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TAX RATES

TAX RATE SCHEDULES FOR 2017 AND 2018

NOTE. The 2017 Tax Rate Schedules reproduced below are based on the rate changes and inflation adjustments to the tax brackets released by the IRS in Rev. Proc. 2016-55. The 2018 Tax Rate Schedules reproduced below are based on the rate changes and inflation adjustments to the tax brackets released by the IRS in Rev. Proc. 2017-58.

The 2017 and 2018 tax rate schedules for single individuals are at ¶ 11; for married individuals filing jointly and surviving spouses, see ¶ 13; for married individuals filing separately, see ¶ 15; for heads of households, see ¶ 17; and for estates and nongrantor trusts, see ¶ 19.

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¶ 11 SCHEDULE X: Single Individuals

2017

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$9,325	$0		10%	$0
9,325—	37,950	932.50		15	9,325
37,950—	91,900	5,226.25		25	37,950
91,900—	191,650	18,713.75		28	91,900
191,650—	416,700	46,643.75		33	191,650
416,700—	418,400	120,910.25		35	416,700
418,400—	. . . . . .	121,505.25		39.6	418,400

2018

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$9,525	$0		10%	$0
9,525—	38,700	952.50		15	9,525
38,700—	93,700	5,328.75		25	38,700
93,700—	195,450	19,078.75		28	93,700
195,450—	424,950	47,568.75		33	195,450
424,950—	426,700	123,303.75		35	424,950
426,700—	. . . . . .	123,916.25		39.6	426,700

¶ 13 SCHEDULE Y-1: Married Filing Jointly and Surviving Spouses

2017

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$18,650	$0		10%	$0
18,650—	75,900	1,865.00		15	18,650
75,900—	153,100	10,452.50		25	75,900
153,100—	233,350	29,752.50		28	153,100
233,350—	416,700	52,222.50		33	233,350
416,700—	470,700	112,728.00		35	416,700
470,700—	......	131,628.00		39.6	470,700

2018

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$19,050	$0		10%	$0
19,050—	77,400	1,905.00		15	19,050
77,400—	156,150	10,657.50		25	77,400
156,150—	237,950	30,345.00		28	156,150
237,950—	424,950	53,249.00		33	237,950
424,950—	480,050	114,959.00		35	424,950
480,050—	......	134,244.00		39.6	480,050

¶ 15 SCHEDULE Y-2: Married Individuals Filing Separately

2017

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$9,325	$0		10%	$0
9,325—	37,950	932.50		15	9,325
37,950—	76,550	5,226.25		25	37,950
76,550—	116,675	14,876.25		28	76,550
116,675—	208,350	26,111.25		33	116,675
208,350—	235,350	56,364.00		35	208,350
235,350—	......	65,814.00		39.6	235,350

2018

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$9,525	$0		10%	$0
9,525—	38,700	952.50		15	9,525
38,700—	78,075	5,328.75		25	38,700
78,075—	118,975	15,172.50		28	78,075
118,975—	212,475	26,624.50		33	118,975
212,475—	240,025	57,479.50		35	212,475
240,025—	......	67,122.00		39.6	240,025

¶ 17 SCHEDULE Z: Heads of Households

2017

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$13,350	$0		10%	$0
13,350—	50,800	1,335.00		15	13,350
50,800—	131,200	6,952.50		25	50,800
131,200—	212,500	27,052.50		28	131,200
212,500—	416,700	49,816.50		33	212,500
416,700—	444,550	117,202.50		35	416,700
444,550—	......	126,950.00		39.6	444,550

2018

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$13,600	$0		10%	$0
13,600—	51,850	1,360.00		15	13,600
51,850—	133,850	7,097.50		25	51,850
133,850—	216,700	27,597.50		28	133,850
216,700—	424,950	50,795.50		33	216,700
424,950—	453,350	119,518.00		35	424,950
453,350—	......	129,458.00		39.6	453,350

¶ 19 INCOME TAX RATE SCHEDULES FOR USE BY ESTATES AND NONGRANTOR TRUSTS

2017

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$2,550	$0		15%	$0
2,550—	6,000	382.50		25	2,550
6,000—	9,150	1,245.00		28	6,000
9,150—	12,500	2,127.00		33	9,150
12,500—	......	3,232.50		39.6	12,500

2018

Taxable Income Over	But Not Over	Pay	+	% on Excess	of the amount over—
$0—	$2,600	$0		15%	$0
2,600—	6,100	390.00		25	2,600
6,100—	9,300	1,265.00		28	6,100
9,300—	12,700	2,161.00		33	9,300
12,700—	......	3,283.00		39.6	12,700

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»»→ Caution: This is a draft 2017 Tax Computation Worksheet. At the time of publication, the IRS had not yet released the 2017 Tax Computation Worksheet. For the latest information, see CCHGroup.com/TaxUpdates.

¶ 20 2017 Tax Computation Worksheet

2017 Tax Computation Worksheet—Line 44

See the instructions for line 44 to see if you must use the worksheet below to figure your tax.

Note. If you are required to use this worksheet to figure the tax on an amount from another form or worksheet, such as the Qualified Dividends and Capital Gain Tax Worksheet, the Schedule D Tax Worksheet, Schedule J, Form 8615, or the Foreign Earned Income Tax Worksheet, enter the amount from that form or worksheet in column (a) of the row that applies to the amount you are looking up. Enter the result on the appropriate line of the form or worksheet that you are completing.

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Section A—Use if your filing status is **Single.** Complete the row below that applies to you.

Taxable income. If line 43 is—	(a) Enter the amount from line 43	(b) Multiplication amount	(c) Multiply (a) by (b)	(d) Subtraction amount	Tax. Subtract (d) from (c). Enter the result here and on Form 1040, line 44
At least $100,000 but not over $191,650	$	× 28% (0.28)	$	$ 7,018.25	$
Over $191,650 but not over $416,700	$	× 33% (0.33)	$	$ 16,600.75	$
Over $416,700 but not over $418,400	$	× 35% (0.35)	$	$ 24,934.75	$
Over $418,400	$	× 39.6% (0.396)	$	$ 44,181.15	$

Section B—Use if your filing status is **Married filing jointly** or **Qualifying widow(er).** Complete the row below that applies to you.

Taxable income. If line 43 is—	(a) Enter the amount from line 43	(b) Multiplication amount	(c) Multiply (a) by (b)	(d) Subtraction amount	Tax. Subtract (d) from (c). Enter the result here and on Form 1040, line 44.
At least $100,000 but not over $153,100	$	× 25% (0.25)	$	$ 8,522.50	$
Over $153,100 but not over $233,350	$	× 28% (0.28)	$	$ 13,115.50	$
Over $233,350 but not over $416,700	$	× 33% (0.33)	$	$ 24,783.00	$
Over $416,700 but not over $470,700	$	× 35% (0.35)	$	$ 33,117.00	$
Over $470,700	$	× 39.6% (0.396)	$	$ 54,769.20	$

Section C—Use if your filing status is **Married filing separately.** Complete the row below that applies to you.

Taxable income. If line 43 is—	(a) Enter the amount from line 43	(b) Multiplication amount	(c) Multiply (a) by (b)	(d) Subtraction amount	Tax. Subtract (d) from (c). Enter the result here and on Form 1040, line 44.
At least $100,000 but not over $116,675	$	× 28% (0.28)	$	$ 6,557.75	$
Over $116,675 but not over $208,350	$	× 33% (0.33)	$	$ 12,391.50	$
Over $208,350 but not over $235,350	$	× 35% (0.35)	$	$ 16,558.50	$
Over $235,350	$	× 39.6% (0.396)	$	$ 27,384.60	$

Section D—Use if your filing status is **Head of household.** Complete the row below that applies to you.

Taxable income. If line 43 is—	(a) Enter the amount from line 43	(b) Multiplication amount	(c) Multiply (a) by (b)	(d) Subtraction amount	Tax. Subtract (d) from (c). Enter the result here and on Form 1040, line 44.
At least $100,000 but not over $131,200	$	× 25% (0.25)	$	$ 5,747.50	$
Over $131,200 but not over $212,500	$	× 28% (0.28)	$	$ 9,683.50	$
Over $212,500 but not over $416,700	$	× 33% (0.33)	$	$ 20,308.50	$
Over $416,700 but not over $444,550	$	× 35% (0.35)	$	$ 28,642.50	$
Over $444,550	$	× 39.6% (0.396)	$	$ 49,091.80	$

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2017 TAX TABLE—INDIVIDUALS

»»→ Caution: This is a draft 2017 Tax Table. At the time of publication, the IRS had not yet released the 2017 Tax Table. For the latest information, see CCHGroup.com/TaxUpdates.

¶ 25 2017 Tax Table for Use with Form 1040

□ The Tax Table that follows is for use with Form 1040. A similar Tax Table applies to Forms 1040A and 1040EZ.

2017 TAX TABLE Based on Taxable Income. For persons with taxable incomes of less than $100,000.

Read down the income columns of the tax table until you find the line covering the taxable income shown on line 43 of Form 1040 (line 27 of Form 1040A or line 6 of Form 1040EZ). Then read across that income line until you find the column heading that describes your filing status. Enter the tax found there on line 44 of Form 1040 (line 28 of Form 1040A or line 10 of Form 1040EZ).

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⋙ Caution: This is a draft 2017 Tax Table. At the time of publication, the IRS had not yet released the 2017 Tax Table. For the latest information, see CCHGroup.com/TaxUpdates.

2017 Tax Table

See the instructions for line 44 to see if you must use the Tax Table below to figure your tax.

Example. Mr. and Mrs. Brown are filing a joint return. Their taxable income on Form 1040, line 43, is $25,300. First, they find the $25,300-25,350 taxable income line. Next, they find the column for married filing jointly and read down the column. The amount shown where the taxable income line and filing status column meet is $2,866. This is the tax amount they should enter on Form 1040, line 44.

Sample Table

At Least	But Less Than	Single	Married filing jointly*	Married filing separately	Head of a household
		Your tax is—			
25,200	25,250	3,318	2,851	3,318	3,116
25,250	25,300	3,325	2,859	3,325	3,124
25,300	25,350	3,333	(2,866)	3,333	3,131
25,350	25,400	3,340	2,874	3,340	3,139

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If line 43 (taxable income) is—		And you are—			
At least	But less than	Single	Married filing jointly*	Married filing separately	Head of a household
		Your tax is—			
0	5	0	0	0	0
5	15	1	1	1	1
15	25	2	2	2	2
25	50	4	4	4	4
50	75	6	6	6	6
75	100	9	9	9	9
100	125	11	11	11	11
125	150	14	14	14	14
150	175	16	16	16	16
175	200	19	19	19	19
200	225	21	21	21	21
225	250	24	24	24	24
250	275	26	26	26	26
275	300	29	29	29	29
300	325	31	31	31	31
325	350	34	34	34	34
350	375	36	36	36	36
375	400	39	39	39	39
400	425	41	41	41	41
425	450	44	44	44	44
450	475	46	46	46	46
475	500	49	49	49	49
500	525	51	51	51	51
525	550	54	54	54	54
550	575	56	56	56	56
575	600	59	59	59	59
600	625	61	61	61	61
625	650	64	64	64	64
650	675	66	66	66	66
675	700	69	69	69	69
700	725	71	71	71	71
725	750	74	74	74	74
750	775	76	76	76	76
775	800	79	79	79	79
800	825	81	81	81	81
825	850	84	84	84	84
850	875	86	86	86	86
875	900	89	89	89	89
900	925	91	91	91	91
925	950	94	94	94	94
950	975	96	96	96	96
975	1,000	99	99	99	99

1,000

At least	But less than	Single	Married filing jointly*	Married filing separately	Head of a household
1,000	1,025	101	101	101	101
1,025	1,050	104	104	104	104
1,050	1,075	106	106	106	106
1,075	1,100	109	109	109	109
1,100	1,125	111	111	111	111
1,125	1,150	114	114	114	114
1,150	1,175	116	116	116	116
1,175	1,200	119	119	119	119
1,200	1,225	121	121	121	121
1,225	1,250	124	124	124	124
1,250	1,275	126	126	126	126
1,275	1,300	129	129	129	129
1,300	1,325	131	131	131	131
1,325	1,350	134	134	134	134
1,350	1,375	136	136	136	136
1,375	1,400	139	139	139	139
1,400	1,425	141	141	141	141
1,425	1,450	144	144	144	144
1,450	1,475	146	146	146	146
1,475	1,500	149	149	149	149
1,500	1,525	151	151	151	151
1,525	1,550	154	154	154	154
1,550	1,575	156	156	156	156
1,575	1,600	159	159	159	159
1,600	1,625	161	161	161	161
1,625	1,650	164	164	164	164
1,650	1,675	166	166	166	166
1,675	1,700	169	169	169	169
1,700	1,725	171	171	171	171
1,725	1,750	174	174	174	174
1,750	1,775	176	176	176	176
1,775	1,800	179	179	179	179
1,800	1,825	181	181	181	181
1,825	1,850	184	184	184	184
1,850	1,875	186	186	186	186
1,875	1,900	189	189	189	189
1,900	1,925	191	191	191	191
1,925	1,950	194	194	194	194
1,950	1,975	196	196	196	196
1,975	2,000	199	199	199	199

2,000

At least	But less than	Single	Married filing jointly*	Married filing separately	Head of a household
2,000	2,025	201	201	201	201
2,025	2,050	204	204	204	204
2,050	2,075	206	206	206	206
2,075	2,100	209	209	209	209
2,100	2,125	211	211	211	211
2,125	2,150	214	214	214	214
2,150	2,175	216	216	216	216
2,175	2,200	219	219	219	219
2,200	2,225	221	221	221	221
2,225	2,250	224	224	224	224
2,250	2,275	226	226	226	226
2,275	2,300	229	229	229	229
2,300	2,325	231	231	231	231
2,325	2,350	234	234	234	234
2,350	2,375	236	236	236	236
2,375	2,400	239	239	239	239
2,400	2,425	241	241	241	241
2,425	2,450	244	244	244	244
2,450	2,475	246	246	246	246
2,475	2,500	249	249	249	249
2,500	2,525	251	251	251	251
2,525	2,550	254	254	254	254
2,550	2,575	256	256	256	256
2,575	2,600	259	259	259	259
2,600	2,625	261	261	261	261
2,625	2,650	264	264	264	264
2,650	2,675	266	266	266	266
2,675	2,700	269	269	269	269
2,700	2,725	271	271	271	[illegible]
2,725	2,750	274	274	274	[illegible]
2,750	2,775	276	276	276	[illegible]
2,775	2,800	279	279	279	279
2,800	2,825	281	281	281	281
2,825	2,850	284	284	284	284
2,850	2,875	286	286	[illegible]	286
2,875	2,900	289	289	289	289
2,900	2,925	291	[illegible]	291	291
2,925	2,950	294	294	294	294
2,950	2,975	[illegible]	[illegible]	296	296
2,975	3,000	[illegible]	299	299	299

* This column must also be used by a qualifying widow(er).

