February 2016

Volume 2, Issue 1

Leslie A. Cesario, Ltd.
Monthly Newsletter

Affordable Care Act Reporting Relief for Employers

Article Highlights:

- Applicable Large Employer
- Form 1095-C and Form 1094-C
- IRS Filing Due Date
- Copy to Employee Due date
- Effect on Filing Individual Returns

Beginning for the 2015 tax year, Applicable Large Employers (ALEs) are required to file Forms 1095-C and 1094-C with the IRS and provide a copy of the 1095-C to each of their employees. An ALE is generally an employer with 50 or more equivalent full time employees (EFTEs) in the prior year. Even though ALE's with 99 or fewer EFTEs are not subject to the insurance mandate for 2015, they are subject to the 1094-C and 1095-C filing requirements for 2015.

Because this is the first year for this requirement, the IRS has decided to provide first year (2015) filing relief for Forms 1095-B and 1095-C. The due dates for furnishing these forms are extended as follows:

- The due date for providing the 2015 Form 1095-B and the 2015 Form 1095-C to the insured and employees is extended from February 1, 2016, to March 31, 2016.

- The due date for health coverage providers and employers to furnish the 2015 Form 1094-B and the 2015 Form 1094-C to the IRS is extended from February 29, 2016, to May 31, 2016 if not filing electronically.

- The due date for health coverage providers and employers electronically filing the 2015 Form 1094-B and the 2015 Form 1094-C with the IRS is extended from March 31, 2016, to June 30, 2016.

While the IRS is prepared to accept information reporting returns beginning in January 2016, employers and other coverage providers who can't meet the original deadlines are encouraged to furnish statements and file the information returns as soon as they are ready.

The information provided to individuals on their copy of Form 1095-B or 1095-C is generally used to confirm that the individual had minimum essential coverage (and thus avoid the penalty that applies when not covered for the full year). However, with the extension of the filing dates for these forms, individuals may not have the forms in hand before filing their 2015 returns. For 2015 only, individuals who rely on other information received from their coverage providers about their coverage for purposes of filing their returns need not amend their returns once they receive Form 1095-B or Form 1095-C or any corrections, according to the IRS.

Likewise, individuals who, when filing their 2015 income tax returns, rely upon other information received from employers about their offers of coverage for purposes of determining eligibility for the premium tax credit need not amend their returns once they receive their Forms 1095-C or any corrected Forms 1095-C.

Homeowner Energy Tax Credits Get New Life

Article Highlights:

- Home Energy-Saving Improvements
- Solar and Other Types of Energy Generation Systems
- Things to Consider Before Signing Up

Recently passed legislation has given new life to two homeowner energy credits that had expired or were about to expire, providing renewed opportunities to homeowners wanting to take advantage of these credits and reduce their energy costs.

Non-business Energy Credit - The first of the two credits is what the tax code refers to as the Non-business Energy Credit. A more descriptive title would be an energy saving credit since it applies to improvements to the taxpayer's existing primary home to make it more energy efficient. This credit was extended for two more years, allowing homeowners to claim the credit for qualifying energy improvements made in 2015 and 2016.

The credit generally applies to insulation, storm windows and doors, and certain types of energy-efficient roofing materials, air-conditioning and hot water systems.

The credit is 10% of the cost of the energy-saving items but does not apply to the cost of installation and is limited to a lifetime maximum of $500. So if you have taken advantage of this credit in the past and received $500 or more in credit in a prior year, you cannot claim any additional credit.

In addition to the $500 overall limitation, there are also per-item limitations on the credit; for example, qualified windows and skylights - $200, qualified hot water boiler - $150 and qualified energy-efficient equipment - $300.

The credit is nonrefundable and can only be used to offset income taxes (including the alternative minimum tax).

Residential Energy Efficient Property Credit - The second credit to be extended is called the Residential Energy Efficient Property Credit. Better known as the home solar credit, it also provides credit for wind energy systems, geothermal systems and fuel cell systems.

