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Recent Developments That May Affect Your Tax Situation

The following is a summary of the most important tax developments that have occurred in the past three months that may affect you, your family, your investments, and your livelihood. Please call us for more information about any of these developments and what steps you should implement to take advantage of favorable developments and to minimize the impact of those that are unfavorable.

Availability of premium credit for health insurance purchased on federal exchange. A credit is available for qualifying individuals who purchase health insurance on an exchange. The credit is payable in advance if the taxpayer chooses. Income affects the amount of the credit, so the taxpayer must go through a special computation when he files his return to see if he received too much or too little of the credit. A controversy has erupted concerning the credit. The statute makes the credit available for insurance purchased on an exchange established by a state. A federal exchange was established for many states that did not establish their own exchanges. The IRS has issued regulations making the credit available for insurance purchased on a federal exchange, but two Circuit Courts reached opposite results on the validity of these regulations. One upheld them, while the other said they were invalid. However, the latter decision was put on hold because, subsequently, that circuit agreed to have the issue considered by all of the judges in the circuit. Depending on what happens in that and other cases, the issue might ultimately have to be resolved by the Supreme Court.

More regulations and guidance on the premium credit. The regulations allowing the credit for insurance purchased on a federal exchange were issued in 2012. They also covered other basic matters pertaining to the credit but did not address a number of issues that could come up in specialized situations. Recently, the IRS issued additional regulations on the credit. Among other things, these regulations address the specialized situations that were left out of the 2012 regulations. For example, they explain how to reconcile advance payments with credit amounts in the case of divorced taxpayers and married taxpayers who file separately. They also provide rules for the interaction between the credit and the deduction for the health insurance costs of a self-employed individual. At the same time, the IRS, in separate guidance, provided two optional computation methods that a taxpayer can use to avoid the circular computations that would otherwise apply if he qualified for both the deduction for health insurance costs for self-employed individuals and the premium tax credit.

Publication outlines exemptions from penalty for not having health coverage. The IRS has released Publication 5172, Facts about Health Coverage Exemptions. It is a one-page outline of the exemptions from the individual shared responsibility provisions of the Affordable Care Act (ACA), also referred to as the individual mandate. Under the ACA provision, beginning in 2014, individuals and their family members must have qualified health insurance (i.e., minimum essential coverage), make a shared responsibility payment when filing their federal income tax return, or qualify for an exemption. A taxpayer obtains an exemption from either the Health Insurance Marketplace or the IRS, depending on the type. All exemptions are reported on the tax return, although a taxpayer is automatically exempt if he doesn't have to file a return because his income is below the filing threshold for his status. A brief description of the available exemptions and where a particular exemption may be obtained (IRS, Marketplace or Either) follows:

- ... Members of certain religious sects (Marketplace)
- ... Short coverage gap (IRS)
- ... Certain noncitizens (IRS)
- ... Coverage is considered unaffordable (IRS)
- ... Household income below the return filing threshold (IRS)
- ... Members of federally-recognized Indian tribes (Either)
- ... Members of health care sharing ministries (Either)
- ... Incarceration (Either)
- ... Hardships (Either depending on which hardship exemption is claimed)

Money market gains and losses simplified. Historically, money market funds were allowed to have a stable value of \$1 per share. Recently, the Securities and Exchange Commission started requiring certain money market funds to price shares in a manner that more accurately reflects the market value of the funds' underlying portfolios. With these funds, the share price "floats." If a shareholder frequently purchases and redeems shares (as is the case where the fund is used as a "sweep arrangement"), the shareholder may experience a high volume of small gains and losses. The IRS has provided a simplified method of accounting for such gains and losses. This method simplifies tax computations by basing them on the aggregate of all transactions in a period and on aggregate fair market values. The IRS also has provided an exemption from the wash sale rule (i.e., the rule that disallows a loss realized by a taxpayer on a sale or other disposition of fund shares if, within a period beginning 30 days before and ending 30 days after the date of the sale or disposition, he acquires substantially identical stock or securities) for the new floating value money market fund shares.

Favorable result for taxpayer who sold home after converting it to rental property. If certain requirements are met, a married couple filing jointly can exclude up to \$500,000 of gain on the sale of their residence. Under the passive activity losses (PAL) rules, losses from rentals and other passive activities

generally can't offset passive income, but such losses can be so used when the taxpayer disposes of his entire interest in the activity. In such cases, the freed up losses usually offset gain from the disposition. These rules could have produced a negative result for a married couple who converted their home to a rental, in the next few years had \$30,000 of losses that were suspended under the PAL rules, and then sold the home for a gain of \$100,000. The IRS determined that the gain qualified for the homesale exclusion and that the taxpayers did not have to offset the \$30,000 of losses against the \$100,000 excluded gain. This was good for the taxpayers because it meant that they could use the \$30,000 of losses to offset other income.

Simplified per-diem increase for post-Sept. 30, 2014 travel. An employer may pay a per-diem amount to an employee on business-travel status instead of reimbursing actual substantiated expenses for away-from-home lodging, meal and incidental expenses (M&IE). If the rate paid doesn't exceed IRS-approved maximums, and the employee provides simplified substantiation, the reimbursement isn't subject to income- or payroll-tax withholding and isn't reported on the employee's Form W-2. In general, the IRS-approved per-diem maximum is the GSA per-diem rate paid by the federal government to its workers on travel status. This rate varies from locality to locality. Instead of using actual per-diems, employers may use a simplified "high-low" per-diem, under which there is one uniform per-diem rate for all "high-cost" areas within the continental U.S. (CONUS), and another per-diem rate for all other areas within CONUS. The IRS released the "high-low" simplified per-diem rates for post-Sept. 30, 2014 travel. The high-cost area per-diem increases \$8 to \$259, and the low-cost area per-diem increases \$2 to \$172.

Relief gives automatic tax deferral to many in Canadian retirement plans. The IRS has provided that eligible U.S. citizens and residents who are beneficiaries of certain Canadian retirement plans will be treated as having made an election under the U.S.-Canada Income Tax Treaty to defer U.S. income tax on income accruing in their retirement plans until a distribution is made. This relief is retroactive to the first year in which they would have been entitled to make the election under the treaty.

As always, please call us (562) 463-3818 if you have any questions or would like to discuss these topics further.

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