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What is *Bonus Depreciation?*



What It Is

Bonus depreciation allows a business to write off the full cost of qualifying property in the first year it is put into use (instead of spreading it over many years). The total write-off amount stays the same; it is just accelerated. A deduction normally spread over 5 to 15 years is applied all at once, and the property's tax basis drops accordingly. An investor with a large passive gain, such as from selling a rental property, may look at this to offset it in the same tax year. The rule is in Section 168(k) of the tax code.

It has been in the code since 2002, previously with an expiration date and a declining benefit schedule. Legislation passed in July 2025 removed the expiration and set the deduction at 100 percent for property acquired and put into use after January 19, 2025.

Key Takeaways

Under current law, the deduction applies at 100 percent, with no expiration date, for qualifying property acquired and put into use after January 19, 2025.

A fund that borrows can purchase more property or other assets, so an investor's share of the deduction may be larger than the amount invested. How much of it an investor can use depends on the at risk rule.

The deduction defers tax to a later year and is generally recaptured at sale. These funds are illiquid, speculative and can lose value.

Which Gains Might This Address?

Investment real estate (passive)	Usually yes. Real estate gain is generally passive, and passive losses like bonus depreciation can offset it in the same year. Recapture is taxed at up to 25 percent on straight-line depreciation, or up to 37 percent (ordinary rates) on accelerated depreciation, including cost segregation components.
Sale of a business	Asset sale. It may work if the seller was a silent owner (not involved day to day), not if they were actively participating. C corp stock. No, even if the seller ran it. Gain on C corp stock is portfolio income. S corp or LLC interest. Depends. The gain is treated as a sale of the seller's share of the business, so it is passive only for a silent owner.
Publicly traded stock, ETFs and mutual funds	No. These are portfolio income, a different category that passive losses do not touch.
Income from another investment	Depends on what type of income the investment earns. Operating income and property gains from an equity fund are usually passive and can be offset. Interest from a debt or mortgage fund, along with dividends and REIT income, is portfolio income and cannot.
1031 Exchange Scenarios	Boot. Cash that was not reinvested is taxable, and passive losses can offset it if the property sold was passive. A partial or failed exchange. Bonus depreciation may defer gain and depreciation recapture from the same tax year. Part of a gain. A 1031 has to absorb all the proceeds and replace the debt. Here an investor can invest only enough to offset part of the gain.

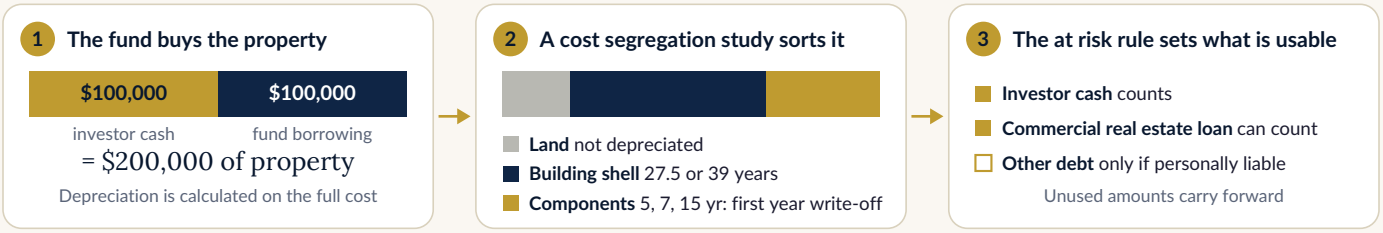
Tax situations vary and each of these has exceptions. Discuss any strategy with a CPA or tax advisor before investing.

Where It Applies

- **Real estate.** A cost segregation study, an engineering review of the building, breaks it into 5, 7 and 15 year pieces that do qualify, even though the shell itself does not. Borrowing tends to help most with real estate, as explained below.
- **Equipment leasing.** Transportation, construction, medical and industrial equipment generally fall into the 5 and 7 year classes.
- **Agricultural.** Farm machinery, grain bins, fencing, irrigation and drainage tile generally qualify, as do fruit and nut bearing trees and vines such as orange groves and pistachio orchards. Purpose built livestock and greenhouse structures can qualify too, but the rules are strict. The building generally has to be designed and used for that specific purpose. A general purpose barn, or one used for storage or processing, does not count.
- **Solar and other energy property.** Solar equipment is generally 5 year property. If the fund claims an energy investment tax credit, the amount it can depreciate is first reduced by half the credit. Under the July 2025 law, new wind and solar projects that did not begin construction by July 4, 2026 lose those credits unless placed in service by the end of 2027.
- **Oil and gas.** Applies to the equipment side of a well, things like casing, tubing, pumping units and tanks, usually 7 year property. It is separate from the intangible drilling cost deduction. See our companion white paper, Oil & Gas Drilling Funds Explainer.

Leveraged Bonus Depreciation

Depreciation is calculated on the full cost of the property, including the part paid for with borrowed money. Because most of the depreciation is used up in the first year or two, the fund's income in later years may be taxable. When the property is sold, the IRS generally recaptures the depreciation, and tax becomes due on that deferred amount.



Hypothetical illustration; proportions are illustrative. Not a projection of any tax result.

