Vehicles = Moving Deductions

Here's how to benefit from changes in the tax law.

BY JAMES D. KRICKETT

Thanks to last December's Tax Cuts and Jobs Act (TCJA), those podiatrists with vehicles in their practice or provided by the practice, are finding it easier than ever to write off the cost of buying and maintaining them. Many small businesses and professional practices are taking advantage of these new rules with the National Federation of Independent Businesses (NFIB) recently reporting 61% of businesses surveyed have made capital outlays, with 43% spending them on equipment and 27% on vehicles.

Knowing how and when to deduct the cost and expenses of the vehicles used in the podiatric practice can have significant tax implications. It pays to understand the nuances of all costs associated with the practice's vehicles, including the revamped mileage deductions, buying versus leasing, and writing off the cost of newly acquired vehicles.

Business Use

A podiatric professional or practice can write off the expenses of a business-owned vehicle and take a depreciation deduction to reduce the out-of-pocket cost. Only the portion of the vehicle use that is for business purposes can, however, be counted when determining tax deductions.

The tax rules permit deductions at a standard mileage rate or for the actual expense incurred during the business use of the vehicle. Using the mileage rate deduction means using an amount calculated based on mileage used.

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Costs by the Mile

The 2019 tax year began with new deductible mileage rates for vehicle usage. According to the IRS, the standard deduction rate for using a car, van, pickup or panel truck for business purposes is 58-cents per mile, up 3.5-cents from the rate for 2018.

The standard mileage rate can also be used for leased vehicles. Of course, if the standard mileage rate is used, switching to the actual expense method in a later year is a no-no. And, if the standard mileage rate is used for a leased vehicle, the lease payment amount is not deductible.

While every podiatric practice, or at least those with fewer than five vehicles, can utilize the business standard mileage rate, using the actual cost of operating a vehicle or vehicles for business purposes is frequently more advantageous, especially for individuals.

Actual Expense Reality

A deduction for the actual expenses of operating a vehicle for business includes costs such as depreciation, licenses, gas, oil, tolls, insurance, parking, registration, maintenance and repairs. If the vehicle is used for business and personal use,

Continued on page 162

Vehicles (from page 161)

deductions and depreciation apply only to the business-use portion.

If the practice vehicle is financed with a loan, the payments are not considered a business expense. The interest on that loan is, obviously, deductible by the practice. In addition to interest payments, deducting the actual expense of operating the vehicle used in or provided by the podiatric practice is an alternative.

The First Impact of Reform

The TCJA suspended all miscellaneous itemized deductions that are subject to the two-percent of adjusted gross income floor on Form 1040. This change affects un-reimbursed employee expenses such as home offices, union dues, and the deduction for business-related meals, entertainment and travel. In other words, the standard mileage rate can no longer be used to claim an itemized deduction for un-reimbursed employee business expenses... at least until 2026.

Writing It Off

When it comes to writing off the cost of passenger autos, trucks, and vans first placed in service during calendar year 2019, there are caps on the amount that can be deducted under the so-called "luxury" car depreciation rules.

If, for example, the practice doesn't claim bonus depreciation, the greatest allowable depreciation deduction was:

$10,000 for the first year,
$16,600 for the second year,
$9,600 for the third year, and
$5,760 for each taxable year later in the recovery period.

Faster Write-Offs Courtesy of the TCJA

As mentioned, the 2017 tax law changes, the TCJA, made it easier to write off the cost of buying equipment such as vehicles. The TCJA offered a number of options for deducting vehicle costs immediately in lieu of regular depreciation.

Section 179

The rules for the Section 179, first-year expensing have, for instance, been expanded. Expensing, which must be chosen, has traditionally been intended for buying equipment and machinery, whether new or used; vehicle costs also qualify.

The cost of qualified property that could be expensed in 2018 was $1 million (up from the $510,000 limit in 2017), as well as a $25,000 limit for buying heavy SUVs. Similar limits will likely apply in 2019. However, the $1 million limit phases out once total investments for the year exceed $2.5 million. The phase-out is dollar for dollar, limiting total investments to $3.5 million for even a portion of Section 179 expensing.