The credit is generally 30% of the qualified property and installation costs, subject to some limitations for fuel cell and geothermal systems.

The credit, which was scheduled to expire after 2016, has been extended through 2021, <u>but only for solar electric and solar hot water systems (excluding swimming pools)</u>. In addition, the credit percentage is phased out beginning after 2019. The following are the credit percentages allowed through 2021:

- 2009 through 2021: No annual limit

- 2009–2019: 30%
- 2020: rate reduced to 26% and only on solar-related systems
- 2021: rate reduced to 22% and only on solar-related systems

There is no limit on the actual credit other than the credit percentage. It is a nonrefundable credit and can be used to offset income tax liability (including the AMT). However, if the credit is unused because it exceeds the income tax amount, it can be carried over to another year as long as the credit has not expired.

Things to Consider - When considering whether or not to go to the expense of installing a solar system, you need to consider a number of issues:

1. Is it cost effective considering your electric usage?
2. How will you pay for it?
3. If you finance it are the terms and interest rate reasonable for your financial situation?
4. How will it affect your property's value?
5. Will you be able to benefit from the tax credits?

Installing solar is a big financial commitment and should be considered carefully. Don't let a solar system salesperson rush you into a decision. If you need assistance analyzing the financial and tax aspects of installing a solar system, please give this office a call before you sign on the dotted line.

IRS Announces 2016 Standard Mileage Rates

Article Highlights:

- 2016 standard mileage rates
- Business, charitable, medical and moving rates
- Switching between the actual expense and the standard mileage rate methods
- Special allowances for SUVs

As it does every year, the Internal Revenue Service recently announced the inflation-adjusted 2016 optional standard mileage rates used to calculate the deductible costs of operating an automobile for business, charitable, medical or moving purposes.

Beginning on Jan. 1, 2016, the standard mileage rates for the use of a car (or a van, pickup or panel truck) will be:

- 54.0 cents per mile for business miles driven (including a 24-cent-per-mile allocation for depreciation). This is down from 57.5 cents in 2015;

- 19 cents per mile driven for medical or moving purposes. This is down from 23 cents in 2015; and

- 14 cents per mile driven in service of charitable organizations.

The standard mileage rate for business is based on an annual study of the fixed and variable costs of operating an automobile. The rate for medical and moving purposes is based on the variable costs as determined by the same study. The rate for using an automobile while performing services for a charitable organization is statutorily set and has been 14 cents for over 15 years.

Taxpayers always have the option of calculating the actual costs of using their vehicle for business rather than using the standard mileage rates. With the extension of the bonus depreciation though 2019, using the actual expense method may be a worthwhile consideration in the first year the vehicle is placed in service. The bonus depreciation allowance adds an additional $8,000 to the maximum first year depreciation deduction of passenger vehicles and light trucks that have an unloaded gross vehicle weight of 6,000 pounds or less.

However, the standard mileage rates cannot be used if the actual method (using Sec. 179, bonus depreciation and/or MACRS depreciation) has been used in previous years. This rule is applied on a vehicle-by-vehicle basis. In addition, the business standard mileage rate cannot be used for any vehicle used for hire or for more than four vehicles used simultaneously.

Employer reimbursement – Where employers reimburse employees for business-related car expenses using the standard mileage allowance method for each substantiated employment-connected business mile, the reimbursement is tax-free if the employee substantiates to the employer the time, place, mileage and purpose of employment-connected business travel.

Employees whose actual employment-related business mileage expenses exceed the employer's reimbursement can deduct the difference on their income tax return as a miscellaneous itemized deduction subject to the 2%-of-AGI floor. However, an employee who leases an auto and is reimbursed using the mileage allowance method can't claim a deduction based on actual expenses unless he does so consistently beginning with the first business use of the auto.

