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ACCELERATED ASSET BASIS RECOVERY – NOT FOR EVERYONE

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Most taxpayers want the immediate tax deduction that various methods of accelerated asset basis recovery afford. Accelerated asset basis recovery can be in the form of bonus depreciation (now increased to 100% post September 27, 2017), § 179 expensing, or just the quicker tax depreciation inherent in the Modified Accelerated Cost Recovery System ("MACRS") defined in the Internal Revenue Code.

However, it might behoove certain taxpayers to forgo the benefit this year for a chance at either a bigger benefit in future years or, instead, to use loss or credit carryforwards, with a looming expiration. Below are a few examples of when more depreciation today might not be the best idea:

1. <u>When you expect a gain on the asset sale in the near future.</u> Tax depreciation taken in prior years could potentially be recaptured as ordinary income if the asset is sold. If a piece of equipment is sold at a gain, generally the business property will be taxed at an ordinary rate up to the depreciation taken. The gain in excess of the asset basis not recovered through depreciation, will be a § 1231 gain, taxed at a capital gain rate (assuming no past §1231 losses to recoup). Additionally, in the example of business use of a building, part of the gain on sale could qualify for §1250 gain, taxed at a 25% maximum capital gains rate.

2. <u>When you have a net operating loss ("NOL") that needs to be utilized before expiration</u>. Not only could an expiring NOL be a case for electing out of bonus depreciation, a taxpayer should consider electing the alternative depreciation system (ADS) rather than MACRS to slow down depreciation deductions. Doing so will allow the taxpayer to utilize the NOL and preserve future deductions in the basis of its assets.

3. <u>When you have tax credits that need to be used before they expire</u>. In certain tax years, Alternative Minimum Tax (AMT) credits can be monetized if bonus depreciation is not taken. In addition, other general business credits like Research and Development Credits (R&D) can potentially be utilized if there is sufficient tax liability. This is another example of how taking tax attributes into consideration can result in an overall more efficient tax answer.

4. <u>If you expect to be in a higher tax rate bracket later</u>. A taxpayer may want to save deprecation for when it gets a bigger bang. Reducing taxable income next year may be more important than this year, if the taxpayer expects much more taxable income taxed at a higher tax rate in the future.

Popeye's friend, Wimpy, had the tagline, "I'll gladly pay you Tuesday for a hamburger today." Alas, with tax planning one often needs to think about the effect of getting the hamburger today.

If you have questions about a business or tax issue, please contact your Account Manager or Helen Floros, CPA, at (314) 205-2510 or via email at hfloros@connerash.com.