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A Business Write-Off

There is now a silver bullet called "bonus depreciation." Another first-year write-off, "bonus" depreciation is another way to write off the cost of vehicles and other property in the year purchased and placed in service.

Today, bonus deprecation applies to 100% of the cost of qualified property, whether new or used... with no limit. What's more, bonus depreciation applies automatically unless the podiatric practice chooses to opt out.

Should the practice or self-employed podiatrist claim the 100% bonus depreciation, the greatest allowable depreciation deduction is:

$18,000 for the first year,
$16,000 for the second year,
$9,600 for the third year, and
%5,760 for later years in the recovery period.

These limits are adjusted for inflation and may increase for the 2019 tax year.

The SUV Loophole

SUVs with a gross vehicle weight (GVW) rating above 6,000 lbs. are not subject to depreciation limits. They are, however, limited to a $25,000 deduction. Of course, no depreciation or Section 179 limits apply to SUVs with a GVW of more than 14,000 lbs.

While newly-purchased SUVs remain subject to the $25,000 limit, both new and used vehicles are eligible for 100% bonus depreciation if they are above 6,000 lbs. A practice purchasing a passenger automobile subject to these limitations should consider the impact of taking bonus depreciation on future depreciation deductions. Fortunately, a self-employed podiatrist or practice can choose to apply a 50% allowance instead of the 100% allowance.

Leased and Limited

Leased vehicles are not depreciated. Instead, only the business portion of the lease payment is deducted. The latest IRS rules contain lease inclusion tables for passenger automobiles with a lease term beginning in 2018. Because of the higher depreciation caps, this table starts with vehicles valued at $50,000 or more.

What's more, a leased vehicle is not, technically, a purchase of the vehicle. With a lease, the payments are an expense and depreciation can be ignored. The lease payment is used as a deduction when claiming the actual vehicle expenses, but cannot be used as a deduction if the standard mileage rate deduction is used.

Unfortunately, despite the new generous dollar limits, expensing continues to be limited to the podiatric practice's taxable income. In other words, if a practice buys %75,000 of new vehicles, but has only $50,000 in income, the expensing deduction is limited to $50,000, although the excess can be carried forward.

New Business Vehicle Deductions—and Limits

Those podiatrists and practices using vehicles in their operations face two potential problems: the al-

Continued on page 164

Vehicles (*from page 162*)

ready-mentioned vehicle depreciation write-off limits and like-kind exchanges. Every podiatric professional and practice has long been able to swap vehicles in a like-kind exchange.

A vehicle used in the operation is turned over for a trade-in allowance and a new vehicle is purchased for the owners or employees to use. A like-kind exchange means there is no gain on the swap while depreciation is claimed on the new vehicle based on the cash paid for the new vehicle on top of the trade-in.

The TCJA removes like-kind vehicle exchanges as an option. The only property now allowed to be used in a like-kind exchange is now "real" property… which vehicles are not.

Personal Use of Employer-Provided Vehicles

As already mentioned, the TCJA suspended the deduction for miscellaneous itemized deductions that were subject to the 2% of adjusted gross income floor through 2025. This category includes un-reimbursed employee business expenses such as the cost of operating a vehicle for business purposes.

Using a practice-provided vehicle for business purposes is not considered a fringe benefit.

Many podiatric practices purchase or lease vehicles that are used by principals or employees in the course of doing business. Using a practice-provided vehicle for business purposes is not considered a fringe benefit. However, personal use such as commuting to and from work, running errands or allowing family members who are not employees of the practice to use the vehicle is a taxable fringe benefit, and the practice is responsible for withholding taxes on this benefit.

The general rule for taxing fringe benefits is that all fringe benefits are taxable to the recipient based on the fair market value (FMV), with the provider of the benefit responsible for withholding federal income taxes, FICA taxes (Social Security and Medicare), and FUTA taxes.