Faster Write-Offs for Heavy Sport Utility Vehicles (SUVs) - Many of today's SUV vehicles weigh more than 6,000 pounds and are therefore not subject to the luxury auto depreciation limit rules; so taxpayers with these vehicles can utilize both the §179 expense deduction (up to a maximum of $25,000) and the bonus depreciation (the §179 deduction must be applied first and then the bonus depreciation) to produce a sizable first-year tax deduction. However, the vehicle cannot exceed a gross unloaded vehicle weight of 14,000 pounds. Caution: Business autos are 5-year class life property. If the taxpayer subsequently disposes of the vehicle early, before the end of the 5-year period, as many do, a portion of the §179 expense deduction will be recaptured and must be added back to income (SE income for self-employed individuals). The future ramifications of deducting all or a significant portion of the vehicle's cost using §179 should be considered.

If you have questions related to best methods of deducting the business use of your vehicle or the documentation required, please give this office a call.

Don’t Miss Out on the Earned Income Tax Credit

Article Highlights:

- Earned Income Tax Credit (EITC) Qualifications
- Computing the Credit
- Limit on Investment Income
- Military Combat Pay Election
- EITC Scams
- Banning EITC Filers

The Earned Income Tax Credit (EITC) is a tax benefit for working people who have low to moderate income. It provides a tax credit that is treated like tax withholding: it goes to pay an individual’s tax liability, and any excess is paid to the individual in the form of a tax refund.

Qualifications for the credit are based upon the amount of the filer’s earned income, the spouse’s earned income if the filer is married, and the number of qualified children on the tax return. Any child must either be under the age of 19 or be a full-time student under the age of 24 at the end of the year. Low-income earners between the ages of 25 and 64 who don’t have a qualifying child may also qualify.

Earned income generally means income from working, such as W-2 wages and self-employment income.

The credit increases as the taxpayer’s earned income or adjusted gross income (AGI) increases until it reaches a plateau, where it remains constant (at the maximum amount) until it reaches the AGI phase-out threshold. Once the threshold amount is exceeded, the credit is reduced by a set percentage; if income exceeds the top of the phase-out range, no credit is allowed.

Computing the credit, like all things tax, is complicated, and the credit is actually determined using IRS tables that reflect the dollar amounts at which phaseout begins and ends. However, the illustration below can help approximate the credit for 2015.

Number of Qual. Children:	None	One	Two	Three
Credit Percentage:	7.65	34.00	40.00	45.00
Max Credit:	$503	$3,359	$5,548	$6,242
Plateau Threshold:	$6,610	$9,880	$13,870	$13,870
Phaseout Threshold:				
Married Filing Jointly	$13,750	$23,630	$23,630	$23,630
Others	$8,240	$18,110	$18,110	$18,110
Totally Phased Out:				
Married Filing Jointly	$20,330	$44,651	$49,974	$53,267
Others	$14,820	$39,131	$44,454	$47,747

Example below

Example: *A married couple with two children has earned income of $20,000 and a modified AGI of $21,000. If we multiply their earned income by their credit percentage ($20,000 x .40), we come up with $8,000. However, that exceeds the maximum credit of $5,548 for a married couple with two children, so their credit before any phaseout is $5,548. Since their* *modified AGI is less than the phaseout threshold, then their EITC is $5,548. Had their earned income been $10,000, then their credit would have been $4,000 ($10,000 x .40). If either their earned income or their modified AGI had exceeded $49,974, their EITC would have been totally phased out and they would not have gotten any credit.*

There is also a limit on investment income a taxpayer can have and qualify for the EITC. For 2015, that limit is $3,400. Thus if a taxpayer qualifies for EITC but has investment income in excess of $3,400, the taxpayer will not receive any EITC.

Individuals that claim either the foreign earned income or foreign housing exclusion also will not qualify for the earned income credit.

Members of the military can elect to treat all or none of their nontaxable combat pay as earned income for the purposes of computing the EITC. The calculation providing the larger EITC benefit can be used.

Because the potential payout of this credit is so generous, it is the constant target of scammers, and in 2014 the government paid out nearly $18 billion in improper EITC payments. Besides scammers, the qualification for EITC is frequently contested between divorced parents who are both attempting to claim the same child in an effort to qualify for the EITC.