(Continued)

⋙ Caution: This is a draft 2017 Tax Table. At the time of publication, the IRS had not yet released the 2017 Tax Table. For the latest information, see CCHGroup.com/TaxUpdates.

2017 Tax Table — *Continued*

DRAFT AS OF September 29, 2017

If line 43 (taxable income) is—		And you are—			
At least	But less than	Single	Married filing jointly*	Married filing separately	Head of a household
		Your tax is—			
3,000					
3,000	3,050	303	303	303	303
3,050	3,100	308	308	308	308
3,100	3,150	313	313	313	313
3,150	3,200	318	318	318	318
3,200	3,250	323	323	323	323
3,250	3,300	328	328	328	328
3,300	3,350	333	333	333	333
3,350	3,400	338	338	338	338
3,400	3,450	343	343	343	343
3,450	3,500	348	348	348	348
3,500	3,550	353	353	353	353
3,550	3,600	358	358	358	358
3,600	3,650	363	363	363	363
3,650	3,700	368	368	368	368
3,700	3,750	[illegible]	373	373	373
3,750	3,800	[illegible]	378	378	378
3,800	3,850	383	383	383	383
3,850	3,900	[illegible]	388	388	388
3,900	3,950	393	393	393	393
3,950	4,000	398	398	398	398
4,000					
4,000	4,050	403	403	403	403
4,050	4,100	408	408	408	408
4,100	4,150	413	413	413	413
4,150	4,200	418	418	418	418
4,200	4,250	423	423	423	423
4,250	4,300	428	428	428	428
4,300	4,350	433	433	433	433
4,350	4,400	438	438	438	438
4,400	4,450	443	443	443	443
4,450	4,500	448	448	448	448
4,500	4,550	453	453	453	453
4,550	4,600	458	458	458	458
4,600	4,650	463	463	463	463
4,650	4,700	468	468	468	468
4,700	4,750	473	473	473	473
4,750	4,800	478	478	478	478
4,800	4,850	483	483	483	483
4,850	4,900	488	488	488	488
4,900	4,950	493	493	493	493
4,950	5,000	498	498	498	498
5,000					
5,000	5,050	503	503	503	503
5,050	5,100	508	508	508	508
5,100	5,150	513	513	513	513
5,150	5,200	518	518	518	518
5,200	5,250	523	523	523	523
5,250	5,300	528	528	528	528
5,300	5,350	533	533	533	533
5,350	5,400	538	538	538	538
5,400	5,450	543	543	543	543
5,450	5,500	548	548	548	548
5,500	5,550	553	553	553	553
5,550	5,600	558	558	558	558
5,600	5,650	563	563	563	563
5,650	5,700	568	568	568	568
5,700	5,750	573	573	573	573
5,750	5,800	578	578	578	578
5,800	5,850	583	583	583	583
5,850	5,900	588	588	588	588
5,900	5,950	593	593	593	593
5,950	6,000	598	598	598	598

At least	But less than	Single	Married filing jointly*	Married filing separately	Head of a household
6,000					
6,000	6,050	603	603	603	603
6,050	6,100	608	608	608	608
6,100	6,150	613	613	613	613
6,150	6,200	618	618	618	618
6,200	6,250	623	623	623	623
6,250	6,300	628	628	628	628
6,300	6,350	633	633	633	633
6,350	6,400	638	638	638	638
6,400	6,450	643	643	643	643
6,450	6,500	648	648	648	648
6,500	6,550	653	653	653	653
6,550	6,600	658	658	658	658
6,600	6,650	663	663	663	663
6,650	6,700	668	668	668	668
6,700	6,750	673	673	673	673
6,750	6,800	678	678	678	678
6,800	6,850	683	683	683	683
6,850	6,900	688	688	688	688
6,900	6,950	693	693	693	693
6,950	7,000	698	698	698	698
7,000					
7,000	7,050	703	703	703	703
7,050	7,100	708	708	708	708
7,100	7,150	713	713	713	713
7,150	7,200	718	718	718	718
7,200	7,250	723	723	723	723
7,250	7,300	728	728	728	728
7,300	7,350	733	733	733	733
7,350	7,400	738	738	738	738
7,400	7,450	743	743	743	743
7,450	7,500	748	748	748	748
7,500	7,550	753	753	753	753
7,550	7,600	758	758	758	758
7,600	7,650	763	763	763	763
7,650	7,700	768	768	768	768
7,700	7,750	773	773	773	773
7,750	7,800	778	778	778	778
7,800	7,850	783	783	783	783
7,850	7,900	788	788	788	788
7,900	7,950	793	793	793	793
7,950	8,000	798	798	798	798
8,000					
8,000	8,050	803	803	803	803
8,050	8,100	808	808	808	808
8,100	8,150	813	813	813	813
8,150	8,200	818	818	818	818
8,200	8,250	823	823	823	823
8,250	8,300	828	828	828	828
8,300	8,350	833	833	833	833
8,350	8,400	838	838	838	838
8,400	8,450	843	843	843	843
8,450	8,500	848	848	848	848
8,500	8,550	853	853	853	853
8,550	8,600	858	858	858	858
8,600	8,650	863	863	863	863
8,650	8,700	868	868	868	868
8,700	8,750	873	873	873	873
8,750	8,800	878	878	878	878
8,800	8,850	883	883	883	883
8,850	8,900	888	888	888	888
8,900	8,950	893	893	893	893
8,950	9,000	898	898	898	898

At least	But less than	Single	Married filing jointly*	Married filing separately	Head of a household
9,000					
9,000	9,050	903	903	903	903
9,050	9,100	908	908	908	908
9,100	9,150	913	913	913	913
9,150	9,200	918	918	918	918
9,200	9,250	923	923	923	923
9,250	9,300	928	928	928	928
9,300	9,350	933	933	933	933
9,350	9,400	940	938	940	938
9,400	9,450	948	943	948	943
9,450	9,500	955	948	955	948
9,500	9,550	963	953	963	953
9,550	9,600	970	958	970	958
9,600	9,650	978	963	978	963
9,650	9,700	985	968	985	968
9,700	9,750	993	973	993	973
9,750	9,800	1,000	978	1,000	978
9,800	9,850	1,008	983	1,008	983
9,850	9,900	1,015	988	1,015	988
9,900	9,950	1,023	993	1,023	993
9,950	10,000	1,030	998	1,030	998
10,000					
10,000	10,050	1,038	1,003	1,038	1,003
10,050	10,100	1,045	1,008	1,045	1,008
10,100	10,150	1,053	1,013	1,053	1,013
10,150	10,200	1,060	1,018	1,060	1,018
10,200	10,250	1,068	1,023	1,068	1,023
10,250	10,300	1,075	1,028	1,075	1,028
10,300	10,350	1,083	1,033	1,083	1,033
10,350	10,400	1,090	1,038	1,090	1,038
10,400	10,450	1,098	1,043	1,098	1,043
10,450	10,500	1,105	1,048	1,105	1,048
10,500	10,550	1,113	1,053	1,113	1,053
10,550	10,600	1,120	1,058	1,120	1,058
10,600	10,650	1,128	1,063	1,128	1,063
10,650	10,700	1,135	1,068	1,135	1,068
10,700	10,750	1,143	1,073	1,143	1,073
10,750	10,800	1,150	1,078	1,150	1,078
10,800	10,850	1,158	1,083	1,158	1,083
10,850	10,900	1,165	1,088	1,165	1,088
10,900	10,950	1,173	1,093	1,173	1,093
10,950	11,000	1,180	1,098	1,180	1,098
11,000					
11,000	11,050	1,188	1,103	1,188	1,103
11,050	11,100	1,195	1,108	1,195	1,108
11,100	11,150	1,203	1,113	1,203	1,113
11,150	11,200	1,210	1,118	1,210	1,118
11,200	11,250	1,218	1,123	1,218	1,123
11,250	11,300	1,225	1,128	1,225	1,128
11,300	11,350	1,233	1,133	1,233	1,133
11,350	11,400	1,240	1,138	1,240	1,138
11,400	11,450	1,248	1,143	1,248	1,143
11,450	11,500	1,255	1,148	1,255	1,148
11,500	11,550	1,263	1,153	1,263	1,153
11,550	11,600	1,270	1,158	1,270	1,158
11,600	11,650	1,278	1,163	1,278	1,163
11,650	11,700	1,285	1,168	1,285	1,168
11,700	11,750	1,293	1,173	1,293	1,173
11,750	11,800	1,300	1,178	1,300	1,178
11,800	11,850	1,308	1,183	1,308	1,183
11,850	11,900	1,315	1,188	1,315	1,188
11,900	11,950	1,323	1,193	1,323	1,193
11,950	12,000	1,330	1,198	1,330	1,198

* This column must also be used by a qualifying widow(er).

(Continued)

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⋙→ Caution: This is a draft 2017 Tax Table. At the time of publication, the IRS had not yet released the 2017 Tax Table. For the latest information, see CCHGroup.com/TaxUpdates.

