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Tax and Accounting

05

Vehicle Deduction

Strategies & Tips

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Tax and Accounting

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Two-Vehicle Tax Deduction Strategy:

Do you have two or more cars in your household? If your circumstances are right, we might find a hefty increase in deductions for you with the two-car strategy.

If this strategy works for you, you don't have to drive one mile farther. You don't have to spend one additional penny. All you need are the right circumstances and a desire to increase your tax deductions (which I's sure you have).

If you have two or more vehicles in your household, please put together the following information for each vehicle:

1. *Business miles for each vehicle*
2. *Total miles for each vehicle*
3. *Cost of each vehicle (you can estimate this)*
4. *Estimated sales proceeds when you plan to sell the vehicle*

That's it. With the above numbers, I can show you the approximate dollar benefit, or detriment, you would have by using two vehicles in your business.

02

Classic Car Strategy:

How does the tax law treat the classic or antique car when you use it for business? Can you deduct it just as you would any car you use in business?

To deduct the classic, or antique car:

- The car must be of a type that's subject to wear and tear, decay, decline, or exhaustion; and,
- The car must be used in your trade or business.

According to the courts, this language is unequivocal (i.e., it allows for no doubt or misinterpretation).

Example. You drive a 1972 GTO in the course of your business. You obviously subject that car to wear and tear, decay, and exhaustion. Because you are driving it for business, you have a tax-deductible 1972 GTO.

In 1981, lawmakers simplified depreciation deductions and removed the requirements of "salvage value" and "estimated useful life," both of which could have prevented your write-off of the GTO.

Today, you can thank the Tax Cuts and Jobs Act (TCJA) for making the money equation easy. Under the TCJA, you encounter no depreciation differences between, say, a 2019 Lexus GS and the 1972 GTO. That's because the TCJA uses the same depreciation schedule for both new and used cars.

If you would like to add a classic or antique car as a business vehicle, we should spend some time planning to make sure you know all that's involved and what records you need to keep.

03

How to Deduct Your Business Motor Home:

Sounds too good to be true, doesn't it? But it isn't. Before you rush out to purchase a $250,000 motor home, lets take a step back and touch on some things that are of great importance here.

The courts have wrestled with this question for years. Instead of providing you hundreds of pages of confusing legal jargon, I've summarized some important things to know below.

You must have a bona fide business purpose and keep good records (both mileage AND nights) to protect your motor home deductions.

• Keep a mileage log for every personal and business use of your motor home. Make sure you have more than 50 percent business miles.

• Keep a record of every night you use the motor home for personal or business lodging. Make sure you have more than 50 percent business nights (mileage for investment, personal, or commuting purposes is not counted as business mileage).

• Don't claim Section 179 expensing on the motor home. The IRS could likely claim transient use (average rental of less than 30 days) and challenge this expense. Don't subject yourself to this.

• Stay with MACRS depreciation to avoid extra IRS audit attention and the possible loss of the Section 179 deduction under the lodging rules. And remember, with depreciation, you get 71.2 percent of the deductions in the first three years anyways! In Hoye, the courts ruled that depreciation expense is not considered "lavish and extravagant."

Say you bought a $250,000 motor home on May 1, 2019 and you used it 100 percent for business. With Section 179 expensing, you could deduct the entire $250,000 in year 1. With MACRS depreciation, you depreciate the motor home using the tax law five-year depreciation table as follows:

Year 1: $50,000 (20 percent of $250,000)
Year 2: $80,000 (32 percent of $250,000)
Year 3: $48,000 (19.2 percent of $250,000)
Year 4: $28,000 (11.52 percent of $250,000)
Year 5: $28,000 (11.52 percent of $250,000)
Year 6: $14,400 (5.76 percent of $250,000)

• Keep IRC Section 290(f)(4) top of mind. Why, you ask? This section of the tax code says that your use of the motor home for overnight business lodging produces business deductions for business travel and that business travel is not subject to the vacation home rules.

• And finally, at all costs, avoid using your motor home as an entertainment facility, or for

04

Title to You, Expense to the Corporation:

You may have started a new corporation, and that's why the vehicle title is in your name. Or perhaps you already operate as a corporation but face a situation where it's better to buy an asset in your personal name rather than in the corporate name. This could be because of legal issues, financing terms, insurance rates, or any number of other reasons.

If title is in your name, can you still use Section 179 and Bonus Depreciation to deduct the cost of the asset? Absolutely – but you need to do this the right way.

The Right Way

To achieve the full deduction for the vehicle, you want the corporation to reimburse you for the vehicle expenses. This is true regardless of your method of deduction (mileage rates or actual expenses).