The IRS is authorized to ban taxpayers from claiming the EITC for two years if it determines during an audit that they claimed the credit improperly due to reckless or intentional disregard of the rules. Last year, there were more than 67,000 two-year bans in effect. The ban lasts 10 years if credit was claimed in an earlier year due to fraud.

The government wants those who are entitled to the credit to claim it, and so the IRS widely promotes the credit. However, the rules are quite complex and best addressed by a tax professional.

If you have questions about how the EITC might apply to you, please call this office for additional information. Please understand that a taxpayer who might not normally be required to file a return might still benefit from filing to claim the EITC.

Jointly or Separately - How to File After Saying I Do

Article Summary:

- Filing Options
- Married Filing Jointly
- Unpleasant Consequences
- Pleasant Consequences
- Married Filing Separately

A taxpayer's filing status for the year is based upon his or her marital status at the close of the tax year. Thus, if you get married on the last day of the tax year, you are treated as married for the entire year. The options for married couples are to file jointly or separately. Both statuses can result in surprises for individuals who previously filed as unmarried. The surprises can be both pleasant and unpleasant.

Individuals filing jointly must combine their incomes, and if both spouses are working, combining income can trigger a number of unpleasant surprises, as many tax benefits are eliminated or reduced for higher-income taxpayers. The following are some of the more frequently encountered issues created by higher incomes:

- Being pushed into a higher tax bracket
- Causing capital gains to be taxed at higher rates
- Reducing the child care credit
- Limiting the deductible IRA amount
- Triggering a tax on net investment income that only applies to higher-income taxpayers
- Causing Social Security income to be taxed.
- Reducing the Earned Income Tax Credit
- Reducing or eliminating medical and/or miscellaneous itemized deductions
- Causing the overall itemized deductions to be phased out
- Causing the personal exemption deduction to be phased out

Filing separately generally will not alleviate the aforementioned issues because the tax code includes provisions to prevent married taxpayers from circumventing the loss of tax benefits that apply to higher-income taxpayers by filing separately.

On the other hand, if only one spouse has income, filing jointly will generally result in a lower tax because of the lower joint tax brackets and the additional exemption provided by the non-working spouse. In addition, some of the higher-income limitations that might have applied to an unmarried individual with the same amount of income may be reduced or eliminated on a joint return.

Filing as married but separate will generally result in a higher combined income tax for married taxpayers. The tax laws are written to prevent married taxpayers from filing separately to circumvent a limitation that would apply to them if they filed jointly. For instance, if a couple files separately, the tax code requires both to itemize their deductions if either does so, meaning that if one itemizes, the other cannot take the standard deduction. Another example relates to how a married couple’s Social Security (SS) benefits are taxed: on a joint return, none of the SS income is taxed until half of the SS benefits plus other income exceeds $32,000. On a married-but-separate return, the taxable threshold is reduced to zero.

Aside from the amount of tax, another consideration that married couples need to be aware of when deciding on their filing status is that when married taxpayers file jointly, they become jointly and individually responsible (often referred to as “jointly and severally liable”) for the tax and interest or penalty due on their returns. This is true even if they later divorce. When using the married-but-separate filing status, each spouse is only responsible for his or her own tax liability.

If you would like to evaluate the impact of marriage on your tax liability before saying “I do,” please give this office a call.

Are You Ignoring Retirement?

Article Highlights:

- Predicting Social Security Income
- Planning for the Future
- Employer Retirement Plans
- Tax Incentive Retirement Savings Plans

Are you ignoring your future retirement needs? That tends to happen when you are younger, retirement is far in the future, and you believe you have plenty of time to save for it. Some people ignore the issue until late in life and then have to scramble at the last minute to fund their retirement. Others even ignore the issue altogether, thinking their Social Security income (assuming they qualify for it) will take care of their retirement needs.

By current government standards, a single individual with $11,770 or a married couple with $15,930 of annual household income is at the 100% poverty level. If you compare those levels with potential Social Security income, you may find that expecting to retire on just Social Security income may result in a bleak retirement.

