Panel Supplement: Bonus Depreciation & Biden Tax Proposals

Steve Pierson, CPA, Selden Fox

Bonus Depreciation Update

Bonus depreciation applies at a 100% rate. However, the rate is scheduled to be phased down to zero in 20% steps from 2023 through 2027.

The basis of the qualified property is reduced by the amount of bonus depreciation allowed or allowable, whichever is greater. When the bonus depreciation rate is less than 100%, the remaining adjusted depreciable basis of the qualified property is depreciated using the applicable depreciation provisions of the Code. If bonus depreciation is available for an asset for regular tax purposes, there is no alternative minimum tax adjustment for either the bonus depreciation or regular depreciation for the asset (even if the taxpayer elects to decline bonus depreciation). In effect this replaced the ability to avoid tax on sale of personal property on like kind exchanges under1031.

Qualified property eligible for bonus depreciation is, subject to some exclusions, property that (1) is modified accelerated cost recovery system (MACRS) property with a recovery period no longer than 20 years, computer software, water utility property, or a qualified film, television or live theatrical production, (2) the original use of which begins with the taxpayer or is property that meets a qualifying acquisition test (used property purchased from unrelated parties),

Alternative to bonus depreciation: A taxpayer is allowed to expense, instead of capitalizing and depreciating, all or part of the cost of Section 179 property.

There are significant differences between the Section 179 expense deduction and bonus depreciation in their operation. One of the two major differences is that Section 179 expensing isn't limited by a legislatively-provided termination date; in contrast, bonus depreciation is scheduled to be phased out. The other major difference is that Section 179 expensing is subject to annual dollar and taxable income limitations that don't apply to bonus depreciation.

Other differences include, but aren't limited to, some differences in the property eligible for each of the benefits. Taxpayers generally benefit by electing the Section 179 expense deduction or claiming bonus depreciation as each increases the present value of the tax savings from depreciation by accelerating deductions to the current tax year.

The dollar limit for the total cost of Section 179 property that a taxpayer can elect to expense for a tax year is $1 million, subject to adjustment for inflation ($1,050,000 for tax years beginning in 2021). However, the dollar limit is reduced on a dollar-for-dollar basis if the Section 179 property placed in service by the taxpayer during the tax year exceeds $2.5 million, subject to adjustment for inflation ($2,620,000 for tax years beginning in 2021) (the threshold amount). Section 179 expensing for many sport utility vehicles (SUVs) is limited to $25,000, subject to adjustment for inflation ($26,200 for tax years beginning in 2021).

Highlights of Biden Tax Proposals

28% corporate income tax rate (currently 21%) beginning in 2022 including the portion of income in 2022 of fiscal years (non-calendar years).

15% minimum tax on book earnings. Would apply only to corporations with book income in excess of $2 billion (the tentative tax is reduced by general business credits and FTCs).

Possibly a 15% global minimum tax.

39.6% top marginal individual income tax rate. For 2022, would apply to those reporting taxable income of more than $509,300 (married filing jointly); $452,700 (unmarried); $481,000 (head of household); $254,650 (married filing separate).

Ordinary tax rates on long term capital gains and qualified dividends for taxpayers with AGI of more than $1 million. Effective retroactively to date of announcement (unclear whether date of The American Families Plan (April 28, 2021) or The Green Book release (May 28, 2021)).

Gift or death transfers of appreciated property as realization event that requires gain, subject to a $1 million lifetime exclusion. Exclusion also would apply for transfers to spouse.

Like-Kind Exchanges: Repeal, but would establish an exclusion of $500,000 ($1 million for married filing jointly) each year for real property exchanges.

Carried Interest: Would be ordinary income (currently treated as capital gain if held 3 years) and subject to self-employment tax.

Excess Business Losses – Section 461(l): Make permanent (currently due to expire in 2027).

All pass-through business income (S corporations, partnerships) over certain thresholds (not specified) would be subject to 3.8% Medicare tax or NIIT.