DRAFT AS OF September 29, 2017

2017 Tax Table — *Continued*

If line 43 (taxable income) is— At least	But less than	And you are— Single	Married filing jointly *	Married filing separately	Head of a household
		Your tax is—			
12,000					
12,000	12,050	1,338	1,203	1,338	1,203
12,050	12,100	1,345	1,208	1,345	1,208
12,100	12,150	1,353	1,213	1,353	1,213
12,150	12,200	1,360	1,218	1,360	1,218
12,200	12,250	1,368	1,223	1,368	1,223
12,250	12,300	1,375	1,228	1,375	1,228
12,300	12,350	1,383	1,233	1,383	1,233
12,350	12,400	1,390	1,238	1,390	1,238
12,400	12,450	1,398	1,243	1,398	1,243
12,450	12,500	1,405	1,248	1,405	1,248
12,500	12,550	1,413	1,253	1,413	1,253
12,550	12,600	1,420	1,258	1,420	1,258
12,600	12,650	1,428	1,263	1,428	1,263
12,650	12,700	1,435	1,268	1,435	1,268
12,700	12,750	1,443	1,273	1,443	1,273
12,750	12,800	1,450	1,278	1,450	1,278
12,800	12,850	1,458	1,283	1,458	1,283
12,850	12,900	1,465	1,288	1,465	1,288
12,900	12,950	1,473	1,293	1,473	1,293
12,950	13,000	1,480	1,298	1,480	1,298
13,000					
13,000	13,050	1,488	1,303	1,488	1,303
13,050	13,100	1,495	1,308	1,495	1,308
13,100	13,150	1,503	1,313	1,503	1,313
13,150	13,200	1,510	1,318	1,510	1,318
13,200	13,250	1,518	1,323	1,518	1,323
13,250	13,300	1,525	1,328	1,525	1,328
13,300	13,350	1,533	1,333	1,533	1,333
13,350	13,400	1,540	1,338	1,540	1,339
13,400	13,450	1,548	1,343	1,548	1,346
13,450	13,500	1,555	1,348	1,555	1,354
13,500	13,550	1,563	1,353	1,563	1,361
13,550	13,600	1,570	1,358	1,570	1,369
13,600	13,650	1,578	1,363	1,578	1,376
13,650	13,700	1,585	1,368	1,585	1,384
13,700	13,750	1,593	1,373	1,593	1,391
13,750	13,800	1,600	1,378	1,600	1,399
13,800	13,850	1,608	1,383	1,608	1,406
13,850	13,900	1,615	1,388	1,615	1,414
13,900	13,950	1,623	1,393	1,623	1,421
13,950	14,000	1,630	1,398	1,630	1,429
14,000					
14,000	14,050	1,638	1,403	1,638	1,436
14,050	14,100	1,645	1,408	1,645	1,444
14,100	14,150	1,653	1,413	1,653	1,451
14,150	14,200	1,660	1,418	1,660	1,459
14,200	14,250	1,668	1,423	1,668	1,466
14,250	14,300	1,675	1,428	1,675	1,474
14,300	14,350	1,683	1,433	1,683	1,481
14,350	14,400	1,690	1,438	1,690	1,489
14,400	14,450	1,698	1,443	1,698	1,496
14,450	14,500	1,705	1,448	1,705	1,504
14,500	14,550	1,713	1,453	1,713	1,511
14,550	14,600	1,720	1,458	1,720	1,519
14,600	14,650	1,728	1,463	1,728	1,526
14,650	14,700	1,735	1,468	1,735	1,534
14,700	14,750	1,743	1,473	1,743	1,541
14,750	14,800	1,750	1,478	1,750	1,549
14,800	14,850	1,758	1,483	1,758	1,556
14,850	14,900	1,765	1,488	1,765	1,564
14,900	14,950	1,773	1,493	1,773	1,571
14,950	15,000	1,780	1,498	1,780	1,579
15,000					
15,000	15,050	1,788	1,503	1,788	1,586
15,050	15,100	1,795	1,508	1,795	1,594
15,100	15,150	1,803	1,513	1,803	1,601
15,150	15,200	1,810	1,518	1,810	1,609
15,200	15,250	1,818	1,523	1,818	1,616
15,250	15,300	1,825	1,528	1,825	1,624
15,300	15,350	1,833	1,533	1,833	1,631
15,350	15,400	1,840	1,538	1,840	1,639
15,400	15,450	1,848	1,543	1,848	1,646
15,450	15,500	1,855	1,548	1,855	1,654
15,500	15,550	1,863	1,553	1,863	1,661
15,550	15,600	1,870	1,558	1,870	1,669
15,600	15,650	1,878	1,563	1,878	1,676
15,650	15,700	1,885	1,568	1,885	1,684
15,700	15,750	1,893	1,573	1,893	1,691
15,750	15,800	1,900	1,578	1,900	1,699
15,800	15,850	1,908	1,583	1,908	1,706
15,850	15,900	1,915	1,588	1,915	1,714
15,900	15,950	1,923	1,593	1,923	1,721
15,950	16,000	1,930	1,598	1,930	1,729
16,000					
16,000	16,050	1,938	1,603	1,938	1,736
16,050	16,100	1,945	1,608	1,945	1,744
16,100	16,150	1,953	1,613	1,953	1,751
16,150	16,200	1,960	1,618	1,960	1,759
16,200	16,250	1,968	1,623	1,968	1,766
16,250	16,300	1,975	1,628	1,975	1,774
16,300	16,350	1,983	1,633	1,983	1,781
16,350	16,400	1,990	1,638	1,990	1,789
16,400	16,450	1,998	1,643	1,998	1,796
16,450	16,500	2,005	1,648	2,005	1,804
16,500	16,550	2,013	1,653	2,013	1,811
16,550	16,600	2,020	1,658	2,020	1,819
16,600	16,650	2,028	1,663	2,028	1,826
16,650	16,700	2,035	1,668	2,035	1,834
16,700	16,750	2,043	1,673	2,043	1,841
16,750	16,800	2,050	1,678	2,050	1,849
16,800	16,850	2,058	1,683	2,058	1,856
16,850	16,900	2,065	1,688	2,065	1,864
16,900	16,950	2,073	1,693	2,073	1,871
16,950	17,000	2,080	1,698	2,080	1,879
17,000					
17,000	17,050	2,088	1,703	2,088	1,886
17,050	17,100	2,095	1,708	2,095	1,894
17,100	17,150	2,103	1,713	2,103	1,901
17,150	17,200	2,110	1,718	2,110	1,909
17,200	17,250	2,118	1,723	2,118	1,916
17,250	17,300	2,125	1,728	2,125	1,924
17,300	17,350	2,133	1,733	2,133	1,931
17,350	17,400	2,140	1,738	2,140	1,939
17,400	17,450	2,148	1,743	2,148	1,946
17,450	17,500	2,155	1,748	2,155	1,954
17,500	17,550	2,163	1,753	2,163	1,961
17,550	17,600	2,170	1,758	2,170	1,969
17,600	17,650	2,178	1,763	2,178	1,976
17,650	17,700	2,185	1,768	2,185	1,984
17,700	17,750	2,193	1,773	2,193	1,991
17,750	17,800	2,200	1,778	2,200	1,999
17,800	17,850	2,208	1,783	2,208	2,006
17,850	17,900	2,215	1,788	2,215	2,014
17,900	17,950	2,223	1,793	2,223	2,021
17,950	18,000	2,230	1,798	2,230	2,029
18,000					
18,000	18,050	2,238	1,803	2,238	2,036
18,050	18,100	2,245	1,808	2,245	2,044
18,100	18,150	2,253	1,813	2,253	2,051
18,150	18,200	2,260	1,818	2,260	2,059
18,200	18,250	2,268	1,823	2,268	2,066
18,250	18,300	2,275	1,828	2,275	2,074
18,300	18,350	2,283	1,833	2,283	2,081
18,350	18,400	2,290	1,838	2,290	2,089
18,400	18,450	2,298	1,843	2,298	2,096
18,450	18,500	2,305	1,848	2,305	2,104
18,500	18,550	2,313	1,853	2,313	2,111
18,550	18,600	2,320	1,858	2,320	2,119
18,600	18,650	2,328	1,863	2,328	2,126
18,650	18,700	2,335	1,869	2,335	2,134
18,700	18,750	2,343	1,876	2,343	2,141
18,750	18,800	2,350	1,884	2,350	2,149
18,800	18,850	2,358	1,891	2,358	2,156
18,850	18,900	2,365	1,899	2,365	2,164
18,900	18,950	2,373	1,906	2,373	2,171
18,950	19,000	2,380	1,914	2,380	2,179
19,000					
19,000	19,050	2,388	1,921	2,368	2,186
19,050	19,100	2,395	1,929	2,395	2,194
19,100	19,150	2,403	1,936	2,403	2,201
19,150	19,200	2,410	1,944	2,410	2,209
19,200	19,250	2,418	1,951	2,418	2,216
19,250	19,300	2,425	1,959	2,425	2,224
19,300	19,350	2,433	1,966	2,433	2,231
19,350	19,400	2,440	1,974	2,440	2,239
19,400	19,450	2,448	1,981	2,448	2,246
19,450	19,500	2,455	1,989	2,455	2,254
19,500	19,550	2,463	1,996	2,463	2,261
19,550	19,600	2,470	2,004	2,470	2,269
19,600	19,650	2,478	2,011	2,478	2,276
19,650	19,700	2,485	2,019	2,485	2,284
19,700	19,750	2,493	2,026	2,493	2,291
19,750	19,800	2,500	2,034	2,500	2,299
19,800	19,850	2,508	2,041	2,508	2,306
19,850	19,900	2,515	2,049	2,515	2,314
19,900	19,950	2,523	2,056	2,523	2,321
19,950	20,000	2,530	2,064	2,530	2,329
20,000					
20,000	20,050	2,538	2,071	2,538	2,336
20,050	20,100	2,545	2,079	2,545	2,344
20,100	20,150	2,553	2,086	2,553	2,351
20,150	20,200	2,560	2,094	2,560	2,359
20,200	20,250	2,568	[illegible]	2,568	2,366
20,250	20,300	2,575	2,109	2,575	2,374
20,300	20,350	2,583	[illegible]	2,583	2,381
20,350	20,400	[illegible]	2,124	2,590	2,389
20,400	20,450	[illegible]	2,131	2,598	2,396
20,450	20,500	[illegible]	2,139	2,605	2,404
20,500	20,550	2,613	2,146	2,613	2,411
20,550	20,600	2,620	2,154	2,620	2,419
20,600	20,650	2,628	2,161	2,628	2,426
20,650	20,700	2,635	2,169	2,635	2,434
20,700	20,750	2,643	2,176	2,643	2,441
20,750	20,800	2,650	2,184	2,650	2,449
20,800	20,850	2,658	2,191	2,658	2,456
20,850	20,900	2,665	2,199	2,665	2,464
20,900	20,950	2,673	2,206	2,673	2,471
20,950	21,000	2,680	2,214	2,680	2,479

(Continued)

* This column must also be used by a qualifying widow(er).

⋙→ Caution: This is a draft 2017 Tax Table. At the time of publication, the IRS had not yet released the 2017 Tax Table. For the latest information, see CCHGroup.com/TaxUpdates.

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2017 Tax Table — *Continued*

If line 43 (taxable income) is— At least	But less than	And you are— Single	Married filing jointly *	Married filing separately	Head of a household
		Your tax is—			
21,000					
21,000	21,050	2,688	2,221	2,688	2,486
21,050	21,100	2,695	2,229	2,695	2,494
21,100	21,150	2,703	2,236	2,703	2,501
21,150	21,200	2,710	2,244	2,710	2,509
21,200	21,250	2,718	2,251	2,718	2,516
21,250	21,300	2,725	2,259	2,725	2,524
21,300	21,350	2,733	2,266	2,733	2,531
21,350	21,400	2,740	2,274	2,740	2,539
21,400	21,450	2,748	2,281	2,748	2,546
21,450	21,500	2,755	2,289	2,755	2,554
21,500	21,550	2,763	2,296	2,763	2,561
21,550	21,600	2,770	2,304	2,770	2,569
21,600	21,650	2,778	2,311	2,778	2,576
21,650	21,700	2,785	2,319	2,785	2,584
21,700	21,750	2,793	2,326	2,793	2,591
21,750	21,800	2,800	2,334	2,800	2,599
21,800	21,850	2,808	2,341	2,808	2,606
21,850	21,900	2,815	2,349	2,815	2,614
21,900	21,950	2,823	2,356	2,823	2,621
21,950	22,000	2,830	2,364	2,830	2,629
22,000					
22,000	22,050	2,838	2,371	2,838	2,636
22,050	22,100	2,845	2,379	2,845	2,644
22,100	22,150	2,853	2,386	2,853	2,651
22,150	22,200	2,860	2,394	2,860	2,659
22,200	22,250	2,868	2,401	2,868	2,666
22,250	22,300	2,875	2,409	2,875	2,674
22,300	22,350	2,883	2,416	2,883	2,681
22,350	22,400	2,890	2,424	2,890	2,689
22,400	22,450	2,898	2,431	2,898	2,696
22,450	22,500	2,905	2,439	2,905	2,704
22,500	22,550	2,913	2,446	2,913	2,711
22,550	22,600	2,920	2,454	2,920	2,719
22,600	22,650	2,928	2,461	2,928	2,726
22,650	22,700	2,935	2,469	2,935	2,734
22,700	22,750	2,943	2,476	2,943	2,741
22,750	22,800	2,950	2,484	2,950	2,749
22,800	22,850	2,958	2,491	2,958	2,756
22,850	22,900	2,965	2,499	2,965	2,764
22,900	22,950	2,973	2,506	2,973	2,771
22,950	23,000	2,980	2,514	2,980	2,779
23,000					
23,000	23,050	2,988	2,521	2,988	2,786
23,050	23,100	2,995	2,529	2,995	2,794
23,100	23,150	3,003	2,536	3,003	2,801
23,150	23,200	3,010	2,544	3,010	2,809
23,200	23,250	3,018	2,551	3,018	2,816
23,250	23,300	3,025	2,559	3,025	2,824
23,300	23,350	3,033	2,566	3,033	2,831
23,350	23,400	3,040	2,574	3,040	2,839
23,400	23,450	3,048	2,581	3,048	2,846
23,450	23,500	3,055	2,589	3,055	2,854
23,500	23,550	3,063	2,596	3,063	2,861
23,550	23,600	3,070	2,604	3,070	2,869
23,600	23,650	3,078	2,611	3,078	2,876
23,650	23,700	3,085	2,619	3,085	2,884
23,700	23,750	3,093	2,626	3,093	2,891
23,750	23,800	3,100	2,634	3,100	2,899
23,800	23,850	3,108	2,641	3,108	2,906
23,850	23,900	3,115	2,649	3,115	2,914
23,900	23,950	3,123	2,656	3,123	2,921
23,950	24,000	3,130	2,664	3,130	2,929
24,000					
24,000	24,050	3,138	2,671	3,138	2,936
24,050	24,100	3,145	2,679	3,145	2,944
24,100	24,150	3,153	2,686	3,153	2,951
24,150	24,200	3,160	2,694	3,160	2,959
24,200	24,250	3,168	2,701	3,168	2,966
24,250	24,300	3,175	2,709	3,175	2,974
24,300	24,350	3,183	2,716	3,183	2,981
24,350	24,400	3,190	2,724	3,190	2,989
24,400	24,450	3,198	2,731	3,198	2,996
24,450	24,500	3,205	2,739	3,205	3,004
24,500	24,550	3,213	2,746	3,213	3,011
24,550	24,600	3,220	2,754	3,220	3,019
24,600	24,650	3,228	2,761	3,228	3,026
24,650	24,700	3,235	2,769	3,235	3,034
24,700	24,750	3,243	2,776	3,243	3,041
24,750	24,800	3,250	2,784	3,250	3,049
24,800	24,850	3,258	2,791	3,258	3,056
24,850	24,900	3,265	2,799	3,265	3,064
24,900	24,950	3,273	2,806	3,273	3,071
24,950	25,000	3,280	2,814	3,280	3,079
25,000					
25,000	25,050	3,288	2,821	3,288	3,086
25,050	25,100	3,295	2,829	3,295	3,094
25,100	25,150	3,303	2,836	3,303	3,101
25,150	25,200	3,310	2,844	3,310	3,109
25,200	25,250	3,318	2,851	3,318	3,116
25,250	25,300	3,325	2,859	3,325	3,124
25,300	25,350	3,333	2,866	3,333	3,131
25,350	25,400	3,340	2,874	3,340	3,139
25,400	25,450	3,348	2,881	3,348	3,146
25,450	25,500	3,355	2,889	3,355	3,154
25,500	25,550	3,363	2,896	3,363	3,161
25,550	25,600	3,370	2,904	3,370	3,169
25,600	25,650	3,378	2,911	3,378	3,176
25,650	25,700	3,385	2,919	3,385	3,184
25,700	25,750	3,393	2,926	3,393	3,191
25,750	25,800	3,400	2,934	3,400	3,199
25,800	25,850	3,408	2,941	3,408	3,206
25,850	25,900	3,415	2,949	3,415	3,214
25,900	25,950	3,423	2,956	3,423	3,221
25,950	26,000	3,430	2,964	3,430	3,229
26,000					
26,000	26,050	3,438	2,971	3,438	3,236
26,050	26,100	3,445	2,979	3,445	3,244
26,100	26,150	3,453	2,986	3,453	3,251
26,150	26,200	3,460	2,994	3,460	3,259
26,200	26,250	3,468	3,001	3,468	3,266
26,250	26,300	3,475	3,009	3,475	3,274
26,300	26,350	3,483	3,016	3,483	3,281
26,350	26,400	3,490	3,024	3,490	3,289
26,400	26,450	3,498	3,031	3,498	3,296
26,450	26,500	3,505	3,039	3,505	3,304
26,500	26,550	3,513	3,046	3,513	3,311
26,550	26,600	3,520	3,054	3,520	3,319
26,600	26,650	3,528	3,061	3,528	3,326
26,650	26,700	3,535	3,069	3,535	3,334
26,700	26,750	3,543	3,076	3,543	3,341
26,750	26,800	3,550	3,084	3,550	3,349
26,800	26,850	3,558	3,091	3,558	3,356
26,850	26,900	3,565	3,099	3,565	3,364
26,900	26,950	3,573	3,106	3,573	3,371
26,950	27,000	3,580	3,114	3,580	3,379
27,000					
27,000	27,050	3,588	3,121	3,588	3,386
27,050	27,100	3,595	3,129	3,595	3,394
27,100	27,150	3,603	3,136	3,603	3,401
27,150	27,200	3,610	3,144	3,610	3,409
27,200	27,250	3,618	3,151	3,618	3,416
27,250	27,300	3,625	3,159	3,625	3,424
27,300	27,350	3,633	3,166	3,633	3,431
27,350	27,400	3,640	3,174	3,640	3,439
27,400	27,450	3,648	3,181	3,648	3,446
27,450	27,500	3,655	3,189	3,655	3,454
27,500	27,550	3,663	3,196	3,663	3,461
27,550	27,600	3,670	3,204	3,670	3,469
27,600	27,650	3,678	3,211	3,678	3,476
27,650	27,700	3,685	3,219	3,685	3,484
27,700	27,750	3,693	3,226	3,693	3,491
27,750	27,800	3,700	3,234	3,700	3,499
27,800	27,850	3,708	3,241	3,708	3,506
27,850	27,900	3,715	3,249	3,715	3,514
27,900	27,950	3,723	3,256	3,723	3,521
27,950	28,000	3,730	3,264	3,730	3,529
28,000					
28,000	28,050	3,738	3,271	3,738	3,536
28,050	28,100	3,745	3,279	3,745	3,544
28,100	28,150	3,753	3,286	3,753	3,551
28,150	28,200	3,760	3,294	3,760	3,559
28,200	28,250	3,768	3,301	3,768	3,566
28,250	28,300	3,775	3,309	3,775	3,574
28,300	28,350	3,783	3,316	3,783	3,581
28,350	28,400	3,790	3,324	3,790	3,589
28,400	28,450	3,798	3,331	3,798	3,596
28,450	28,500	3,805	3,339	3,805	3,604
28,500	28,550	3,813	3,346	3,813	3,611
28,550	28,600	3,820	3,354	3,820	3,619
28,600	28,650	3,828	3,361	3,828	3,626
28,650	28,700	3,835	3,369	3,835	3,634
28,700	28,750	3,843	3,376	3,843	3,641
28,750	28,800	3,850	3,384	3,850	3,649
28,800	28,850	3,858	3,391	3,858	3,656
28,850	28,900	3,865	3,399	3,865	3,664
28,900	28,950	3,873	3,406	3,873	3,671
28,950	29,000	3,880	3,414	3,880	3,679
29,000					
29,000	29,050	3,888	3,421	3,888	3,696
29,050	29,100	3,895	3,429	3,895	3,694
29,100	29,150	3,903	3,436	3,903	3,701
29,150	29,200	3,910	3,444	3,910	3,709
29,200	29,250	3,918	3,451	3,918	3,716
29,250	29,300	3,925	3,459	3,925	3,724
29,300	29,350	3,933	3,466	3,933	3,731
29,350	29,400	3,940	3,474	3,940	3,739
29,400	29,450	3,948	3,481	3,948	3,746
29,450	29,500	3,955	3,489	3,955	3,754
29,500	29,550	3,963	3,496	3,963	3,761
29,550	29,600	3,970	3,504	3,970	3,769
29,600	29,650	3,978	3,511	3,978	3,776
29,650	29,700	3,985	3,519	3,985	3,784
29,700	29,750	3,993	3,526	3,993	3,791
29,750	29,800	4,000	3,534	4,000	3,799
29,800	29,850	4,008	3,541	4,008	3,806
29,850	29,900	4,015	3,549	4,015	3,814
29,900	29,950	4,023	3,556	4,023	3,821
29,950	30,000	4,030	3,564	4,030	3,829

