

Tax Planning Tip: Bonus Depreciation and Year-End Asset Purchases

The October 15, 2020, filing deadline has passed and thoughts turn to year-end tax planning. Normally, as businesses look toward year end, business owners review their fixed asset purchases made year-to-date and consider making additional purchases prior to December 31, 2020. Immediate expensing of some asset purchases for tax purposes, either through Section 179 expensing or bonus depreciation, is often thought of as the preferred approach to accelerate the deduction for tax purposes. Everyone likes a deduction in the current year; however, this could be the year to consider another approach.

Let us begin with a few reminders on the tax depreciation concepts. For the 2020 tax year, with total qualified Section 179 property purchases up to \$2,590,000, the federal Section 179 maximum deduction is \$1,040,000 (\$1,075,000 for qualified enterprise zone properties), and applies to both new and used equipment purchases. For the 2020 tax year, federal bonus depreciation is 100% and is also applicable to both new and used equipment purchases with no limit on the amount of bonus depreciation utilized. While most businesses focus on the federal impact of tax elections, the state impact is another important piece which varies from the federal treatment and also varies state-by-state. As with any tax law, there are additional rules which are applicable and make one method of expensing some fixed asset purchases more appropriate than the other.

The 2020 tax year has a variety of factors to consider when determining whether a Section 179 depreciation deduction, bonus depreciation deduction, or the timing of the year-end asset purchases, is the better choice for a business. Below are a few items to consider before making a decision:

- How much federal tax depreciation is still available to be utilized on prior year purchases? As a reminder, when reviewing company financial statements, the book depreciation on prior year purchases included in the financial statement can vary significantly from the tax depreciation utilized in the calculation of taxable income.
- How has the COVID-19 pandemic impacted the business's income for 2020? If your income is lower than expected in future years, what is the projected timeline to return to higher profitability?

- If the business received a Paycheck Protection Program (PPP) loan, will the business apply for forgiveness for all or a portion of the loan?
 - If so, what amount of the loan forgiveness is expected to be approved?
 - If so, when is the loan forgiveness application expected to be approved?
- How will the results of the November election potentially impact the expected tax policy for the next few years?
- In closely held businesses, what other factors in the owners' financial situations impact their overall taxable income for 2020 and future years?
- When contemplating future fixed asset purchases and investments, is the equipment needed and what are the long-term cash flow impacts of the investments?
- What is the supply chain of available equipment and should the purchase be initiated quickly to guarantee delivery by year end?
- Is the business considering an ownership change?
- How do the tax depreciation elections interact with other tax elections?

When considering the above factors and others, there are situations where saving the tax deduction for future years by delaying asset purchases until January 2021, or not accelerating the tax depreciation in 2020 on assets already purchased, is the most beneficial tax strategy. Alternatively, there are situations where utilizing the tax deduction in 2020 is the most beneficial tax strategy. While no one can predict what 2021 holds, making an educated decision considering the specifics of your tax situation is the best way to proceed.

Discussions on possible election outcomes and timing of fixed asset purchases are important factors to consider in overall tax planning.

Contact your ACT client service representative with questions about the best approach for you and how it might impact your business, or email us at info@actcpas.com.