take a larger write-off because of that premium cost. The "luxury vehicle" limits are designed to do just that, although taxpayers may debate the price points above which Congress set the "luxury" level. For example, the maximum depreciation deduction for passenger automobiles and for trucks and vans first placed in service in 2022 (for which no first-year bonus depreciation applies) is $11,200 for the first year and $18,000 for the second year.

Bonus depreciation. Bonus depreciation may be added to the available first-year deduction allowed on the purchase of a vehicle used for business if certain criteria are met. The vehicle must be new and placed in service before January 1, 2027. For most vehicles (those that are not fully depreciated in their first-year after applying the cap), business taxpayers claiming bonus depreciation are allowed an additional $8,000 in first year depreciation over and above the $11,200 first-year limit.

Section 179 Deduction. A new or used vehicle may qualify for expensing under Code Sec. 179 in the tax year that it is placed in service if business use of the vehicle exceeds 50 percent. However, the sum of the section 179 expense deduction and regular first-year depreciation deduction (including any bonus depreciation) cannot exceed the applicable first-year depreciation cap for that vehicle.

Personal and business use. If you use your business vehicle for personal trips (including commuting back and forth from home and your principal business location) you must pro-rate your deduction to exclude the percentage of personal use. The magic number here is 50 percent. As long as you use your vehicle more than 50 percent for business during the year, you can pro-rate your deduction. You also have the option of using the standard mileage rate, based on miles of business use for the year times the prescribed rate.

Please consult your tax advisor for how these rules may impact you specifically. Your individual circumstances may require further analysis or consideration of how these rules interact with other elements of your overall tax situation.