You can predict your future Social Security income by visiting the Social Security Administration's **Retirement Estimator**. With the Retirement Estimator, you can plug in some basic information to get an instant, personalized estimate of your future benefits. Different life choices can alter the course of your future, so try out different scenarios – such as higher and lower future earnings amounts and various retirement dates – to get a good idea of how these scenarios can change your future benefit amounts. Once you've done this, consider what your retirement would be like with only Social Security income.

If you are fortunate enough to have an employer-, union- or government-funded retirement plan, determine how much you can expect to receive when you retire. Add that amount to any Social Security benefits you are entitled to and then consider what retirement would be like with that combined income. If this result portends an austere retirement, know that the sooner you start saving for retirement, the better off you will be.

With today's relatively low interest rates and up-and-down stock market, it is much more difficult to grow a retirement plan with earnings than it was 10 or 20 years ago. With current interest rates barely mirroring inflation rates, there is little or no effective growth. That means one must set aside more of one's current earnings for retirement to prepare for a comfortable retirement.

Because the government wants you to save and prepare for your own retirement, tax laws offer a variety of tax incentives for retirement savings plans, both for wage earners and for self-employed individuals and their employees. These plans include:

- **Traditional IRA** – This plan allows up to $5,500 (or $6,500 for individuals age 50 and over) of tax-deductible contributions each year until reaching age 70½. However, the amount that can be deducted phases out for higher-income taxpayers who also have retirement plans through their employer.

- **Roth IRA** – This plan also allows up to $5,500 (or $6,500 for individuals age 50 and over) of contributions each year. Like the Traditional IRA, the amount that can be contributed phases out for higher-income taxpayers; unlike the Traditional IRA, these amounts phase out even for those who do not have an employer-related retirement plan.

- **myRA Accounts** – This relatively new retirement vehicle is designed to be a starter retirement plan for individuals with limited financial resources and those whose employers do not offer a retirement plan. The minimum amount required to establish one of these government-administered plans is $25, with monthly contributions as little as $2. Once the total value of the account reaches $15,000 or after 30 years, the account must be converted to a commercial Roth IRA account.

- **Employer 401(k) Plans** – An employer 401(k) plan generally enables employees to contribute up to $18,000 per year, before taxes. In addition, taxpayers who are age 50 and over can contribute an extra $6,000 annually, for a total of $24,000. Many employers also match a percentage of the employee's contribution, and this can amount to a significant sum for those who stay in the plan for many years.

- **Health Savings Accounts** – Although established to help individuals with high-deductible health insurance plans pay medical expenses, these accounts can also be used as supplemental retirement plans if an individual has already maxed out his or her contributions to other types of plans. Annual contributions for these plans can be as much as $3,350 for individuals and $6,750 for families.

- **Tax Sheltered Annuities** – These retirement accounts are for employees of public schools and certain tax-exempt organizations; they enable employees to make annual tax-deferred contributions of up to $18,000 (or $24,000 for those age 50 and over).

- **Self-Employed Retirement Plans** – These plans, also referred to as Keogh plans, allow self-employed individuals to contribute 25% of their net business profits to their retirement plans. The contributions are pre-tax (which means that they reduce the individual's taxable net profits), so the actual amount that can be contributed is 20% of the net profits.

- **Simplified Employee Pension (SEP)** – This type of plan allows contributions in the same amounts as allowed for self-employed retirement plans, except that the retirement contributions are held in an IRA account under the control of the employee or self-employed individual. These accounts can be established after the end of the year, and contributions can be made for the prior year.

Each individual's financial resources, family obligations, health, life expectancy, and retirement expectations will vary greatly, and there is no one-size-fits-all retirement savings strategy for everyone. Purchasing a home and putting children through college are examples of events that can limit an individual's or family's ability to make retirement contributions; these events must be accounted for in any retirement planning.

If you have questions about any of the retirement vehicles discussed above, please give this office a call.

Household Help: Employee or Contractor?