Personal use of employer-provided vehicles is a non-cash fringe benefit, so its value must be determined at least once a year. The FMV of the benefit is subject to tax withholding at the time that value is determined which can be once a year or even monthly. The amount may be added to the individual's regular compensation and the necessary taxes withheld.

A special accounting rule allows employers to include the value of a fringe benefit for the last two months of the calendar year with the value for the first ten months of the following year. After all, it may be the case that the value of some fringe benefits can't be determined until after the end of a month. An employer might not be able to determine the value of personal use for a vehicle provided by the practice until after the employee turns in his or her mileage logs in the following month. Thus, using mileage logs turned in during November 2019, an employer can determine the value of personal use for the period November 1, 2019, to October 31, 2020.

Employers generally have four options for valuing an employee's personal use of a practice-provided vehicle: a general valuation rule, the automobile annual lease valuation rule, the cents-per-mile rule, or the commuting valuation rule.

• The general valuation method is determined by the cost an individual would incur to lease the same vehicle under the same terms in the same geographic area.

• To use the annual lease value method, multiply the annual lease value of the vehicle by the percentage of personal miles driven. The result is the FMV of the employee's personal use of a practice-provided vehicle.

• Using the cents-per-mile method, the FMV is determined by multiplying the IRS's standard business

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mileage rate (58 cents per mile for 2019) by the number of personal miles driven. However, two conditions must be met in order for this method to be used: (1) the vehicle must have been driven at least 10,000 miles annually and the FMV of the vehicle when first put into service cannot exceed the "luxury car" limits covered above.

• The continuing value method is calculated by multiplying the number of trips by either $1.50 (one way) or $3 (round trip). Here too, there are restrictions such as the vehicle owned or leased by the podiatric practice and provided to the employee must be for use in conjunction with the business or practice. Employees must be required to commute to and from work and adhere to a written policy prohibiting employees (and their families) from using the vehicle for personal use other than commuting to and from work. And, most importantly, no highly compensated or part owner of the practice can use this method.

Although the maximum values were earlier calculated separately for trucks and vans first made available for personal use, they currently do not have separate maximum values.

Practice-Provided Vehicle Challenges

Naturally, any podiatric practice providing vehicles to principals and

Continued on page 165

Vehicles (from page 164)

key employees faces a number of potential trouble spots. Those vehicles are liable for accidents 24/7. Considering that almost one-third of crashes occur on Saturdays and Sundays, the practice assumes a substantial amount of risk during non-business hours.

Those practice-provided vehicles can require a large, upfront capital cost. Despite the many tax breaks to reduce the out-of-pocket cost, expenditures are still required. Up-front expenses can be reduced by leasing vehicles rather than purchasing but remember leases must now be shown on the practice's financial statements as a liability.

Employees are often allowed to drive practice—or business-owned vehicles outside of work without insight into how often they are using it for business or personal reasons. This lack of oversight can expose the practice or business to risk of an audit and increased costs.

Every business and practice is required to report personal use of owned or leased vehicles as a fringe benefit. Inaccurate records could lead to penalties or back taxes in the event of an audit.

Records

Every podiatrist planning to take a deduction for vehicles used in or by the practice should keep a detailed log of business miles and other expenses related to the vehicle's use. The best way to prove business use is with a mileage log.

While substantiating the percentage of business use is essential, the Section 179, first-year expensing deduction can only be taken up to the amount of the practice's or business's profits. Bonus depreciation is not, of course, limited by profit.

Every podiatric professional providing or using vehicles in their practice should know how and when the business use write-off is taken can have significant tax implications. It pays to learn the nuances of mileage deductions of buying versus leasing and depreciation of vehicles.

The principals in many podiatric practices will have to live and, in many cases, suffer with today's tax laws, especially the deduction limits for cars, vans, light trucks, and SUVs. Or, they might be able to write off a large part of the vehicle's purchase price in the year it is first used for business purposes, but guidance by a qualified professional is always strongly recommended. **PM**

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