TaxTips

Keeping You Informed ▪ Summer/Fall 2018

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Renting your home

A hidden source of tax-free income

Have you ever thought of your home as a source of untapped income? Consider this: Your home is located in an area that has a lot of tourism or large events that attract many people. Sometimes hotel space is limited or fills quickly. You prefer to be out of town while these events are taking place. If you rent your home for less than 15 days during the year, you just earned some tax-free income.

If you itemize deductions, your mortgage interest and real estate taxes are deducted on your Schedule A. None of the income you collect is taxable, nor is it reported on your tax return. The key to keeping the income tax-free is the number of days you rent your home. You must keep it to less than 15 days during the year. If you rent your home for 15 days or more, tax reporting becomes a bit more complex. Since you also use your home for personal purposes—meaning you live there—you must divide your expenses between the rental use and the personal use based on the number of days used for each purpose. If, after you reduce your rental income by allowed expenses, you have a profit, that profit is taxable. Deductions are limited to rental income.

If you are considering renting your home to others, regardless of the number of days, consult with me first so we can discuss all potential tax consequences.

Home equity loan interest

New law eliminates deduction

For many of you, finding the money to pay for a new car, boat or dream vacation was as easy as tapping the equity in your home. Prior to 2018, you could use the equity in your home to make large purchases, pay expenses or consolidate debt and deduct the interest on up to $100,000 of debt.

After 2017 and before 2026, this tax savings strategy is gone. While you can still use the equity in your home to borrow needed funds, the interest is no longer deductible unless you use the money to buy, construct or improve your home. The elimination of this deduction applies regardless of when the home equity debt was incurred.

Starting a new business?

Keep track of your expenses

There are many costs associated with the start-up of a business that can be deducted once your business opens. To qualify as a start-up cost, the expense must be one that you could deduct if you were already in business. Examples include travel to suppliers, training for your new employees, advertising, utilities and other pre-opening expenses. If start-up costs are less than $50,000, you are allowed to deduct up to the first $5,000 of expenses you incur in the current year. Any additional start-up expenses are deducted over a remaining period of not less than 180 months.

To incorporate, or not

Factors to consider

Now that the corporate tax rate has been reduced to 21% permanently, is it a good time to incorporate your business? There is no one-size-fits-all answer to this question but there are some general guidelines to consider.

The primary nontax advantage of incorporating a small business is personal asset protection. Both corporations and LLCs allow owners to separate and protect their personal assets. In a properly structured and managed corporation or LLC, owners should have limited liability for business debts and obligations. Another nontax reason business owners incorporate is perpetual existence. Corporations and LLCs can continue to exist even if ownership or management changes. Sole proprietorships simply end if an owner dies or leaves the business.

If you file a Schedule C, E or F and your only concern is a loss of deductions because of the new tax changes, there is likely little benefit to incorporating your business. None of the deductions for expenses have been eliminated or suspended if you are a business owner, landlord or farmer. In fact, certain noncorporate businesses are considered pass-through entities and may qualify for a 20% qualified business income (QBI) deduction.

Other considerations to incorporating include the type of business you operate, your gross income, the type of assets you use in your business, and whether you have employees and wish to provide benefits. One final point: Regular C corporations are subject to double taxation. This means the income is taxed once at the corporate level and again at the shareholder level when income is distributed in the form of dividends. Pass-through entities pass the income through to the owners, and it is taxed only once on their return.

Be sure to consult with me first before making any decisions on how you should structure your business.

Donating noncash items to charity

How to reap the full tax benefit

You've done your spring cleaning and now you have boxes of outgrown clothing and unused household items. Should you toss them, have a garage sale or keep them?

If you opt for a garage sale, you have to devote time to making everything presentable, marking prices, setting up tables, advertising and running the actual event. The benefit is instant money for all your hard work, but generally at far less than what it's really worth.