(Continued)

* This column must also be used by a qualifying widow(er).

Chapter 9

BUSINESS EXPENSES

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Trade or Business Expenses

901. Deductibility of Business Expenses—Generally. An individual, corporation, partnership, trust, or estate generally may deduct from gross income the ordinary and necessary expenses of carrying on a trade or business that are paid or incurred during the tax year (Code Sec. 162; Reg. § 1.162-1).[1] Business expenses incurred by a cash-basis taxpayer while conducting a business but paid in a year after terminating the business are deductible as business expenses in the year paid (Rev. Rul. 67-12).[2] However, a deduction is not permitted for any expenditure that is a capital expense (¶ 903). Expenses for property used for both business and personal activities must be allocated between the different activities. The origin and character of a claim control whether an expense is a deductible business expense or a nondeductible personal expense.

Ordinary and Necessary. Whether a business expense is ordinary and necessary is based on the facts surrounding the expense. An expense is necessary if it is appropriate and helpful to the taxpayer's business (*S.B. Heininger*, SCt, 44-1 USTC ¶ 9109).[3] An expense is ordinary if it is one that is common and accepted in the particular business activity.

Trade or Business. The term "trade or business" is not defined in the Internal Revenue Code, but is characterized as an activity carried on for a livelihood or for profit. A profit motive must be present and some type of economic activity must be conducted. In determining whether an activity is engaged in for profit, all facts and circumstances with respect to the activity are taken into account (Reg. § 1.183-2(b)).[4] No one factor is conclusive in making this determination. In addition, it is not intended that only the factors described below are to be taken into account in making the determination, or

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[1] ¶ 8500, ¶ 8501; BUSEXP: 3,100; § 9,001

[2] ¶ 8520.1546; BUSEXP: 3,058.20; § 9,001

[3] ¶ 8520.517; BUSEXP: 3,100; § 9,010.05

[4] ¶ 12,173; BUSEXP: 15,150; § 17,210.05

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that a determination is to be made on the basis that the number of factors, whether or not listed in the regulations, indicating a lack of profit objective exceeds the number of factors indicating a profit objective, or vice versa. Among the factors that should normally be taken into account are the following: the manner in which the taxpayer carries on the activity; the expertise of the taxpayer or his or her advisors; the time and effort expended by the taxpayer in carrying on the activity; the expectation that assets used in the activity may appreciate in value; the success of the taxpayer in carrying on other similar or dissimilar activities; the taxpayer's history of income or losses with respect to the activity; the amount of occasional profits, if any, that are earned; the financial status of the taxpayer; and elements of personal pleasure or recreation.

903. Capital Expenditures. A taxpayer may not currently deduct a capital expenditure. A capital expenditure is: (1) any amount paid out for new buildings, permanent improvements, or betterments made to increase the value of any property or estate; or (2) any amount expended in restoring property or in making good the exhaustion thereof for which an allowance has been made (Code Sec. 263; Reg. § 1.263(a)-1).[5] Capital expenditures are included in basis (¶ 1611) and generally recovered through depreciation, amortization, or depletion (¶ 1201). Amounts paid or incurred for incidental repairs and maintenance of property are not capital expenditures.

Capital expenses include amounts paid to produce or acquire tangible or intangible property, to improve tangible property, to facilitate the acquisition of a trade or business or a change in a business entity's capital structure, or to acquire or create an interest in land. They also include amounts paid in a corporate financing or restructuring, such as amounts paid by bondholders and shareholders to be used in a corporate reorganization, voluntary contributions by shareholders to a corporation, and amounts paid by a holding company to carry out a guaranty of dividends on the stock of a subsidiary corporation in certain circumstances (Reg. § 1.263(a)-1(d)).[6]

Taxpayers may elect to treat certain capital expenditures as deductible or deferred expenses, or treat certain deductible expenses as capital expenditures (Reg. § 1.263(a)-6).[7] These include: expenses related to newspaper or magazine circulation (¶ 971); research and experiments (¶ 979); soil and water conservation (¶ 982); Code Sec. 179 property (¶ 1208); energy efficient commercial buildings (¶ 1286); advanced mine safety equipment (¶ 989A); fertilizer (¶ 985); film, television production, and live theatrical production (¶ 1229); removal of barriers to the handicapped and elderly (¶ 1287); tertiary injectants (Code Sec. 193); reforestation (¶ 1287); business start-up (¶ 904); corporate organization (¶ 237); carrying charges (¶ 1614); mine development (¶ 988); and partnership organization and syndication (¶ 477).

Repair Regulations—Effective Date and Accounting Method Changes. Final "repair" regulations relating to amounts paid to acquire, produce, or improve tangible property apply to tax years beginning on or after January 1, 2014 (T.D. 9636). Effective for Form 3115 filed on or after April 19, 2017, for a tax year of change ending on or after August 31, 2016, a taxpayer changing to an accounting method described in the repair regulations uses the automatic change procedures described in Sec. 11.08 of Rev. Proc. 2017-30. For changes filed on or after May 5, 2016, and before April 19, 2017, Rev. Proc. 2016-29, as modified by Notice 2017-6, applied. Sec. 10.11 of Rev. Proc. 2015-14 contains the relevant automatic change procedures for complying with the repair regulations for changes filed on or after January 16, 2015, and before May 5, 2016. For earlier filed changes, see Appendix Sec. 10.11 of Rev. Proc. 2011-14, as modified by Rev. Proc. 2014-16 and Rev. Proc. 2012-19.[8]

A small business taxpayer does not have to file Form 3115 to comply with the final repair regulations for its first tax year beginning in 2014 (Rev. Proc. 2015-20). Therefore, no section 481(a) adjustment (¶ 1531) is permitted or required. A small business

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[5] ¶ 13,700, ¶ 13,701; BUSEXP: 9,000; § 10,201

[6] ¶ 13,701; BUSEXP: 9,000; § 10,201

[7] ¶ 13,704J; BUSEXP: 9,102; § 10,201

[8] ¶ 13,709.105; BUSEXP: 9,099; § 9,930.05, § 10,215.05

taxpayer is a taxpayer with one or more separate and distinct trades or businesses that has either: (1) total assets of less than $10 million as of the first day of the tax year for which the change in method of accounting is effective, or (2) average annual gross receipts of $10 million or less for the prior three tax years.

A qualifying taxpayer may choose this relief by not filing Form 3115 for its 2014 tax year. The relief applies to all accounting method changes required by Sec. 10.11 of Rev. Proc. 2015-14 to comply with the final repair regulations for the 2014 tax year. A taxpayer choosing this relief, however, could not file an accounting method change for the 2014 tax year to make the late partial disposition election to claim losses on previously retired structural components (¶ 1239). An electing taxpayer could also not file an accounting method change relating to permissible changes in identifying assets or portions of assets disposed of from multiple asset accounts and mass asset accounts. An electing taxpayer does not receive audit protection for expenditures paid or incurred prior to the first tax year beginning on or after January 1, 2014.

Acquired or Produced Tangible Property. Taxpayers are required to capitalize amounts paid or incurred to produce or acquire a unit of tangible real or personal property, including leasehold improvement property, land and land improvements, buildings, machinery, equipment, furniture, and fixtures unless a current deduction is allowed under the *de minimis* safe harbor (discussed below) or the rules that apply to materials and supplies (discussed below). Capitalized amounts include the invoice price, amounts that facilitate the acquisition of the property (i.e., transactions costs), and costs for work performed before the taxpayer places the property in service (e.g., repairs). Amounts paid to acquire real or personal property for resale are also capitalized (Reg. § 1.263(a)-2).[9]

An amount facilitates the acquisition of property if the amount is paid in the process of investigating or otherwise pursuing the acquisition or production of the property. Inherently facilitative costs of acquiring or producing property that must be capitalized are amounts paid for: (1) transporting the property (e.g., shipping fees and moving costs); (2) appraisals and valuations; (3) negotiating the terms or structure of the acquisition; (4) tax advice on the acquisition; (5) application fees, bidding costs, or similar expenses; (6) preparing and reviewing the documents that effectuate the acquisition of the property (e.g., preparing the bid, offer, sales contract, or purchase agreement); (7) title examination and evaluation; (8) obtaining regulatory approval of the acquisition; (9) securing permits related to the acquisition, including application fees; (10) conveying property between the parties, including sales and transfer taxes, and title registration costs; (11) finders' fees or brokers' commissions, including contingency fees; (12) architectural, geological, survey, engineering, environmental, or inspection services pertaining to particular properties; and (13) services provided by a qualified intermediary or other facilitator of a like-kind exchange (Reg. § 1.263(a)-2(f)).

Activities performed in the process of determining whether to acquire real property and which real property to acquire are currently deductible. Inherently facilitative amounts are capitalized even if paid or incurred during the "whether and which" process (Reg. § 1.263(a)-2(f)(2)(iii)).

Employee compensation and overhead do not facilitate the acquisition of real or personal property but may need to be capitalized under the uniform capitalization rules for property produced by the taxpayer or to property acquired for resale (¶ 990). A taxpayer may elect to capitalize employee compensation and overhead on a timely filed original federal tax return (including extensions) for the tax year during which the amounts are paid or incurred (Reg. § 1.263(a)-2(f)(2)(iv)).

De Minimis Expensing Safe Harbor. A taxpayer who meets certain requirements may make an annual *de minimis* safe harbor expensing election on a timely filed income tax return (including extensions) (Reg. § 1.263(a)-1(f)).[10] A taxpayer electing the safe

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[9] ¶ 13,703; BUSEXP: 9,080; § 10,215.05

[10] ¶ 13,701; BUSEXP: 9,080; § 10,215.15

harbor may not capitalize any amount paid in the tax year for the acquisition or production of a unit of tangible property. In addition, the taxpayer may not treat as a material or supply an amount paid for tangible property that costs no more than $5,000 if the taxpayer has an applicable financial statement (AFS), and $2,500 ($500 for tax years beginning before 2016) if the taxpayer does not have an AFS (Notice 2015-82). The uniform capitalization rules (¶ 990) may require a taxpayer to capitalize amounts that are deductible under the safe harbor as a direct and allocable indirect cost of property produced by the taxpayer or property acquired for resale.

A taxpayer with an AFS may elect the *de minimis* expensing safe harbor for a tax year if: (1) at the beginning of the tax year, the taxpayer has written accounting procedures that expense, for non-tax purposes, amounts paid for property that costs less than a specified dollar amount or that has an economic useful life of 12 months or less; and (2) it treats such amounts paid or incurred during the tax year as an expense on the AFS. A taxpayer without an AFS must have similar accounting procedures in effect at the beginning of the tax year. The procedures do not need to be written. A taxpayer without an AFS must expense the amount paid for the property on its books and records in accordance with its accounting procedures.

Repairs. Expenses that keep tangible property in an ordinarily efficient operating condition and do not add to its value or appreciably prolong its useful life are generally deductible as repair and maintenance costs (Reg. § 1.162-4).[11] Taxpayers may elect to capitalize certain repair expenses (discussed below).

