

Abstract: Every business needs a website, but it's not always easy to determine which costs of running one are deductible. Fortunately, there are guidelines and even IRS guidance to follow. This article discusses both the hardware and software costs associated with a website.

Which business website costs are deductible?

Every business needs a website, but it's not always easy to determine which costs of running one are deductible. Fortunately, established rules that generally apply to the deductibility of more long-standing business costs provide business owners with a basic idea of how to anticipate and handle the tax impact of a website. And the IRS has issued guidance that applies to software costs.

Hardware considerations

Hardware costs generally fall under the standard rules for depreciable equipment. Specifically, once website-related assets are up and running, you can deduct 100% of the cost in the first year they're placed in service (before 2023). This favorable treatment is allowed under the 100% first-year bonus depreciation break.

In later years, you can probably deduct 100% of these costs in the year the assets are placed in service under the Section 179 first-year depreciation deduction privilege. However, Sec. 179 deductions are subject to several limitations.

For the 2021 tax year, the maximum Sec. 179 deduction is \$1.05 million, subject to a phaseout rule. Under the rule, the deduction is phased out if more than a specified amount of qualified property is placed in service during the year. The threshold amount for 2021 is \$2.62 million.

There's also a taxable income limit. Under it, your Sec. 179 deduction can't exceed your business taxable income. In other words, Sec. 179 deductions can't create or increase an overall tax loss. However, any Sec. 179 deduction amount that you can't immediately deduct is carried forward and can be deducted in later years (to the extent permitted by the applicable limits).

Software issues

Similar rules apply to off-the-shelf software that you buy for your business. However, software license fees are treated differently from purchased software costs for tax purposes. Payments for leased or licensed software used for your website are currently deductible as ordinary and necessary business expenses.

An alternative position is that your software development costs represent currently deductible research and development costs under the tax code. To qualify for this treatment, the costs must be paid or incurred by December 31, 2022. A more conservative approach would be to capitalize the costs of internally developed software. Then you would depreciate them over 36 months.

If your website is primarily for advertising, you can also currently deduct internal website software development costs as ordinary and necessary business expenses.

Are you paying a third party for software to run your website? This is commonly referred to as “software as a service.” In general, payments to third parties are currently deductible as ordinary and necessary business expenses.

Still important

So much of business today seems to happen in virtual places other than your website — such as social media, apps and teleconferencing calls. Nonetheless, a central website where you can provide a solid overview of your company is still important. We can help you determine the appropriate tax treatment of website costs.

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