Article Highlights:

- Household Employee Definition
- Employee Control Factors
- Self-employed or Employee
- Withholding Requirements
- Reporting Requirements

Frequently taxpayers will hire an individual or firm to provide services at the taxpayer's home. Because the IRS requires employers to withhold taxes for employees and issue them W-2s at the end of the year, the big question is whether or not that individual is a household employee.

Whether a household worker is considered an employee depends a great deal on circumstances and the amount of control the person hiring has over the job and the hired person. Ordinarily, when someone has the last word about telling a worker what needs to be done and how the job should be done, then that worker is an employee. Having a right to discharge the worker and supplying tools and the place to perform a job are primary factors that show control.

Not all those hired to work in a taxpayer's home are considered household employees. For example, an individual may hire a self-employed gardener who handles the yard work for a taxpayer and others in the taxpayer's neighborhood. The gardener supplies all tools and brings in other helpers needed to do the job. Under these circumstances, the gardener isn't an employee and the person hiring him/her isn't responsible for paying employment taxes. The same would apply to the pool guy or to contractors making repairs or improvements on the home.

Contrast the following example to the self-employed gardener described above: The Smith family hired Lynn to clean their home and care for their 3-year old daughter, Lori, while they are at work. Mrs. Smith gave Lynn instructions about the job to be done, explained how the various tasks should be done, and provided the tools and supplies; Mrs. Smith, rather than Lynn, had control over the job. Under these circumstances, Lynn is a household employee, and the Smiths are responsible for withholding and paying certain employment taxes for her and issuing her a W-2 for the year.

If an individual you hire is considered an employee, then you must withhold both Social Security and Medicare taxes from the household employee's cash wages if they equal or exceed the $2,000 threshold for 2016.

The employer must match from his/her own funds the FICA amounts withheld from the employee's wages. Wages paid to a household employee who is under age 18 at any time during the year are exempt from Social Security and Medicare taxes unless household work is the employee's principal occupation.

Although the value of food, lodging, clothing or other noncash items given to household employees is generally treated as wages, it is not subject to FICA taxes. However, cash given in place of these items is subject to such taxes.
A household employer doesn't have to withhold income taxes on wages paid to a household employee, but if the employee requests such withholding, the employer can agree to it. If income taxes are to be withheld, the employer can have the employee complete Form W-4 and base the withholding amount upon the federal income tax and FICA withholding tables.

The wage amount subject to income tax withholding includes salary, vacation and holiday pay, bonuses, clothing and other noncash items, meals and lodging. However, meals are not taxable, and therefore they are not subject to income tax withholding if they are furnished for the employer's convenience and on the employer's premises. The same goes for lodging if one additional requirement applies—that the employee lives on the employer's premises. In lieu of withholding the employee's share of FICA taxes from the employee's wages, some employers prefer to pay the employee's share themselves. In that case, the FICA taxes paid on behalf of the employee are treated as additional wages for income tax purposes.

A household employer who pays more than $1,000 in cash wages to household employees in any calendar quarter of either the current or the prior year is also liable for unemployment tax under the Federal Unemployment Tax Act (FUTA)."

Although this may seem quite complicated, the IRS provides a single form (Schedule H) that generally allows a household employer to report and pay employment taxes on household employees' wages as part of the employer's Form 1040 filing. This includes Social Security, Medicare, and income tax withholdings and FUTA taxes.

If the employer runs a sole proprietorship with employees, the household employees' Social Security and Medicare taxes and income tax withholding may be included as part of the individual's business employee payroll reporting but are not deductible as a business expense.

Although the federal requirements can generally be handled on an individual's 1040 tax return, there may also be state reporting requirements for your state that entail separate filings.

If the individual providing household services is determined to be an independent contractor, there is currently no requirement that the person who hired the contractor file an information return such as Form 1099-MISC. This is so even if the services performed are eligible for a tax deduction or credit (such as for medical services or child care). The 1099-MISC is used only by businesses to report their payments of $600 or more to independent contractors. Most individuals who hire other individuals to provide services in or around their homes are not doing so as a business owner.