When the corporation reimburses you, then the business expenses and deductions move to the corporate return. You have the money in your pocket as a non-taxable reimbursed employee expense, and the corporation has the deductions.

If you operate your business as an S corporation, then the expenses and education pass through to you as the sole shareholder of the corporation.

Reimbursements from the Corporation

A corporation can reimburse an employee for all expenses allowable under Sections 161 to 199 of the tax code – which includes Section 179 expensing and bonus depreciation.

Here's what happens when your corporation properly reimburses you for the expenses:

1. You as the employee do not have taxable income.
2. The corporation gets the full deduction the law allows for the expenses.
3. If the corporation is an S corporation, then those expenses reduce the corporate income and the corporation passes that reduced income to you – say, as the sole shareholder of your S corporation.

Technical note for the tax geeks. Section 179 does not require the S corporation to obtain title to the property to expense it. Section 179 requires only that the corporation incur the cost for the qualifying property that is predominantly used in the conduct of the business. Private Letter Ruling 200930029 does a good job of explaining this IRS-endorsed reimbursement of Section 179 expenses.

Document Your Reimbursement

To properly move the expense to the corporation, you have to do some paper shuffling.

First, your corporation needs to have an official accountable plan (I can help with this), which can be as simple as requiring timely expense reports or a document stating that the corporation allows reimbursement of certain employee expenses. During the year, you will generally list your vehicle operating expenses on the expense report.

This expense report must include

- A receipt for the vehicle purchase that shows your ownership and the cost of the vehicle.
- A statement of recognition by you that the reimbursements of Section 179 expensing and/or bonus or other depreciation reduce the basis in your vehicle for purposes of gain or loss.
- A statement of recognition that you will reduce the overall annual Section 179 limits that apply to you and your spouse on your personal tax return by the amount of Section 179 expensing reimbursed by the corporation to you.
- A statement of recognition by you that if business use of the vehicle drops to 50 percent or less, you will reimburse the corporation for the required recapture of deductions in excess of straight-line depreciation (this requirement disappears when the five years have passed or when you sell or trade the vehicle).
- A mileage log that proves your percentage business use of the vehicle.

To assist with your submission of the vehicle expenses to the corporation as in the bullets above, consider using our sample enhanced expense report for a personally owned vehicle.

A Note on the Mechanics

The Section 179 deduction does not separately show on either the corporate or the personal tax return. It is a reimbursement of an employee expense.

On the corporate return, you have two choices for labeling the reimbursed vehicle expenses in the other deductions section:

1. Vehicle expenses
2. Employee reimbursed expenses

Remember. The employee reduces his or her basis in the vehicle by the amount of the deduction and faces recapture if the business use declines to 50 percent or below.

Takeaways: Wow! You can buy the business vehicle in your personal name and have the corporation reimburse you just as if the corporation had purchased the vehicle.
You need the corporate reimbursement of:

- Operating expenses, following the general requirements for an accountable plan; and
- Section 179 expensing, bonus depreciation, and MACRS depreciation in an enhanced expense report.

When having your corporation reimburse you for Section 179 expensing and/or depreciation, consider using our sample enhanced expense report for a vehicle, where you:

- Certify business use.
- Recognize the Section 179 limits.
- Decrease your vehicle's basis by the Section 179 deduction.
- State that you will keep your business use at more than 50 percent for the required period or reimburse to the corporation any tax-law-required recapture of Section 179 expensing or depreciation deductions.

05

Purchase The Vehicle You Currently Lease:

Before the Tax Cuts and Jobs Act (TCJA), your purchase of the vehicle you were leasing did not qualify for either Section 179 expensing or bonus depreciation.

But times have changed.

The TCJA made two changes that mean 100 percent bonus depreciation is available on the vehicle you lease and then purchase, regardless of whether you purchase it during the lease term or at the end of the lease. The two technical reasons you can do this are as follows:

1. *During the lease, you had no depreciable interest.*

2. Bonus depreciation is now available on used property.

Technically, the two changes work like this:

- *While you were leasing the vehicle, you had no depreciable interest in the vehicle. The lessor depreciated the vehicle. You, the lessee, paid rent.*
- *Your purchase of the vehicle that you were leasing is the purchase of a vehicle that you had NOT used under the bonus depreciation law, because you did not have a depreciable interest in it at any time.*

Example. *You pay $32,000 for a pickup truck that you have been leasing for business purposes. The pickup truck has a gross vehicle weight rating of 6,531 pounds, and your mileage log proves 90 percent business use. You may use bonus depreciation to deduct the $28,800 business cost of the pickup ($32,000 x 90 percent).*

Note the difference: *As with prior law, with Section 179 expensing, you get no additional deductions. But with bonus depreciation, you can expense your entire business cost.*

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