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Tax-Saving

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New Individual Coverage HRA Allows You to Reimburse Employees for Health Insurance

The new Individual Coverage HRA (ICHRA) lets you help employees with their health care costs without fear of ACA penalties. Starting January 1, 2020, employers can offer this new ICHRA.

The ICHRA allows you to

- reimburse (free of payroll and income tax) employees' individual health care premiums and other permitted medical expenses, up to a dollar limit *you* choose—not one imposed by the government;
- offer a regular group health plan (or not—it's your choice) to certain employees and ICHRAs to other employees;
- let employees pay for coverage, beyond the amount you reimburse, via a cafeteria plan if those employees have off-Exchange individual insurance coverage;
- offer higher reimbursement levels to older workers and workers with more dependents;
- let employees roll over excess ICHRA funds from year to year, without limitation; and
- help employees with their health care costs without fear of running afoul of the ACA and its dreaded $100 per-employee-per-day penalty.

The ICHRA is a plan for employees. It's not for the owners of partnerships, proprietorships, or S corporations.

Employee Eligibility

ICHRAs are available *only* to employees enrolled in

- individual Exchange coverage,
- other individual insurance coverage, or
- Medicare.

If you already offer a traditional group health plan, you cannot offer an ICHRA to the employees who are eligible for the group plan. Employers are legally barred from giving employees a choice between a group plan and the ICHRA.
But you can offer a traditional group health plan to some classes of employees and the ICHRA to other classes of employees. Classes may be distinguished on the following factors:

- Full-time employees
- Part-time employees
- Employees working in the same geographic location
- Seasonal employees
- Employees covered by the same collective bargaining agreement
- Employees who have not satisfied a waiting period
- Nonresident aliens with no U.S. income
- Salaried workers
- Non-salaried (e.g., hourly) workers
- Temporary employees
- Any group formed by a combination of two or more of the groups listed above

Minimum class size requirements apply if you are offering a traditional group health plan to some employees and the ICHRA to other employees. The minimum class sizes are

- 10 employees, for employers with fewer than 100 employees;
- 10 percent of the total number of employees, for employers with 100 to 200 employees; and
- 20 employees, for employers with more than 200 employees.

Integration with Cafeteria Plans

What happens if the reimbursement amount you provide is insufficient to cover an employee's premiums? Can you allow the employee to pay the balance pretax through a cafeteria plan?

Yes, but only if the employee has a non-Exchange health plan. The tax code prohibits employees from making salary reduction contributions to a cafeteria plan to purchase coverage offered through the Exchange. But if the employee has a non-Exchange plan, this is permissible, subject to the existing rules that govern cafeteria plans.

The Clock Is Ticking

Employers can start offering ICHRAs on January 1, 2020. You don't need to provide the 90 days' required notice in the first year, so you still have time to get your plan in place before January 1.

But keep in mind that your employees will need to obtain individual insurance coverage and many may need to use the open enrollment period that runs from November 1 through December 15. This means you should have your notice to the employees before November 1 if you want your ICHRA effective on January 1, 2020. We have a model notice that you can use, and it includes information on Exchange enrollment.

The new law provides that the individual health plans purchased by your employees are *not* subject to ERISA, provided the following safe-harbor requirements are met:

1. An employee's purchase of any individual health insurance coverage is voluntary (the fact that individual health insurance coverage must be purchased in order to participate in an ICHRA does not make it involuntary).
2. The employer does not endorse any specific issuer or insurance coverage, though employers may provide general information, such as directing employees to HealthCare.gov or a state insurance commissioner's office.
3. Reimbursement for individual health insurance premiums is limited to individual health insurance coverage that does not consist solely of excepted benefits.
4. The employer does not receive cash or other kickbacks in connection with the employee's selection or renewal of coverage.
5. All plan participants are notified annually that their individual health insurance coverage is not subject to ERISA (this statement is included in the model notice).

If you are interested in the ICHRA, you need to move quickly.

Know Whether Your Trip Is a Deductible Business Expense

To help you understand business travel, consider this:

You planned a personal trip to Los Angeles, arriving on Friday afternoon and leaving on Sunday afternoon.

About a week later, you learn that a vendor you need to meet with is going to be in L.A. when you are. You arrange a dinner on Friday night to finalize negotiations on a large contract.

Can you now deduct 100 percent of your flight expenses to Los Angeles? How about meals?

Trouble. You must have business as your primary purpose for the trip. In general, a business trip can involve two types of business days:

1. **Travel day.** You count as business those days you spend traveling in a reasonably direct route to your business destination. (Again, note this is your business not your personal destination.)
2. **Presence-required day.** If someone requires your presence at a particular place for a specific and bona fide business purpose, this counts as a business day. That "someone" could be any business associate, employee, partner, client, customer, or vendor.

This trip we created for you works like this:

- Day 1, Friday, is a personal day. (You may deduct the cost of the business meal with the vendor whether you pay for it in total or go Dutch treat.)
- Day 2, Saturday, is a personal day.
- Day 3, Sunday, is a personal day.

But let's say you had this situation: you travel on Friday to meet with the vendor on Saturday and return home on Sunday. Now, you have a deductible trip.

Tax Issues of Converting Your Residence into a Rental Property

The simple maneuver of converting your personal residence to a rental property brings with it many tax rules, mostly good when you know how they work.

The first question that arises when you convert a personal residence into a rental is how to determine the property's tax basis for depreciation purposes during the rental period and for gain/loss purposes when you eventually sell.