Improvements. Expenses that improve a unit of property must be capitalized (Reg. § 1.263(a)-3).[12] A unit of property is improved if the amounts paid for activities performed after the property is placed in service by the taxpayer either result in a betterment to the unit of property, restore the unit of property, or adapt the unit of property to a new or different use. A taxpayer generally must capitalize all the direct costs of an improvement, as well as all the indirect costs, such as otherwise deductible repair costs, that directly benefit or are incurred by reason of an improvement. Indirect costs that do not directly benefit and are not incurred by reason of an improvement generally are not capital improvements, regardless of whether they are paid or incurred at the same time as a capital improvement.

A betterment is an expenditure that:

- ameliorates a material condition or defect that existed prior to the taxpayer's acquisition of the unit of property or arose during the production of the property, whether or not the taxpayer was aware of the condition or defect at the time of acquisition:
- is for a material addition to the unit of property, such as a physical enlargement, expansion, extension, or addition of a new major component;
- is for a material increase in the capacity of the unit of property, such as additional cubic or linear space; or
- is reasonably expected to materially increase the productivity, efficiency, strength, quality, or output of the unit of property (Reg. § 1.263(a)-3(j)(1)).

An amount is paid to restore a unit of property if:

- the taxpayer replaces a component of a unit of property and deducts a loss for that component, other than a casualty loss, for example, by making a partial disposition election under Reg. § 1.168(i)-8(d);
- the taxpayer replaces a component of a unit of property and realizes gain or loss by selling or exchanging the component;

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[11] ¶ 8620; BUSEXP: 9,150; § 9,930.05

[12] ¶ 13,704; BUSEXP: 9,090; § 10,215.12

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- the expenditure is for the restoration of damage to a unit of property caused by a casualty and the taxpayer is required to make a basis adjustment to the unit of property on account of a casualty loss or the receipt of insurance;
- the expenditures return a unit of property to its ordinary efficient operating condition after the property has deteriorated to a state of disrepair and is no longer functional for its intended use;
- the expenditures rebuild a unit of property to a like-new condition after the end of its class life (i.e., its MACRS alternative depreciation system recovery period); or
- the expenditures are for the replacement of a part or a combination of parts that comprise a major component or a substantial structural part of a unit of property (Reg. § 1.263(a)-3(k)(1)).

Repair expenditures paid in connection with a casualty are currently deductible if the capitalized restoration expenditures exceed the adjusted basis of the property prior to reduction by the casualty loss deduction or insurance reimbursement. If the capitalized restoration expenditures do not exceed the adjusted basis, but the sum of the capitalized restoration expenditures and repair expenditures exceed the adjusted basis, then the repair expenditures not used to offset the adjusted basis may be deducted (Reg. § 1.263(a)-3(k)(4)(i) and (k)(7), Example 5). Repair expenditures are not deductible if a basis adjustment is made to a property on account of a casualty loss or event, such as the receipt of insurance (Reg. § 1.263(a)-3(k)(1)(iii)).

An adaptation to a new or different use is a type of improvement that is capitalized. An amount is generally paid to adapt a unit of property to a new or different use if the adaptation is not consistent with the taxpayer's ordinary use of the unit of property at the time it was originally placed in service by the taxpayer (Reg. § 1.263(a)-3(l)).

Removal Costs. If a taxpayer disposes of a depreciable asset, including a partial disposition (¶ 1239), and has taken into account the adjusted basis of the asset or component of the asset in realizing gain or loss, then the costs of removing the asset or component are deductible. If a taxpayer disposes of a component of a unit of property, but the disposal is not a disposition, then the taxpayer must capitalize the removal cost if it directly benefits or is incurred by reason of an improvement to the unit of property (Reg. § 1.263(a)-3(g)(2)).[13] For example, the cost of removing shingles on a roof is deductible if the replacement costs are a deductible repair. However, if the entire roof is replaced and the replacement costs are capitalized, then the removal costs are capitalized provided the taxpayer does not make a partial disposition election and claim a loss deduction on the replaced roof. Special rules apply to demolitions (¶ 1105).

Remodel-Refresh Safe Harbor. A qualified taxpayer engaged in the trade or business of operating a retail establishment or a restaurant may adopt a safe harbor method of accounting under which 25 percent of qualified remodel/refresh costs are capital expenditures, and 75 percent of such costs are currently deductible (Rev. Proc. 2015-56; Sec. 11.10 of Rev. Proc. 2017-30).[14] A qualified taxpayer must have an AFS as defined in Reg.§ 1.263(a)-1(f). The building and improvements capitalized under the safe harbor must be placed in separate MACRS general asset accounts (GAAs). A late election to place the building in a GAA may be made in the tax year that the safe harbor is first used as part of the safe harbor accounting method change. Improvements that are depreciable under MACRS and made prior to the year that the safe harbor is first used generally must also be placed in a GAA by making a late election. A taxpayer may not make a partial disposition election (¶ 1239) to claim retirement losses on building components once this safe harbor is used.

The safe harbor accounting method change is applied on a cut-off basis unless the taxpayer revokes any prior year partial disposition elections on an amended return filed within the limitations period for the tax year for which the election was made or files an

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[13] ¶ 13,704; BUSEXP: 9,091; § 10,215.12

[14] ¶ 13,709.105; BUSEXP: 9,096.30; § 10,215.12

accounting method change to revoke any partial disposition elections that were made in prior tax years. The method change to revoke prior partial disposition elections is only allowed for a tax year beginning after December 31, 2013, and ending before December 31, 2016 (Sec. 6.18(3) of Rev. Proc. 2017-30).

Taxpayers who applied Temp. Reg.§ 1.168(i)-8T or the general asset account rules under Temp. Reg.§ 1.168(i)-1T in a tax year beginning before January 1, 2014, to claim losses on building components may not use the safe harbor until an accounting method change is filed to comply with the final regulations (Reg.§ 1.168(i)-8 or Reg.§ 1.168(i)-1) (¶ 1239). The positive section 481(a) adjustment related to the losses previously claimed under the temporary regulations or partial disposition losses under the final regulations is included in income in a single tax year (i.e., the year of change).[15]

Routine Maintenance Safe Harbor. Under a safe harbor, routine maintenance activities on a unit of property do not improve that unit (Reg. § 1.263(a)-3(i)).[16] The safe harbor is an accounting method and not an election. Routine maintenance activities are the recurring activities expected to be performed to keep a unit of property in ordinarily efficient operating order. The activities are routine only if at the time the unit of property is placed in service the taxpayer reasonably expects to perform the activities more than once during the class life (i.e., MACRS alternative depreciation system recovery period) of the unit of property or, in the case of a building, more than once during a ten-year period beginning on the date the taxpayer places the building in service.

Routine maintenance *does not* include amounts paid or incurred for a betterment or adaptation. The following types of restorations also do not qualify: (1) the cost of replacing a component if a retirement loss is claimed or gain or loss is realized upon a sale of the replaced component; (2) amounts paid for the restoration of damage to a unit of property for which a basis adjustment as a result of a casualty loss or casualty event is required; and (3) the cost of restoring deteriorated and nonfunctional property to its ordinarily efficient operating condition. In addition, routine maintenance does not include amounts paid for repairs, maintenance, or improvement of rotable and temporary spare parts if the taxpayer applies the optional method of accounting for such spare parts. Routine maintenance may include the replacement of a major component or substantial structural part of a unit of property.

Routine maintenance performed on a building structure or any of its building systems qualifies for the routine maintenance safe harbor. However, repairs, maintenance, or improvement of network assets (e.g., railroad track, oil and gas pipelines, water and sewage pipelines, power transmission and distribution lines, and telephone and cable lines) does not qualify for the safe harbor.

Building Improvements Safe Harbor for Small Taxpayers. A taxpayer with $10 million or less of average annual gross receipts in the three preceding tax years may elect not to capitalize improvements on a building, condominium, or cooperative that has an unadjusted basis of $1 million or less if the total amount paid or incurred for repairs, maintenance, and improvements for the tax year of the election does not exceed the lesser of $10,000 or two percent of the unadjusted basis of the building. Amounts deducted under the *de minimis* safe harbor or the safe harbor for routine maintenance are counted toward the $10,000 limit. This election must be made by the due date of the return (including extensions) for the year of the election. The safe harbor is applied separately to each eligible building owned or leased by the taxpayer. A lessee's unadjusted basis of a leased building or leased building space is equal to the total amount of undiscounted rent paid or expected to be paid over the entire lease term, including expected renewal periods (Reg. § 1.263(a)-3(h)).[17]

Election to Capitalize Repair and Maintenance Costs. A taxpayer may elect on a timely filed original return (including extensions) to capitalize as improvements all amounts paid during the tax year for repair and maintenance of tangible property, if the

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[15] ¶ 11,275B, ¶ 11,276Q; BUSEXP: 9,096.30; § 10,215.12

[16] ¶ 13,704; BUSEXP: 9,096.10; § 10,215.40

[17] ¶ 13,704; BUSEXP: 9,096.20; § 10,215.12b

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taxpayer incurs these amounts in carrying on its trade or business and treats them as capital expenditures on its books and records for the tax year covered by the election (Reg. § 1.263(a)-3(n)).[18] An electing taxpayer cannot currently deduct the repair and maintenance amounts affected by the election. The election does not apply to amounts paid for repairs or maintenance of rotable or temporary spare parts to which the optional method of accounting is applied.

Unit of Property. All components that are functionally interdependent comprise a single unit of property. Components are functionally interdependent if the placing in service of one component is dependent on the placing in service of the other components (Reg. § 1.263(a)-3(e)).[19] Although a building, including its structural components, is a unit of property, the improvement rules are applied separately to each building system and the building structure. A building structure consists of a building and its structural components, *other than* those designated as building systems. Designated building systems, including their components, that are separate from the building structure are:

- heating, ventilation, and air conditioning (HVAC) systems, including motors, compressors, boilers, furnace, chillers, pipes, ducts, and radiators;
- plumbing systems, including pipes, drains, valves, sinks, bathtubs, toilets, water and sanitary sewer collection equipment, and site utility equipment;
- electrical systems, including wiring, outlets, junction boxes, lighting fixtures and associated connectors, and site utility equipment;
- all escalators;
- all elevators;
- fire-protection and alarm systems, including sensing devices, computer controls, sprinkler heads, sprinkler mains, associated pipes or plumbing, pumps, visual and audible alarms, alarms control panels, heat and smoke detection devices, fire escapes, fire doors, emergency exit lighting and signage, and fire fighting equipment;
- security systems for the protection of the building and its occupants, including windows and door locks, security cameras, recorders, monitors, motion detectors, security lighting, alarm systems, entry and access systems, and related junction boxes, wiring and conduits;
- gas distribution systems, including associated pipes and equipment used to distribute gas to and from the property line and between buildings; and
- any other structural components designated as a building system by the IRS in published guidance.

Example: A taxpayer replaces the steps on the sole escalator in a building. The improvement rules are applied separately to the escalator because it is a building system. Since the steps are a major component of the escalator, the cost of replacing the steps is for a restoration and must be capitalized. If the improvement rules applied to the entire building, including its building systems, then the steps might not be considered a major component of the building and a repair deduction could be claimed. Generally, the larger the unit of property the more likely an expenditure is for a repair.

Materials and Supplies. The cost of nonincidental materials and supplies are deducted in the tax year they are first used or consumed, while the cost of incidental materials and supplies for which no inventories or records of consumption are kept is deductible in the tax year when paid or incurred if taxable income is clearly reflected (Reg. § 1.162-3(a)).[20] However, materials and supplies that improve tangible property are capitalized (Reg. § 1.263(a)-3(c)). In addition, the uniform capitalization rules (¶ 990) require taxpayers to capitalize the direct and allocable indirect costs, including the cost

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[18] ¶ 13,704; BUSEXP: 9,096.25; § 9,930.05.
[19] ¶ 13,704; BUSEXP: 9,094; § 10,215.12.
[20] ¶ 8600; BUSEXP: 18,558; § 9,935.05

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of materials and supplies, of property produced by the taxpayer and property acquired for resale. Taxpayers may also be required to include in inventory certain materials and supplies (¶ 1553) (Reg. § 1.162-3(b)). Finally, the cost of materials and supplies that meet the requirements of the *de minimis* safe harbor are deductible in the year paid or incurred if a taxpayer makes the *de minimis* safe harbor election.

Material and supplies include tangible property that is used or consumed in the taxpayer's business operations, is not inventory, and is:

- a component that is acquired to maintain, repair, or improve a unit of tangible property owned, leased, or serviced by the taxpayer, but is not acquired as part of any single unit of tangible property;
- fuel, lubricants, water, and similar items that are reasonably expected to be consumed in 12 months or less, beginning when used in a taxpayer's operations;
- a unit of property that has an economic useful life of 12 months or less, beginning when the property is used or consumed in the taxpayer's operations;
- a unit of property with an acquisition or production cost of $200 or less; or
- identified as a material or supply by the IRS in published guidance (Reg. § 1.162-3(c)(1)).

Rotable, Temporary, and Standby Emergency Parts. Rotable and temporary spare parts are materials and supplies. Their cost is deducted in the year used or consumed unless the taxpayer uses the optional method of accounting to deduct their cost in the year of installation (Reg. § 1.162-3(c)(2)).[21] If the election is not made, rotable and temporary spare parts are treated as used or consumed in the year they are discarded (Reg. § 1.162-3(a)(3)).

Rotable spare parts are parts that are acquired for installation on a unit of property, removable from that unit of property, generally repaired or improved, and either reinstalled on the same or other property or stored for later installation. Temporary spare parts are parts that are used temporarily until a new or repaired part can be installed and then are removed and stored for later installation (Reg. § 1.162-3(c)(2)).

A taxpayer may elect to capitalize and depreciate the cost of rotable, temporary, and standby emergency spare parts. The election does not apply to rotable and temporary spare parts for which the optional method of accounting is used (Reg. § 1.162-3(d)). The *de minimis* safe harbor election does not apply to rotable, temporary, or standby emergency spare parts that a taxpayer elects to capitalize and depreciate, or to rotable and temporary spare parts that are accounted for under the optional method (Reg. § 1.162-3(f)).