What Qualifies

The general test is whether the tax code treats the property as wearing out in 20 years or less. That includes:

- Machinery, equipment, vehicles, furniture and computers
- Interior improvements made to a commercial building after it opened
- Land improvements such as fencing, paving, drainage and site work
- Gasoline filling stations (retail motor fuel outlets)
- Car washes and the improvements around them
- Certain new US manufacturing, refining and agricultural or chemical production buildings (added July 2025)
- Computer software and water utility property
- Fruit and nut bearing plants, by election, claimed when planted or grafted rather than when they start producing
- Film, television, live theatrical and sound recording productions
- Used property, as long as it is new to the buyer and did not come from a related party

Land is not depreciated. Buildings are written off over 27.5 years (residential rental) or 39 years (commercial) and generally do not qualify. A filling station counts if at least half its revenue or floor space goes to fuel sales, or if the building is 1,400 square feet or smaller. Car washes are 15 year property. The production building option has its own deadlines and a 10 year clawback if the use changes.

Deferral, Not Elimination

Bonus depreciation pushes tax into a later year. It does not erase it.

Whether it makes sense for an investor depends on how long the delay lasts, what the money earns in the meantime, and whether the investment holds up without the tax benefit. The rate can also change: the deduction may offset gain taxed at capital gains rates today, while recapture later is often taxed at higher ordinary rates. A 1031 exchange defers gain without changing how it is taxed. Talk any strategy through with a CPA before acting.

What to Look For in a Fund

Five things to consider before making an investment like this:

- **How is the debt secured, and who is liable for it?** Commercial debt secured by real property can count toward an investor's at risk amount even where no one is personally liable for it. Otherwise it counts only where investors take on a real repayment obligation. This determines how much of the deduction an investor can use.
- **When does the property go into service?** The deduction belongs to the tax year the property is put into use, not the year the investment is made. If an investor funds in December and the property goes into service in January, the deduction lands in the next tax year.
- **What does year two look like?** A large first year write-off leaves little depreciation remaining. Consider any taxable income from the investment and plan for other methods to pay or offset it.
- **What happens at exit?** Depreciation taken is generally recaptured as ordinary income when the property is sold. Some investors offset that income with a new bonus depreciation investment, which defers it again rather than ending it. Understand how the fund expects to exit and how it anticipates taxation at exit.
- **Does the deal work before the tax benefit?** A tax deduction cannot make up for a weak investment. These are illiquid, speculative private placements and investors can lose some or all of what they invest.

Limits on the Deduction

LIMIT	WHAT IT MEANS FOR THE INVESTOR
1. Basis	An investor's deduction cannot exceed their basis: the cash invested plus their share of the fund's debt. Because the debt counts, this limit rarely comes into play.
2. At risk	Debt the investor is not liable for counts only if it is a commercial loan on real property.
3. Passive activity	Passive losses offset passive income only, not wages, interest, dividends or stock gains.
4. Excess business loss	Business losses against other income are capped at annual limits. For 2026 those are $256,000 filing single or $512,000 filing jointly.

Losses held back by any of these limits generally carry forward to later years.

Have a Gain This Year?

We can walk through whether bonus depreciation fits your passive gain and what to ask.

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Tangible Wealth Solutions does not provide tax or legal advice. See disclosures.

Sections 168(k), 168(n), 465, 469, 1245 and 1250 of the Internal Revenue Code. Current as of October 22, 2026. IRS guidance issued in 2026 is interim and proposed regulations have been announced but not yet issued.

Disclosures

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- Educational purpose only: This material is general education. It is not tax, legal, accounting or investment advice, it is not a recommendation to enter into any transaction, and no tax opinion is rendered. Tangible Wealth Solutions does not provide tax or legal advice.
- Individual facts control: Whether any deduction is available, and in what amount, depends on the taxpayer's entity structure, income, material participation, placed in service date and other facts. No result described here is assured for any taxpayer.
- Limits apply in order: A deduction must clear basis, then at risk, then passive activity, then excess business loss. Depreciation is calculated on the full cost of property, including property purchased with debt. A share of fund level nonrecourse debt increases basis but generally does not increase the amount at risk. Qualified nonrecourse financing counts toward the amount at risk only for an activity of holding real property and only where the financing is secured by that real property. In other programs, debt counts toward the amount at risk only where investors are personally liable for repayment. Amounts limited in one year generally carry forward.
- Only passive gains can be offset: Gains on publicly traded securities, C corporation stock and other portfolio assets are outside the passive category and cannot be offset by these losses. Gain on the sale of a business is passive only where the seller did not materially participate.
- Deferral, not elimination: Bonus depreciation shifts tax to later years. It does not reduce lifetime tax and in nominal dollars often increases it.
- Character changes against the investor: Because basis is driven toward zero, the later reversal is largely ordinary income under Section 1245, plus unrecaptured Section 1250 gain at up to 25 percent on real property components. Ordinary rates can exceed the capital gains rate that applied to the gain originally deferred.
- Later year income and debt amortization: After the first year, a leveraged program may generate taxable income with little remaining depreciation to offset it. A declining share of fund debt can produce taxable gain without a corresponding cash distribution.
- Placed in service deadline: Property must be acquired and placed in service by the last day of the tax year. The election out of bonus depreciation is made by class of property and is not revocable.
- Tax law and regulatory risk: These provisions are subject to change by legislation, regulation, IRS guidance and judicial interpretation. Guidance issued in 2026 is interim, with proposed regulations announced but not yet issued, and future changes could reduce or eliminate anticipated benefits.
- State conformity risk: Many states do not conform to federal bonus depreciation and require an addback, which may materially reduce or eliminate the state level benefit while state tax on the reversal still applies.
- Investment risk: These are illiquid, speculative private placements with no established secondary market and a risk of loss of some or all principal. Tax treatment should never be the sole basis for an investment decision, and the investment should be evaluated on its merits before any tax benefit.
- Professional advice: Consult your own tax, legal and financial professionals about your specific circumstances before acting on any information in this paper.