Please call this office if you need assistance with your household employee reporting requirements or need information related to the reporting requirements for your state.

Ways To Deduct Health Insurance

Article Highlight:

- Itemized Deduction
- AGI Limitations
- What Insurance Is Deductible
- Above-The-Line Deduction for the Self-Employed
- Income Limitation
- Subsidized Limitation

Health insurance premiums, especially in the wake of the "Affordable Care Act," have risen dramatically and are one of the largest expenses that most individuals pay. Although the cost of health insurance is allowed as part of an individual's medical deductions when itemizing deductions, only the amount of total medical expenses that exceed 10% of the taxpayer's adjusted gross income (AGI) is deductible. The 10% limitation is reduced to 7.5% through 2016 where a taxpayer or spouse (if any) is age 65 or over as of the end of the year. Prior to the increased limitation imposed by the "Affordable Care Act," the limitation was 7.5% for everyone.

The purpose of this article is twofold: first, to remind you what insurance can be included as a medical deduction, and second, to inform you of an alternate means of deducting health insurance for certain self-employed individuals—a means that avoids the AGI limitation and allows for deduction without itemizing.

Let's start by looking at what is treated as deductible health insurance. It includes the premiums you pay for coverage for yourself, your dependents, and your spouse, if applicable, for the following types of plans:

- Health Care and Hospitalization Insurance
- Long-Term Care Insurance (but limited based upon age)
- Medicare-B
- Medicare-C (aka Medicare Advantage Plans)
- Medicare-D
- Dental Insurance
- Vision Insurance
- Premiums Paid through a Government Marketplace net of the Premium Tax Credit

However, premiums paid on your or your family's behalf by your employer aren't deductible because their cost is not included in your wage income. Or, if you pay premiums for coverage under your employer's insurance plan through a "cafeteria" plan, those premiums aren't deductible either because they are paid with pre-tax dollars.

If you are a self-employed individual, you can deduct 100% (no AGI reduction) of the premiums without itemizing your deductions. This above-the-line deduction is limited to your net profits from self-employment. If you are a partner who performs services in the capacity of a partner and the partnership pays health insurance premiums on your behalf, those premiums are treated as guaranteed payments that are deductible by the partnership and are includible in your gross income. In turn, you may deduct the cost of the premiums as an above-the-line deduction under the rules discussed in this article.

No above-the-line deduction is permitted when the self-employed individual is eligible to participate in a "subsidized" health plan maintained by an employer of the taxpayer, the taxpayer's spouse, any dependent, or any child of the taxpayer who hasn't attained age 27 as of the end of the tax year. This rule is applied separately to plans that provide coverage for long-term care services. Thus, an individual eligible for employer-subsidized health insurance may still be able to deduct long-term care insurance premiums, as long as he isn't eligible for employer-subsidized long-term care insurance. In addition, to be treated as subsidized, 50% or more of the premium must be paid by the employer.

This above-the-line deduction is also available to more-than-2% S corporation shareholders. For purposes of the income limitation, the shareholder's wages from the S corporation are treated as his or her earned income.

If you have any questions related to deducting health insurance premiums, either as an itemized deduction or an above-the-line deduction for self-employed individuals, please give this office a call.

Better To Sell Or Trade A Business Vehicle?

Article Highlights:

- Trade-in
- Sale
- Personal Use Allocation
- Other Considerations

From time to time business owners will replace vehicles used in their business. When replacing a business vehicle, the tax ramifications are different when selling the old vehicle and when trading it in for a new vehicle. If the vehicle is sold, the result is reported on the taxpayer's return as an above-the-line gain or loss. Since a trade-in is treated as an exchange, any gain or loss is absorbed into the replacement vehicle's depreciable basis, thereby avoiding any current taxable gain or reportable loss.

Thus, it is generally better to trade in a vehicle that would result in a gain if it were sold and to sell a vehicle if doing so would result in a loss.

Let's say a taxpayer sells a 100%-business-use vehicle for $12,000. The original purchase price was $32,000, and $17,000 is taken in depreciation. As illustrated below, the sale results in a loss, so it generally would be better to sell the vehicle and deduct the loss rather than trade in the vehicle.