Intangible Property. Amounts must be capitalized if they are paid or incurred for: (1) specific categories of expenditures that are incurred in acquiring, creating, or enhancing, or that facilitate the acquisition or creation of an intangible that is acquired from another person in a purchase or similar transaction; (2) certain rights, privileges, or benefits that are created or originated by the taxpayer; (3) a separate and distinct intangible asset; or (4) a future benefit that the IRS identifies in published guidance (Reg. § 1.263(a)-4).[22]

904. Business Start-Up Costs. A taxpayer who enters into a trade or business can elect to expense up to $5,000 of its start-up costs. The maximum $5,000 deduction is reduced dollar for dollar when the start-up expenses exceed $50,000. The balance of start-up expenses, if any, are amortized over the 180-month period starting with the month in which the business begins (Code Sec. 195).[23] The taxpayer must make the election no later than the date for filing the return (including extensions) for the tax year in which the business begins or is acquired. The election is made by completing Part VI of Form 4562. A taxpayer who does not make the election must capitalize the expenses.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[21] ¶ 8600; BUSEXP: 18,558; § 9,935.05
[22] ¶ 13,704C; BUSEXP: 9,104.20; § 10,210.05
[23] ¶ 12,370; DEPR: 21,400; § 9,201

A taxpayer is deemed to elect to deduct and amortize start-up expenses for the tax year in which the active trade or business begins. A taxpayer may forego the deemed election by affirmatively electing to capitalize its start-up costs on a timely filed federal income tax return (including extensions) for the tax year in which the active trade or business begins. The election either to deduct and amortize start-up costs, or capitalize them, applies to all start-up expenses that are related to the active trade or business (Reg. § 1.195-1).[24]

Start-up expenses are those paid or incurred in connection with:

- investigating the creation or acquisition of an active trade or business;
- creating an active trade or business; or
- any activity engaged in for profit or for the production of income before the day the active trade or business begins, in anticipation of that activity becoming an active trade or business.

The start-up expense must also be a cost that would be allowable as a deduction if it were paid or incurred in connection with an existing active business in the same field (Code Sec. 195(c)).[25]

Start-up costs do not include any amount with respect to which a deduction is allowed for interest on debt (¶ 1043), taxes (¶ 1021), or research and experimental expenses (¶ 979). If the trade or business is disposed of completely by the taxpayer before the end of the 180-month period, any remaining deferred expenses may be deductible as a loss (¶ 1101) (Code Sec. 195(b)(2)).[26]

The organizational costs of business entities are a separate class of expense from start-up expenses, though subject to similar rules. Corporate organization fees are discussed at ¶ 237. Costs of organizing a partnership are discussed at ¶ 477 and ¶ 481.

905. Business Expenses, Interest Deductions, and Losses for Related Taxpayers. No deduction is allowed for any trade or business expense or interest payable to the payee until the payee includes the payment in income if the payor and payee are related taxpayers (¶ 1717), and the payor is on the accrual method of accounting and the payee is on the cash method, (Code Sec. 267(a)(2)).[27] A similar rule denies a deduction for a loss (except for a loss from a distribution in corporate liquidation) for property sold or exchanged between related taxpayers. However, the transferee's gain on a later sale or exchange of the property is recognized only to the extent that it exceeds the previously disallowed loss.

Compensation Paid

906. Compensation for Personal Services. A taxpayer carrying on a trade or business is entitled to deduct reasonable salaries or other compensation for personal services. The deduction is allowable for the year in which the salary is paid or incurred (Code Sec. 162(a)(1); Reg. § 1.162-7).[28]

Publicly held corporations generally cannot deduct compensation paid to certain covered employees that exceeds $1 million per tax year (Code Sec. 162(m); Reg. § 1.162-27).[29] A covered employee is any employee of the taxpayer who, as of the close of the tax year, is:

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[24] ¶ 12,370F; BUSEXP: 12,252; § 9,215
[25] ¶ 12,370; DEPR: 21,400; § 9,205.10
[26] ¶ 12,370; DEPR: 21,450; § 9,205.05
[27] ¶ 14,150; ACCTNG: 12,150; § 17,601
[28] ¶ 8500, ¶ 8635; COMPEN: 9,050; § 9,305.05
[29] ¶ 8500, ¶ 9051B; COMPEN: 12,350; § 9,310

- the principal executive officer of the taxpayer, including an individual acting in that capacity; or
- one of the three highest compensated officers for the tax year and, therefore, must have his or her compensation reported to shareholders (Notice 2007-49).[30]

The $1 million limit does not apply to certain performance-based compensation payable solely on account of attaining one or more performance goals (Code Sec. 162(m)(4)(C); Reg. § 1.162-27(e)).[31] Performance-based compensation can include compensation issued in the form of stock rights and options exercised when the plan specifies the maximum number of shares that may be granted to all employees in the aggregate. Performance-based compensation attributable to stock rights or stock options must include a specific per-employee limitation on the amount granted.

Awards paid under a corporate bonus plan are not qualified performance-based compensation if the plan allows payments to be made, even if the specified performance goals have not been met, upon the employee's retirement, termination without cause, or voluntary termination of employment for good reason (Rev. Rul. 2008-13).[32] If the bonus was paid solely for attaining a performance goal, the goal must be determined by a compensation committee consisting solely of two or more outside directors. An outside director cannot be a current employee, a former employee who receives compensation during the year, or a current or former officer (Rev. Rul. 2008-32).[33]

Reasonable compensation is the amount that would ordinarily be paid for like services by like enterprises in like circumstances (Reg. § 1.162-7(b)(3)).[34] Thus, whether compensation is reasonable in a given situation depends on the relevant facts and circumstances, including personal ability, responsibility of the position, and local economic conditions. The U.S. Court of Appeals for the Seventh Circuit has used an independent-investor test that presumes that compensation is reasonable if the company's investors earn their expected rate of return (*Exacto Spring Corporation*, CA-7, 99-2 USTC ¶ 50,964).[35] A bonus is deductible if it is paid for services performed, and, when added to other salaries, it does not exceed reasonable compensation (Reg. § 1.162-9).[36] Compensation paid to a relative is deductible if the relative performs needed services that would otherwise be performed by an unrelated party. The deduction is limited to the amount that would have been paid to a third party (*Transport Mfg. & Equip. Co.*, CA-8, 70-2 USTC ¶ 9627).[37] The IRS does not rule in advance on whether compensation is reasonable in amount (Rev. Proc. 2017-3).[38]

Officer-Stockholders of Closely Held Corporations. An officer-shareholder of a closely-held corporation may deduct repayments of salary to the corporation that are made under an agreement requiring such repayments if the IRS determines the salaries are excessive (Rev. Rul. 69-115).[39] The agreement must be legally enforceable and in existence *before* the excess salary is paid.

Deferred Compensation Plans. For unfunded deferred compensation plans, the employer deducts compensation when the compensation, or amount attributable to it, is included in the gross income of the recipient (¶ 723) (Code Sec. 404(a)(5) and (b)(1)).[40] Other benefits that are excluded from the recipient's gross income are deductible when they otherwise would have been includible but for the exclusion (Code Sec. 404(b)(2)).[41] This rule also applies to compensation paid to independent contractors (Code Sec. 404(d)).[42]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[30] ¶ 8636.2763; COMPEN: 12,354
[31] ¶ 8500, ¶ 9051B; COMPEN: 12,356; § 9,310
[32] ¶ 8636.2768; COMPEN: 12,356.10
[33] ¶ 8636.2764; COMPEN: 12,356.10; § 9,310.15
[34] ¶ 8635; COMPEN: 9,100; § 9,305.10
[35] ¶ 8637.227, ¶ 8637.57; COMPEN: 9,114; § 9,305.10
[36] ¶ 8641; COMPEN: 9,054; § 9,335
[37] ¶ 8637.752; COMPEN: 9,202; § 9,305.20
[38] ¶ 8637.692; COMPEN: 9,054
[39] ¶ 8640.165; COMPEN: 9,456; § 7,101
[40] ¶ 18,330; COMPEN: 15,250; § 25,605
[41] ¶ 18,330; COMPEN: 12,108.10; § 25,605
[42] ¶ 18,330; COMPEN: 15,252; § 25,605

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A plan is unfunded if it consists of an unsecured promise to pay compensation at some time in the future. If the employer sets aside a reserve for the future obligation, the plan is unfunded if the employee has no rights in the reserve or its earnings, and if the reserve remains solely the property of the employer or other payor, subject to the claims of creditors (Rev. Rul. 55-525).[43]

A plan is presumed to defer compensation if the compensation is received after the 15th day of the third calendar month after the end of the employer's tax year in which the related services are rendered. This presumption may be overcome if the employer establishes that it was administratively or economically impractical to avoid the deferral of compensation beyond the 2½-month period. Payments within the 2½-month period are not deferred compensation and may be accrued by an accrual-method employer in the year earned by the employee (Temp. Reg. § 1.404(b)-1T, Q&A-2).[44]

For a discussion of rules governing the employer's deduction for compensation for deferred compensation plans, see ¶ 2117 and ¶ 2199.

Health Insurance Providers. The deduction for compensation or remuneration paid to officers, directors, and employees of covered health insurance providers, including those that provide services for or on behalf of covered health insurance providers, is limited to $500,000 for disqualified tax years (Code Sec. 162(m)(6); Reg. § 1.162-31).[45] A disqualified tax year is any tax year in which the employer is a covered health insurance provider. A covered health insurance provider is a health insurance issuer for any tax year during which at least 25 percent of the gross premiums it receives from providing health insurance coverage is from providing minimum essential coverage (¶ 131). A *de minimis* exception applies if health insurance premiums are less than two percent of gross revenues.

Deduction Limit for TARP Recipients. Under the Troubled Asset Relief Program (TARP) established by the Emergency Economic Stabilization Act of 2008 (P.L. 110-343), the federal government may purchase troubled assets from financial institutions. A TARP participant's deduction for compensation paid to a covered executive is limited to $500,000 in each year that TARP financial assistance remains outstanding (Code Sec. 162(m)(5)).[46]

907. Golden Parachute Payments. A corporation that enters into a contract agreeing to pay an employee additional compensation if control or ownership of the corporation changes cannot take a deduction for an "excess parachute payment" made to a disqualified individual (Code Sec. 280G).[47] A disqualified individual is an officer, shareholder, or highly compensated person who performs personal services for the corporation as an employee or independent contractor. A personal service corporation is treated as an individual. The disqualified individual is subject to an excise tax of 20 percent of the excess parachute payment in addition to the income tax due (Code Sec. 4999(a)).[48]

Parachute Payment Defined. A parachute payment is any payment in the nature of compensation to a disqualified individual if:

- the payment is contingent on a change in the ownership or effective control of the corporation or a substantial portion of the assets of the corporation; and
- the aggregate present value of the contingent payments equals or exceeds three times the individual's base amount.

A payment in the nature of compensation to a disqualified individual made under an agreement that violates any securities law or regulations is also a parachute payment. Parachute payments do not include reasonable compensation for personal services to be rendered on or after the date of change or for personal services actually rendered before the date of change, or payments to or from certain qualified plans (Code Sec. 280G(b)).[49]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[43] ¶ 18,352.48; COMPEN: 15,050; § 25,610.15
[44] ¶ 18,354; COMPEN: 15,254; § 24,005
[45] ¶ 8500, ¶ 9051I; COMPEN: 12,360; § 9,310.05
[46] ¶ 8500; COMPEN: 12,358; § 9,310.05
[47] ¶ 15,150; COMPEN: 30,050; § 21,805.15
[48] ¶ 34,940; COMPEN: 30,250; § 21,820
[49] ¶ 15,150; COMPEN: 30,100; § 21,815.05

Base Amount. The base amount is the individual's annualized includible compensation for the base period. This is the most recent five tax years ending before the date on which the ownership or control changed, or the portion of that period during which the disqualified individual performed personal services for the corporations (Code Sec. 280G(b)(3)(A) and (d)(2)).[50]

Exceptions. A parachute payment generally does not include any payment made to a disqualified individual by a small business corporation. It also does not include a payment from a corporation if, immediately before the change in ownership or control, none of the corporation's stock was readily tradable on an established securities market and the payment met shareholder approval requirements (Code Sec. 280G(b)(5)).[51]

Excess Parachute Payment. An excess parachute payment is the portion of any parachute payment that exceeds the base amount, reduced, in the case of a change-in-control parachute payment, by the excess of the amount of the payment determined to be reasonable compensation for services performed before the date of the change, over average compensation (Code Sec. 280G(b)).[52]

908. Contributions for Employee Benefits and Health Insurance. An employer's deduction for contributions to a funded welfare benefit plan for sickness, accident, hospitalization, or medical benefits is governed by Code Sec. 419 (¶ 2011) (Temp. Reg. § 1.162-10T).[53] Although amounts that are added to a self-insurance reserve account are not currently deductible, actual claims charged to the account are deductible (*General Dynamics Corp.*, SCt, 87-1 USTC ¶ 9280).[54] Group health plans that fail to provide COBRA continuing coverage to qualified beneficiaries may subject employers to an excise tax (Code Sec. 4980B).[55]

Self-Employed Persons. A self-employed individual may deduct 100 percent of amounts paid during the year for health insurance for himself or herself, as well as his or her spouse and dependents (Code Sec. 162(l)).[56] The deduction cannot exceed the taxpayer's net earned income derived from the trade or business for which the insurance plan was established, minus the deduction for 50 percent of the self-employment tax and/or the deduction for contributions to qualified retirement plans, self-employed pensions (SEPs), or SIMPLE plans. The deduction is not available for amounts paid during any month, or part of a month, that the self-employed individual was able to participate in a subsidized health plan maintained by his or her employer or spouses' employer. The IRS has issued guidance providing optional calculation methods to claim the health insurance premium assistance credit (¶ 1331) and the self-employed health insurance deduction (Rev. Proc. 2014-41).[57]

Children Under the Age of 27. Children under the age of 27 are considered dependents of a taxpayer for purposes of the deduction for the health insurance costs of a self-employed person, spouse, and dependents. See ¶ 137A for a discussion of a child for dependency exemption purposes.