A better option might be to donate that property to a qualified charity such as Goodwill, the Salvation Army or your local church. If you are able to itemize your deductions, you can deduct the fair market value (FMV) of the property you donate. Here are the three most common mistakes that people make when donating property:

- Failure to document what was actually donated to the charity. Say you donated six men's shirts, two pairs of children's shorts, three blouses and five pairs of men's pants. Chances are you just put everything in a bag and told your preparer that you donated a bag full of clothing and you have no documentation. Keep a detailed list of the items you donate and their condition.
- Undervaluing the property that was given to the charity. This is always a subjective area but the law states the deduction is equal to the FMV of the property given. What do you use as the FMV? If you give used clothing to Goodwill, for example, the FMV would be the price that typical buyers actually pay Goodwill for clothing of this age, condition, style and use. Along with a detailed list of the items you donate, establish a value for each item. Local thrift stores often have a list of items with suggested values.
- Failure to obtain documentation that the charitable organization received the property. Charitable organizations will provide you with a receipt acknowledging your contribution.

If you can establish these three areas, you are in complete compliance with the law and are allowed to deduct the value of all property you donate to a charity.

Unreimbursed expenses

Many common employee business expenses are no longer deductible

Are you an employee who incurs unreimbursed expenses? Beginning in 2018 and continuing through 2025, some expenses you could previously claim as itemized deductions won't be allowed. Here's a list of the more common items that are no longer deductible:

- Uniforms and certain work clothes
- Safety shoes and other safety equipment
- Tools needed for your job
- Union dues
- Job-seeking expenses
- Professional dues and licenses
- Home office deductions
- Subscriptions to professional journals
- Continuing education
- Work-related travel, meals and lodging
- Rural mail carrier vehicle expenses
- Passport for a business trip

Now may be a great opportunity to negotiate an accountable plan with your employer.

The IRS encourages taxpayers who typically itemize their deductions on Schedule A to use the new withholding Calculator this year to perform a "paycheck checkup." People who have itemized before may be affected by changes from the Tax Cuts and Jobs Act. Taxpayers who itemize should make sure their employers are withholding the appropriate amount of tax from their paychecks. Please contact Tax On Wheels, LLC for assistance in adjusting your withholding.

Did you receive an e-mail from the IRS?

Hit the delete button

There were various e-mail and phone scams circulating this past year that appeared as though they were from the IRS. The e-mails claim you may owe additional tax or have a refund waiting for you, and all you need to do is provide some information, such as your name, address, Social Security number and filing status. Some of the e-mails even went so far as to ask for your bank account information so they could deposit your refund.

For starters, the IRS never initiates correspondence with taxpayers via e-mail, nor does it ask for your bank account information. The scam is a ruse to collect your personal information and steal your identity. Don't fall for it. Delete the e-mail and keep your personal information safe.

If someone claiming to be from the IRS calls you, hang up. If the IRS needs your attention, they will send you a letter.

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Quick Tips

- Up to $2,500 of interest you paid on a student loan is deductible if your income is below $65,000 if single ($135,000 for joint filers).
- Beginning in 2019, the penalty under the Affordable Care Act for failing to have minimum essential health care coverage is suspended.
- In 2018, the estate and gift tax exemption has been increased to roughly $11.2 million ($22.4 million for married couples).
- Deductions for personal exemptions for yourself, a spouse and any dependents are no longer allowed.
- Charitable contributions of cash to certain charities are limited to 60% of your income.
- Once you convert a regular IRA contribution to a Roth IRA, it can no longer be converted back into a regular IRA contribution. In other words, you can no longer undo a Roth conversion.
- State and local income tax, property tax and sales tax are limited to an aggregate $10,000 deduction.
- In 2018, medical expenses are allowed as an itemized deduction to the extent they exceed 7.5% of adjusted gross income for all taxpayers.
- The deduction for job-related moving expenses and the exclusion for moving expense reimbursements have been eliminated, except for certain military personnel.
- For post-2018 divorce decrees and separation agreements, alimony will not be deductible by the paying spouse and will not be taxable to the receiving spouse.