Sale price		$12,000
Original Cost	$32,000	
Depreciation Taken	<$17,000>	
Depreciated Basis	$15,000	<$15,000>
Loss		<$ 3,000>

On the other hand, had the business owner sold the vehicle for $16,000, the sale would result in a $1,000 taxable gain, and trading it in would be a better option. **Caution**: Sales to the same dealer are treated as trade-ins.

If a vehicle is used for both business and personal purposes, the loss or gain must be prorated for the proportion of business use, as the personal portion of any loss is not deductible.

If you are considering trading a vehicle in, determine whether the tax benefits exceed the additional money received from selling the old business vehicle, as trade-in values are generally less than actual sales values. You should also consider the time and energy it will take to sell the vehicle on your own.

This concept can also be used when selling or disposing of other business assets. If you have questions about how this tax strategy might apply to your specific tax situation, please give this office a call.

Not All Home Mortgage Interest Is Deductible; The IRS is Watching

Article Highlights:

- Acquisition Debt
- Equity Debt
- Tracing Excess Debt
- Unsecured Election

One of the current IRS audit initiatives is checking to see if taxpayers are deducting too much home equity debt interest. Generally, taxpayers are allowed to deduct the interest on up to $1 million of home acquisition debt (includes subsequent debt incurred to make improvements, but not repairs) and the interest on up to $100,000 of home equity debt. Equity debt is debt not incurred to acquire or improve the home. Taxpayers frequently exceed the equity debt limit and fail to adjust their interest deduction accordingly.

The best way to explain this interest deduction limitation is by example. Let's assume you have never refinanced the original loan that was used to purchase your home, and the current principal balance of that acquisition debt is less than $1 million. However, you also have a line of credit on the home, and the debt on that line of credit is treated as equity debt. If the balance on that line of credit is $120,000, then you have exceeded the equity debt limitation and only 83.33% ($100,000/$120,000) of the equity line interest is deductible as home mortgage interest on Schedule A. The balance is not deductible unless you can trace the use of the excess debt to either investment or business use. If traceable to investments, the interest you pay on the amount traceable would be deductible as investment interest, which is also deducted on Schedule A but is limited to an amount equal to your net investment income (investment income less investment expenses). If the excess debt was used for business, you could deduct the interest on that excess debt on the appropriate business schedule.

Alternatively, the IRS allows you to elect to treat the equity line debt as "not secured" by the home, which would allow the interest on the entire equity debt to be traced to its use and deducted on the appropriate schedule if deductible. For instance, you borrow from the equity line for a down payment on a rental. If you make the "not secured" election, the interest on the amount borrowed for the rental down payment would be deductible on the Schedule E rental income and expense schedule and not subject to the home equity debt limitations.

However, one of the rules that allows home mortgage interest to be deductible is it must be secured by the home, and if the unsecured election is used, none of the interest can be traced back to the home itself. So, for example, if the equity line was used partly for the rental down payment and partially for personal reasons, the interest associated with the personal portion of the loan would not be deductible since you elected to treat it as not secured by your home.

Using the unsecured election can have unexpected results in the current year and in the future. You should use that election only after consulting with this office.

Generally, people not familiar with the sometimes complicated rules associated with home mortgage interest believe the interest shown on the Form 1098 issued by their lenders at the end of the year is fully deductible. In many cases when taxpayers have refinanced or have equity loans, that may be far from the truth and could result in an IRS inquiry and potential multi-year adjustments. In fact, for Forms 1098 issued after 2016 (thus effective for 2016 information), the IRS will be requiring lenders to include additional information, including the amount of the outstanding mortgage principal as of the beginning of the calendar year, the mortgage origination date and the address of the property securing the mortgage, which will provide the IRS with additional tools for audits.

When in doubt about how much interest you can deduct or if you have questions about how refinancing or taking on additional home mortgage debt will impact your taxes, please call this office for assistance.