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Tax Savings for Married Taxpayers Claiming Section 179 Deductions

If you are married, you need to know three special rules that can benefit your Section 179 deductions:

1. The Section 179 business income limit includes W-2 income earned by both you and your spouse.

2. Section 179 expensing treats you and your spouse as one taxpayer.

3. If you and your spouse file separate returns, you need to make an overt election of how you are going to share your Section 179 deductions.

The W-2

For Section 179, among other purposes, employees are engaged in the active conduct of the trade or business of their employment.[1] Thus, wages, salaries, tips, and other compensation derived by a taxpayer as an employee count as income for the business income limit on Section 179 expensing.[2]

Example. You have business income of $10,000 and qualifying Section 179 expenses of $90,000. Your spouse has W-2 income of $50,000. Your husband-and-wife business income limit for Section 179 expensing is $60,000 ($10,000 plus $50,000).

If you elect to expense the entire $90,000, you deduct $60,000 this year and carry the $30,000 excess over to next year, where it again enters into a Section 179 computation.[3] You may carry over the excesses to any number of years, without limit.[4]

Planning point. Taxpayers and tax professionals periodically miss this combination because the words "business income" do not trigger thoughts of all the income this involves.

Husband and Wife Are One Taxpayer

If you file a joint return, tax law treats you and your spouse as one taxpayer for purposes of applying the Section 179 limits.[5]

Separate Returns

If you and your spouse file separate returns, you must first treat yourselves as one person for Section 179 ceilings and limits.[6] This is step 1.

Step 2 triggers the need for a decision. You and your spouse may elect how you want to handle the allocations in your tax returns. If you do not make a formal election, the law makes a 50/50 allocation for you and your spouse.[7]

Example. You are married and place in service $65,000 of qualifying Section 179 property during the year. With elections on separately filed returns, you and your spouse may choose how to allocate the $65,000. You could take it all, give it all to your spouse, or take $55,000 and give $10,000 to your spouse. If you don't choose, the law gives each of you $32,500 (half of $65,000).

Planning note. Separate tax returns usually are a bad idea. Joint returns almost always put more tax dollars in your pocket than separate returns do, although with the COVID-19 tax rules, there are more opportunities for separate returns.

Also, with the joint return, you do not have to think about and then make an allocation of Section 179 expensing—hence, less paperwork and headache.

Takeaways

If your Section 179 deduction is larger than your Schedule C net income or the income passed through to you by your S corporation or partnership interest, make sure to consider the W-2 income reported by you and your spouse as a means of obtaining the full Section 179 deduction to which you are entitled.

Key point. W-2 income is business income for purposes of the Section 179 deduction.

And if you are married filing *separate* tax returns, make sure to allocate your Section 179 deduction to create the best tax benefits for you and your spouse.

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1 Reg. Section 1.179-2(c)(6)(iv).
2 Ibid.
3 Reg. Section 1.179-3.
4 Ibid.
5 Reg. Section 1.179-2(c)(7).
6 IRC Section 179(b)(4)(A).
7 IRC Section 179(b)(4)(B).