Weirdly enough, two different basis rules apply:

1. If, after conversion to a rental, you sell at a **gain**, your basis on the conversion date is the usual computed amount (cost of home plus improvements, minus depreciation—such as from a home office).

2. If, after conversion to a rental, you sell at a **loss**, your basis on the conversion date is the lesser of the computed basis or the fair market value.

Once you've converted a former personal residence into a rental, you must follow the tax rules for landlords. Here is a quick summary of the most important things to know:

- You can deduct mortgage interest and real estate taxes on a rental property.

- You can also write off all the standard operating expenses that go along with owning a rental property: utilities, insurance, repairs and maintenance, yard care, association fees, and so forth.

- Finally, you can also depreciate the cost of a residential building over 27.5 years, even while it is (you hope) increasing in value.

If your rental property throws off a tax loss, things can get complicated.

The so-called passive activity loss (PAL) rules will usually apply. In general, the PAL rules allow you to deduct passive losses only to the extent you have passive income from other sources, such as positive income from other rental properties or gains from selling them.

Eventually your rental property should start throwing off positive taxable income instead of losses because escalating rents will surpass your deductible expenses. Of course, you must pay income taxes on those profits. But if you piled up suspended passive losses in earlier years, you now get to use them to offset your passive profits.

Another nice thing: positive taxable income from rental real estate is not hit with the dreaded self-employment (SE) tax, which applies to most other unincorporated profit-making ventures. The SE tax rate can be up to 15.3 percent, so it's a wonderful thing when you don't have to pay it.

One other good thing is that your net rental profits may qualify for the Section 199A deduction.

When you sell a rental property that you've owned for more than one year, the profit (the difference between the net sales proceeds and the tax basis of the property after subtracting depreciation deductions during the rental period) is generally treated as a long-term capital gain.

Always keep in mind the good news here. You don't pay the taxes on the property appreciation until you sell.

Remember those suspended passive losses we mentioned above? The suspended losses are ordinary losses. When you sell a rental, you can find two great benefits:

1. Gains are tax-favored capital gains.

2. And then, to the extent of your gains, you release suspected passive losses that offset ordinary income.

And always keep this in mind: rental real estate owners can avoid taxes indefinitely using Section 1031 exchanges (named after the applicable section of our beloved Internal Revenue Code).

The tax code totally mislabeled the 1031 exchange. It's absolutely not an exchange or a swap. It works like this:

1. You sell your property.
2. You buy a new, more expensive property.
3. Your Section 1031 exchange intermediary (such as a bank) handles the paperwork, and that makes the taxes go away.

How to Deduct Assisted Living and Nursing Home Bills

Watch your wallet: the median cost in 2018 for an assisted living facility was $48,000 and over $100,000 for nursing home care.

If you could deduct these expenses, you'd substantially reduce your income tax liability—possibly down to $0—and dramatically reduce your financial burden from these costs. As you might expect, the rules are complicated as to when you can deduct these expenses. But I'm going to give you some tips to help you understand the rules.

Medical Expenses in General

On your IRS Form 1040, you can deduct expenses paid for the medical care of yourself, your spouse, and your dependents, but only to the extent the total expenses exceed 10 percent of your adjusted gross income.

Medical care includes qualified long-term care services. Assisted living and nursing home expenses can be qualified long-term care expenses, depending on the health status of the person living in the facility.

If you operate a business, with the right circumstances, your business could establish a medical plan strategy that could turn the medical expenses into business deductions.

Qualified Long-Term Care Services

The term "qualified long-term care services" means necessary diagnostic, preventive, therapeutic, curing, treating, mitigating, and rehabilitative services, and maintenance or personal care services, which

- are required by a chronically ill individual, and
- are provided pursuant to a plan of care prescribed by a licensed health care practitioner.

Chronically Ill Individual

A chronically ill individual is someone certified within the previous 12 months by a licensed health care practitioner as

1. being unable to perform, without substantial assistance from another individual, at least two activities of daily living for a period of at least 90 days due to a loss of functional capacity;
2. having a similar level of disability (as determined under IRS regulations prescribed in consultation with the Department of Health and Human Services) to the level of disability described in the first test; or

3. requiring substantial supervision to protect the individual from threats to health and safety due to severe cognitive impairment.

A licensed health care provider is a doctor, a registered professional nurse, a licensed social worker, or another individual who meets IRS requirements.

Activities of Daily Living Test

For someone to be a chronically ill individual, at least two of the following activities of daily living must require substantial assistance from another individual:

- Eating
- Toileting
- Transferring
- Bathing
- Dressing
- Continence

Substantial assistance is both hands-on assistance and standby assistance:

- Hands-on assistance is the physical assistance of another person without which the individual would be unable to perform the activity of daily living.
- Standby assistance is the presence of another person within arm's reach of the individual that's necessary to prevent, by physical intervention, injury to the individual while the individual is performing the activity of daily living.

Examples of standby assistance include being ready to

- catch the individual if the individual falls while getting into or out of the bathtub or shower as part of bathing, or
- remove food from the individual's throat if the individual chokes while eating.

Cognitive Impairment Test

Severe cognitive impairment is a loss or deterioration in intellectual capacity that is comparable to, and includes, Alzheimer's disease and similar forms of irreversible dementia, and measured by clinical evidence and standardized tests that reliably measure impairment in the individual's short- or long-term memory; orientation as to person, place, and time; and deductive or abstract reasoning.

Substantial supervision is continual supervision (which may include cuing by verbal prompting, gestures, or other demonstrations) by another person that is necessary to protect the severely cognitively impaired individual from threats to his or her health or safety (such as may result from wandering).