Excise Tax on High-Cost Employer-Provided Insurance. A 40-percent excise tax will be imposed on health coverage providers starting in 2020 to the extent that the aggregate value of employer-sponsored health coverage for an employee exceeds a threshold amount (Code Sec. 4980I).[58]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[50] ¶ 15,150; COMPEN: 30,150; § 21,805.25
[51] ¶ 15,150; COMPEN: 30,110; § 21,815.15
[52] ¶ 15,150; COMPEN: 30,150; § 21,805.25
[53] ¶ 8751; COMPEN: 42,100; § 9,345
[54] ¶ 8522.3947; BUSEXP: 18,210; § 9405.30, § 9,345
[55] ¶ 34,600; HEALTH: 24,100; § 42,850.05
[56] ¶ 8500; HEALTH: 15,100; § 5,401
[57] ¶ 8522.405; HEALTH: 3,322; § 42,015.20
[58] ¶ 34,619ZE; HEALTH: 9,302

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908A. Business Deduction for Overhead Disability Insurance. A taxpayer may deduct as a trade or business expense premiums paid on a disability insurance policy that pays overhead expenses should the taxpayer become disabled. The portion of the premiums attributable to overhead expenses that are actually incurred in the operation of the business are deductible (i.e., rent, utilities, depreciation, and employee's salaries), but the portion of the premiums paid to provide the taxpayer's salary, fees, or drawing account are not (Rev. Rul. 55-264).[59] The proceeds of the policy are includible in gross income. If an insurance premium is paid in advance for more than one year, only a pro rata portion of the premium is deductible for each year, regardless of the taxpayer's method of accounting (Reg. § 1.461-1; Rev. Rul. 70-413).[60]

908B. Employer-Provided Day Care. An employer's payments to a day care center are a deductible business expense where the purpose of providing the day care is:

- to provide employees with a place to send their children while at work, so that the employees can be reassured that the children are receiving proper care;
- to reduce absenteeism, increase productivity, and reduce company training costs; and
- to reduce employee turnover (Rev. Rul. 73-348).[61]

An S corporation, however, could not deduct amounts it paid for day care for its sole shareholder's preschool children where there was no direct relationship to the corporation's business, and it did not pay day care expenses for any of its other employees (*F.M. Settimo*, Dec. 56,694(M), 92 TCM 473 (2006)).[62]

Up to $5,000 of employer-provided child or dependent care assistance services is excludable from the employee's gross income (¶ 2065).

909. Business Deduction for Life Insurance Premiums. Premiums paid by an employer for insurance on the life of an employee or officer are deductible only if it can be shown that: (1) the premium payments are in the nature of additional compensation; (2) total compensation, including premiums, is not unreasonable; and (3) the employer is not directly or indirectly a beneficiary under the policy (*L. Hyman & Co.*, Dec. 6447, 21 BTA 159; *Brown Agency, Inc.*, Dec. 6615, 21 BTA 1111).[63] However, an employer cannot deduct premiums paid under a split dollar arrangement (¶ 2057).

An employer can deduct premiums on group-term life insurance covering the lives of employees only if the employer is not a direct or indirect beneficiary (Code Sec. 264(a)(1); Reg. § 1.264-1).[64] The premiums generally represent income to the employee to the extent that the coverage exceeds $50,000 (¶ 2055).

Generally, no deduction is allowed for interest paid or accrued on a debt incurred or continued to purchase or carry any single premium life insurance, endowment or annuity contract. If substantially all the premiums on a life insurance or endowment contract are paid within four years from the date of purchase, or if an amount is deposited with the insurer for payment of a substantial number of future premiums, it is regarded as a single premium contract (Code Sec. 264(a)(2) and (c)).[65]

Interest on a debt incurred to purchase or continue a life insurance, endowment, or annuity contract under a purchase plan that contemplates the systematic borrowing of part or all of the increases in cash value is not deductible (Code Sec. 264(a)(3)).[66] However, an interest deduction is allowed in limited situations (Code Sec. 264(d)). Special rules may permit the deduction of interest incurred for key person policies owned by corporations (Code Sec. 264(e)).[67]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[59] ¶ 8522.385; BUSEXP: 18,220; § 9,415.05
[60] ¶ 21,805, ¶ 21,817.21; BUSEXP: 18,216; § 9,420.05
[61] ¶ 8752.21; BUSEXP: 3,104; § 9,010.15
[62] ¶ 8520.517; BUSEXP: 3,104; § 9,010.15
[63] ¶ 8522.386, ¶ 8636.27; BUSEXP: 18,154.05; § 9405.05
[64] ¶ 14,002, ¶ 14,003; COMPEN: 48,100; § 21,005.05
[65] ¶ 14,002; INDIV: 48,556; § 9405.05
[66] ¶ 14,002; INDIV: 48,556; § 9,405.15
[67] ¶ 14,002; COMPEN: 48,062; § 9,405.15

Entertainment, Meal, and Gift Expenses

910. Entertainment Expenses. Special limits are imposed on the deduction of business-related entertainment, meals, and gift expenses in addition to those imposed by other Code sections. Entertainment, amusement, or recreation costs are not deductible as trade or business expenses unless they are (1) *directly related* to the active conduct of the trade or business (¶ 911), or (2) for entertainment directly before or after a substantial and bona fide business discussion *associated with* the conduct of the trade or business (¶ 912) (Code Sec. 274(a)(1); Reg. § 1.274-2).[68] Certain entertainment expenses are not subject to these rules (¶ 915).

Entertainment generally includes entertaining guests at nightclubs, sporting events, theaters, etc. A taxpayer's trade or business is considered in applying an objective test as to what constitutes entertainment. For example, a ticket to a play is generally an entertainment expense, but it might be a business expense if the taxpayer is a professional theater critic. Only 50 percent of meal and entertainment expenses is deductible (¶ 916), but there are numerous exceptions to this limit (¶ 917).

911. Directly-Related to Business Test for Entertainment Expenses. For an entertainment expense to meet the directly related test for a deductible business expense (¶ 910), the taxpayer must have had more than a general expectation of deriving income, or some other specific business benefit, from the entertainment at some indefinite future time. The taxpayer must engage in the active conduct of business with the person being entertained, and the active conduct of business must be the principal aspect of the combined business and entertainment (Reg. § 1.274-2(c)).[69]

912. Entertainment Associated with Trade or Business. Entertainment expenses associated with the active conduct of the taxpayer's business are deductible if they directly precede or follow a bona fide and substantial business discussion (¶ 910). This includes goodwill expenditures to obtain new business or encourage continuation of existing business relationships. The business discussion must be the principal aspect of the combined entertainment and business discussion and must represent an active effort by the taxpayer to obtain income or other specific business benefit (Reg. § 1.274-2(d)).[70]

913. Business-Related Entertainment Facility. No business deduction is allowed for any expense for entertainment facilities, such as yachts, hunting lodges, swimming pools, tennis courts, or bowling alleys (¶ 910) (Code Sec. 274(a)(1)(B)).[71] However, expenses for recreational facilities primarily for the benefit of employees generally are deductible (Reg. § 1.274-2(f)(2)(v)).[72]

913A. Business-Related Club Dues. Club dues generally are not a business expense deduction. This rule extends to business, social, athletic, luncheon, sporting, airline, and hotel clubs (Code Sec. 274(a)(3); Reg. § 1.274-2(a)(2)(iii)).[73] Dues paid to professional or public service organizations (e.g., accounting associations, or Kiwanis and Rotary clubs) are deductible if they are paid for business reasons and the organization's principal purpose is *not* to conduct entertainment activities for members or their guests or to provide those parties with access to entertainment facilities.

914. Business-Related Entertainment and Meals. An entertainment-related meal expense is generally not deductible unless the taxpayer establishes that the expense is directly related to the active conduct of a trade or business. If a meal expense directly precedes or follows a substantial and bona fide business discussion, including a business meeting at a convention, then it is deductible if it is established that the expense was

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[68] ¶ 14,402, ¶ 14,405; BUSEXP: 24,550; § 9,610.05, § 9,635.05
[69] ¶ 14,405; BUSEXP: 24,558; § 9,615
[70] ¶ 14,405; BUSEXP: 24,560; § 9,615
[71] ¶ 14,402; BUSEXP: 24,650; § 9,625.10
[72] ¶ 14,405; BUSEXP: 24,562.20; § 9,630.25
[73] ¶ 14,402, ¶ 14,405; BUSEXP: 24,658; § 9,625.15

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associated with the active conduct of a trade or business. The taxpayer must be able to substantiate the expense (¶ 953) (Code Sec. 274(d); Temp. Reg. § 1.274-5T(c) and (f)).[74]

There are two additional restrictions placed on the deduction of meal expenses: (1) meal expenses generally are not deductible if neither the taxpayer nor the taxpayer's employee is present at the meal, and (2) a deduction will not be allowed for food and beverages to the extent that such expense is lavish or extravagant under the circumstances. These restrictions do not apply to the expenses described in exceptions (2), (3), (4), (7), (8), and (9) at ¶ 915 (Code Sec. 274(k)).[75]

915. Exceptions to Entertainment Rules. The following entertainment expenses are not subject to the special rules for the deduction of entertainment expenses (¶ 912, ¶ 913, and ¶ 914). They are deductible as long as they meet the ordinary and necessary requirements and are properly substantiated (Code Sec. 274(e); Reg. § 1.274-2(f)(2)).[76] However, they may be subject to the 50-percent limit on meals and entertainment expenses (¶ 916 and ¶ 917). The exceptions are:

(1) food and beverages for employees furnished on the business premises;

(2) expenses for services, goods, and facilities that are treated as compensation and as wages for withholding tax purposes, but if the recipient is a specified individual such as an officer, director, or 10-percent shareholder or related person, the employer's deduction is limited to the compensation reported;

(3) reimbursed expenses, but only:

(a) if the services relating to the expenses are performed for an employer that has not treated the expenses as wages subject to withholding; or

(b) if the services are performed for a person other than an employer and the taxpayer incurring the reimbursed expenses accounts to that person;

(4) recreational expenses primarily for employees who are not highly compensated (¶ 2114) (e.g., a company picnic);

(5) expenses of employees', stockholders', agents', or directors' business meetings;

(6) expenses directly related and necessary to attendance at a business meeting of a tax-exempt business league, including a real estate board, chamber of commerce or board of trade;

(7) expenses for goods, services, and facilities made available to the public;

(8) expenses for entertainment sold to customers in a bona fide transaction for adequate consideration; and

(9) expenses for goods, services, and facilities that are furnished to a nonemployee as entertainment, amusement or recreation and are includible in the recipient's income as compensation for services (¶ 713) or as a taxable prize or award (¶ 785).

916. 50-Percent Limit for Meal and Entertainment Expenses. The business deduction for meal and entertainment expenses is generally limited to 50 percent of such expenses (Code Sec. 274(n)).[77] Food and beverage costs incurred in the course of travel away from home fall within the scope of this rule. The 50-percent limit applies to all meal and entertainment expenses unless an exception applies (¶ 917). The limit is applied only after determining the amount of the otherwise allowable deductions. For instance, the portion of a travel meal that is lavish and extravagant must first be subtracted from the meal cost before the 50-percent limit is applied. Related expenses, such as taxes, tips, room rental and parking fees, must be included in the total expense before applying the 50-percent limit. Allowable deductions for transportation costs to and from a business meal are not reduced.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[74] ¶ 14,402, ¶ 14,410; BUSEXP: 24,810; § 10,105

[75] ¶ 14,402; BUSEXP: 24,562; § 9,601

[76] ¶ 14,402, ¶ 14,405; BUSEXP: 24,562; § 9,630.10

[77] ¶ 14,402; BUSEXP: 24,600; § 9,635

Transportation Workers. The deductible percentage of the cost of meals consumed while away from home by individuals subject to Department of Transportation hours of service rules (e.g., interstate truck and bus drivers and certain railroad, airline, and merchant marine employees) is 80 percent (Code Sec. 274(n)(3)).[78]

Leased Employees. If an employee or independent contractor incurs unreimbursed meal and incidental expenses (M&IE) in connection with the performance of services for a third party, the 50-percent limit applies to any deduction claimed by the employee or independent contractor (Reg. § 1.274-2(f)(2)(iv)).[79] However, if an employee or independent contractor accounts for the expenses to a leasing company and is reimbursed under an allowance arrangement with a payment that is treated as compensation, the leasing company, rather than the employee or independent contractor, bears the expense and is subject to the 50-percent limit. Similarly, if the leased company accounts for the expenses to the third party and is reimbursed under an allowance arrangement, the third party bears the expenses and is subject to the 50-percent limit on its deduction.

917. Exceptions to 50-Percent Limit for Meal and Entertainment Expenses. The following expenses are *not* subject to the 50-percent limit on meal and entertainment expense deductions (80-percent limit for certain transportations workers) (¶ 916):

- expenses described in categories (2), (3), (4), (7), (8), and (9) at ¶ 915;
- food and beverage expenses associated with benefits that are excludable from the recipient's gross income as a *de minimis* fringe benefit (¶ 2089);
- the cost of a ticket package to a sporting event and related expenses if the event is organized to benefit a tax-exempt organization, all net proceeds are contributed to the organization, and volunteers perform substantially all of the work in carrying out the event (in other situations, a deduction for a ticket is limited to the ticket's face value);
- an employee's meal expenses incurred while moving that are reimbursed by the employer and includible in the employee's gross income (¶ 1073); and
- expenses for food and beverages provided to employees on certain vessels, and oil or gas platforms and drilling rigs and their support camps (Code Sec. 274(l)(1) and (n)).[80]

Skyboxes. When a skybox is rented for more than one event, the deduction may not exceed the price of non-luxury box seats (subject to the usual 50-percent limit) (Code Sec. 274(l)(2)).[81]

Tickets to College Sporting Events. For any payment to or for an institution of higher education that would be allowable as a charitable deduction but for the fact that the taxpayer receives (directly or indirectly) the right to purchase tickets for seating at an athletic event in an athletic stadium of the institution, 80 percent of that payment is treated as a charitable contribution (Code Sec. 170(l)).[82]

918. Business Gifts. Deductions for business gifts, whether made directly or indirectly, are limited to $25 per recipient per year (Code Sec. 274(b)(1); Reg. § 1.274-3).[83] Items clearly of an advertising nature that cost $4 or less and signs, display racks, or other promotional materials given for use on business premises are not gifts.

