Code Section 179 (small business) expensing election

Under currently available 100% bonus depreciation, the entire cost of eligible assets placed in service before calendar year 2023 can be written off in the placed in service year (the bonus depreciation rate phases down to zero from 2023 to 2027). However, I wanted to remind you about the rules for an election under Code Sec. 179 to immediately expense certain assets. There is considerable overlap, but not complete overlap, between the Code Sec. 179 election and 100% bonus depreciation. So assets that aren't eligible for one of the benefits may be eligible for the other benefit.

Summary of Code Sec. 179 election.

Generally. The election is available on a tax year by tax year basis subject to a dollar limit.

Qualifying property. To qualify for the election, the property must generally be tangible personal property. This means that generally real estate (buildings and most land improvements) and intangibles (such as patent rights) don't qualify. Nevertheless, the following types of property also qualify: (1) real property that is qualified real property (which includes many internal, and some external, nonresidential building improvements), and (2) non-customized computer software available to the general public. Also, to qualify, property must be "purchased." Thus, you acquired the property in certain tax-free transactions, by gift or inheritance, or from an individual or entity to which you bear a close relationship, the property does not qualify.

Dollar limit. The annual deduction limit is $1,080,000 for tax years beginning in 2022 ($1,160,000 for tax years beginning in 2023) subject to a phaseout rule (see below). The dollar limit doesn't mean the election can't be made for property costing more than that amount. For example, if you place into service a qualified real property project in 2022 for $1.2 million you can elect to immediately deduct $1,080,000 of its cost for that year if the phaseout rule (see below) doesn't apply. Also, you can make the election for all or part of the costs of an unlimited number of assets as long as the total cost covered by the election doesn't exceed the dollar limit for the year as modified by the phaseout rule.

Phaseout rule. Under this rule the deduction is phased out (gradually reduced) if more than a specified amount of qualifying property is placed in service during the tax year. The specified amount is $2,700,000 for tax years beginning in 2022 ($2,890,000 for tax years beginning in 2023). For example, if you place in service $2,800,000 of qualifying property in 2022, you can make the expensing election for no more than $980,000 of property ($1,080,000 limit minus $100,000 phaseout [excess of $2,800,000 over $2,700,000]).

Taxable income limit. If your taxable income from all of your trades or businesses is less than the dollar limit for that year, the amount for which you can make the election is limited to that taxable income. However, any amount you can't immediately deduct because of the taxable income limitation is carried forward and can be deducted in later years (to the extent that the applicable dollar limit, the phaseout rule, and the taxable income limit permit).

Recapture. If you dispose of the property, or stop using it in a trade or business, before the end of the cost recovery period that would have applied to the property had you not made the election for the property, all or part of the amount of the deduction you claimed under the election must be taken back into income (“recaptured”). Exactly how much will depend on the type of property and how long you used the property in a trade or business.

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.