919. Business Deduction for Employee Achievement Awards. An employer may deduct up to $400 of the cost of an employee achievement award for all nonqualified plan

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[78] ¶ 14,402; BUSEXP: 24,606; § 9,640.60

[79] ¶ 49,544; BUSEXP: 24,604; § 9,635.05

[80] ¶ 14,402; BUSEXP: 24,604; § 9,640.05

[81] ¶ 14,402; BUSEXP: 24,662; § 9,650

[82] ¶ 11,600; INDIV: 51,052.40; § 7,510.75

[83] ¶ 14,402, ¶ 14,406; BUSEXP: 24,706; § 9,945.05

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awards to each employee (Code Sec. 274(j)).[84] The deduction for the cost of a qualified plan award made to a particular employee is limited to $1,600 per year, taking into account all other qualified and nonqualified awards made to that employee during the tax year.

An employee achievement award is an item of tangible personal property awarded to an employee as part of a meaningful presentation for length-of-service or safety achievements, and under circumstances that do not create a significant likelihood of disguised compensation (¶ 2069). Tangible personal property does not include cash, gift certificates, or other intangible property such as vacations, meals, lodging, tickets to events, stocks, bond, and other securities.

A qualified plan award is an employee achievement award provided under an established written plan or program that does not discriminate in favor of highly compensated employees (¶ 2114) as to eligibility or benefits. An employee achievement award is not a qualified plan award if the average cost of all employee achievement awards under the plan exceeds $400. This average cost calculation includes the entire cost of all qualified plan awards other than awards of nominal value.

A length of service award does not qualify if it is received during the employee's first five years of service or if the employee has received another length of service award (other than a *de minimis* fringe benefit (¶ 2089)) during the year or within the last four years. An award is not a safety achievement award if it is made to a manager, administrator, clerical employee, or other professional employee, or if, during the tax year, awards for safety achievement previously have been made to more than 10 percent of the employees, excluding managers, administrators, clerical employees, or other professional employees.

Taxes

920. Business Deduction for Taxes. All state, local, and foreign taxes (¶ 1020) directly attributable to a taxpayer's trade or business or activities for the production of income are generally deductible in the year in which the taxes are paid or accrued (Code Sec. 164(a)).[85] If taxes other than those specified as deductible are paid or accrued by the taxpayer in connection with the acquisition of property, then they are treated as part of the cost of the acquired property or, if in connection with the disposition of property, as a reduction in the amount realized. The uniform capitalization rules also require some taxpayers to capitalize certain taxes that would otherwise be deductible (¶ 990–¶ 999).

921. Business Deduction for FUTA Taxes. The Federal Unemployment Tax Act (FUTA) tax (¶ 2649) is an *excise* tax, so an employer may deduct it as a business expense if it represents an ordinary and necessary expense paid or incurred during the tax year in the conduct of a trade or business, or the production of income (Reg. § 1.164-2(f)).[86] The FUTA tax is deductible as a business expense after application of credits for the employer's contributions to the state unemployment fund (Code Sec. 3302(a)(1)). On the cash basis (¶ 1515), the tax is deductible when paid. On the accrual basis (¶ 1540), the deduction may be accrued for the calendar year in which the wages were paid even though the tax is not due until the following year.

922. Business Deduction for State Unemployment Insurance and Disability Fund Contributions. An employer's contributions to a state unemployment insurance fund are deductible as taxes only if they are classified as taxes under state law and are incurred in carrying on a trade or business or for the production of income.[87] If the state does not classify the contributions as taxes, the employer may be able to deduct them as a business expense. Similar treatment applies to employer contributions to state disabil-

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[84] ¶ 14,402; BUSEXP: 24,714, BUSEXP: 24,716; § 9,340.10
[85] ¶ 9500; BUSEXP: 21,350; § 9,940.10
[86] ¶ 9503; INDIV: 45,112.35; § 9,365
[87] ¶ 8752.692—¶ 8752.694, ¶ 9502.31; BUSEXP: 21,506.05; § 9,415.05

ity funds.[88] An employee who is required to contribute to a state unemployment compensation fund may claim an itemized deduction for the contribution as a state income tax (¶ 1023). Also, compulsory employee contributions to state disability funds are deductible as itemized deductions for state income taxes. However, employees cannot deduct their contributions to private disability benefit plans.

923. Business Deduction for FICA Taxes. An employer's share of the Federal Insurance Contributions Act (FICA) tax for Social Security and Medicare (¶ 2648) is an *excise* tax, so the employer may deduct it as a business expense if it represents an ordinary and necessary expense paid or incurred during the tax year in the conduct of a trade or business or for the production of income (Reg. § 1.164-2(f)).[89] The employer contribution on wages paid to a domestic worker is not deductible unless it qualifies as a business expense (*R.A. Biggs*, CA-6, 71-1 USTC ¶ 9306).[90]

An employee's portion of FICA taxes is not deductible (¶ 1025). However, if the employer pays the employee's portion of the tax without deduction from the employee's wages under an agreement with the employee, the amount is deductible by the employer as a business expense. It is also includes wage income to the employee (Rev. Rul. 86-14).[91]

A self-employed individual may deduct from gross income 50 percent of the self-employment tax imposed for the tax year, other than the additional 0.9-percent Medicare tax on incomes over a certain threshold (¶ 2664).

924. Deduction for Federal and State Income Tax. Federal income taxes are not deductible in determining taxable income of any taxpayer (Code Sec. 275).[92] However, they are deductible in determining the amount of a corporation's income subject to the accumulated earnings tax (¶ 251) and the personal holding company tax (¶ 275) (Reg. §§ 1.535-2 and 1.545-2).[93] A corporation or partnership may deduct its state income taxes as a business expense. State income taxes that are based on net business income may be deducted only by self-employed individuals as an itemized deduction on Schedule A of Form 1040. If the state income tax is based on gross business income, the tax may be deducted as a business expense (Temp. Reg. § 1.62-1T(d)).[94]

Charitable Contributions

927. Charitable Deduction Limits for Corporations. A corporation's deduction for charitable contributions is limited to 10 percent of its taxable income for the year, computed without regard to:

- the deduction for charitable contributions;
- the corporate deductions for dividends received and for dividends paid on certain preferred stock of public utilities;
- the limitation on the deduction for bond premium;
- any net operating loss or capital loss carryback to the tax year; and
- the deduction for domestic production activities (Code Sec. 170(b)(2); Reg. § 1.170A-11).[95]

Corporate donors that qualify as farmers or ranchers may deduct certain qualified conservation contributions of real property interests (¶ 1063), up to the excess of the donor's taxable income over all other allowable charitable contributions. Similar treatment applies to Native Corporation donors for qualified conservation contributions of land that was conveyed under the Alaska Native Claims Settlement Act.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[88] ¶ 8752.2959; BUSEXP: 21,506.05
[89] ¶ 9503; INDIV: 45,112.35; § 9,365
[90] ¶ 9502.30; INDIV: 45,152.10, PAYROLL: 9,050; § 22,210.60
[91] ¶ 8636.49; INDIV: 45,112.35; § 9,005.20, § 22,210.45
[92] ¶ 14,500; BUSEXP: 21,350; § 7,345
[93] ¶ 23,042, ¶ 23,252; CCORP: 18,252, CCORP: 36,254; § 26,905.05, § 27,001
[94] ¶ 6003; INDIV: 45,100; § 9,940.10
[95] ¶ 11,600, ¶ 11,672; CCORP: 9,350; § 7,575.05

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Chapter 20

HEALTH AND EMPLOYEE BENEFITS

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Employer Health Insurance Mandate

2001. Employer Health Insurance Mandate. For any month beginning on or after January 1, 2015 (for employers with 100 or more full-time employees), and January 1, 2016 (for employers with 50 or more full-time employees), an applicable large employer may be assessed a nondeductible penalty known as a shared responsibility payment if either:

- the employer fails to offer at least 95 percent of its full-time employees and their dependents the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan (¶ 2003); or
- the employer offers its full-time employees and their dependents the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan but the coverage is unaffordable to the employee or does not provide minimum value (¶ 2005) (Code Sec. 4980H; Notice 2013-45; T.D. 9655).[1]

An applicable large employer may be liable for either type of assessable payment in any calendar month, but not both. Minimum essential coverage for this purpose means coverage under an employer-sponsored plan offered in the small or large group market within a state and which meets the requirements for group health plans or group health insurance coverage under section 2791 of the Public Health Service Act (Code Sec. 5000A(f); Reg. § 54.4980H-1(a)(27)).[2]

Applicable Large Employer. An applicable large employer is any employer that employed on average at least 50 full-time employees, full-time equivalents (FTEs), or some combination on business days during the preceding calendar year (Code Sec. 4980H(c)(2); Reg. § § 54.4980H-1(a)(4) and 54.4980H-2).[3] An individual who has medical coverage under the TRICARE program or the Veterans' Administration is not considered an employee in determining whether an employer meets the 50-employee threshold.

FTEs are determined by adding all hours of service for the month for employees who were not full-time employees (but no more than 120 hours per employee), and dividing by 120. An employer not in existence during an entire preceding calendar year is an applicable large employer for the current year if it is reasonably expected to employ an average of 50 or more full-time employees (including FTEs) on business days during the current calendar year.

An exemption to the 50-employee threshold applies if the employer has more than 50 employees for 120 days or less during the preceding calendar year, but the employees in excess of 50 are seasonal workers. A seasonal worker is an employee who performs labor or services on a seasonal basis including, but not limited to, certain agricultural workers and retail workers employed during the holiday season.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[1] ¶ 34,619ZA, ¶ 34,619ZD.35; HEALTH: 6,050; § 42,101

[2] ¶ 34,619ZBF, ¶ 34,962; HEALTH: 6,050; § 42,101

[3] ¶ 34,619ZA, ¶ 34,619ZBF, ¶ 34,619ZBI; HEALTH: 6,052; § 42,105

In applying the 50-employee threshold, an employer means all common law employers, including for-profit businesses, tax-exempt organizations, and government entities (federal, state, local, and Indian tribes). Employers with common ownership such as controlled groups under Code Sec. 414(b) or (c), or related employers such as an affiliated service group under Code Sec. 414(m), are combined for the 50-employee threshold. Moreover, any references to an employer include references to the employer's predecessors and successors.

Full-Time Employee. A full-time employee for purposes of determining applicable large employer status is an employee who was employed on average at least 30 hours of service per week or 130 hours of service in a calendar month (Code Sec. 4980H(c)(4); Reg. § § 54.4980H-1(a)(21) and 54.4980H-3).[4] Employee is defined under the common law standard (i.e., right to control, direct, etc.). It does not include a leased employee, sole proprietor, partner in partnership, or two-percent or more S corporation shareholder, unless services are provided as both an employee and nonemployee.

An hour of service includes each hour for which the employee is paid or entitled to be paid for services performed in the United States for the employer, including periods of paid leave. For an hourly employee, the employer calculates hours of service using records of hours worked and for which payment is made or due. For a non-hourly employee, an employer can count actual hours worked and for which payment is due, or apply a days-worked equivalency (8 hours of service) or weeks-worked equivalency (40 hours of service). An employer may use different methods for different classifications of non-hourly employees as long as the categories are reasonable and consistently applied.

Safe harbors are provided allowing an employer the option of using either a look-back method or monthly measurement method to determine full-time employee status (Reg. § 54.4980H-3).[5] Look-back measurements are provided for ongoing employees, new employees, and employees with a change in employment status.

Offer of Coverage. An employer is treated as offering coverage for a calendar month if it offers the coverage for that month to at least 95 percent of its full-time employees and their dependents (Reg. § § 54.4980H-4(b) and 54.4980H-5(b)).[6] An offer occurs if the employee has the opportunity to elect to enroll in or decline coverage at least once during the plan year. Failure to offer coverage for any day of a calendar month is treated as failure to offer coverage for the entire month.

A full-time employee is treated as having been offered coverage only if the employer also offers coverage to the employee's dependents. A dependent is the employee's child who is under the age of 26. It does not include anyone other than children, such as the employee's spouse. If an employee or dependent enrolls in coverage but fails to pay his or her share of premiums on a timely basis, the employer is nonetheless treated as offering coverage for that coverage period.

Reporting Requirements. Employers and insurers are required to file an annual information return with the IRS reporting health care coverage provided to employees and other individuals (¶ 2567) (Code Secs. 6055 and 6056; Notice 2013-45).

2003. Penalty for Employers Not Offering Health Care Coverage. Applicable large employers (¶ 2001) are liable for a shared responsibility payment (assessable payment) if:

- the employer fails to offer to its full-time employees and their dependents the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored group health plan for any month, and
- at least one full-time employee is certified as having enrolled in a qualified health plan through a Health Insurance Exchange and eligible to receive a premium tax credit (¶ 1331) or cost-sharing reduction payment (Code Sec. 4980H(a); Reg. § 54.4980H-4; Notice 2013-45).[7]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[4] ¶ 34,619ZA, ¶ 34,619ZBF, ¶ 34,619ZBL; HEALTH: 6,052; § 42,110

[5] ¶ 34,619ZBL; HEALTH: 6,056; § 42,110

[6] ¶ 34,619ZBO, ¶ 34,619ZBR; HEALTH: 6,054; § 42,125

[7] ¶ 34,619ZA, ¶ 34,619ZBO, ¶ 34,619ZD.35; HEALTH: 6,054; § 42,130.10

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The assessable payment for an employer not offering coverage with respect to any calendar month equals the number of the employer's full-time employees reduced by 30, multiplied by 1/12 of $2,260 for 2017 (Code Sec. 4980H(a), (c)(1) and (c)(5); T.D. 9655; Notice 2015-87).

The 30-employee reduction applies only for purposes of calculating the assessable payment (Code Sec. 4980H(c)(2)(D)). It does not apply for determining if the employer is an applicable large employer (i.e., 50-employee threshold). Also, a full-time employee does not include a full-time equivalent (FTE) employee for purposes of the payment calculation (Code Sec. 4980H(c)(2)(E)). Employers with common ownership or otherwise related are allowed only one 30-employee reduction which is allocated ratably among all the related employers.

An employer must pay the assessable payment upon notice and demand by IRS; it is not required to be included with the employer's tax return (Code Sec. 4980H(d)). The payment is assessed and collected in the same manner as an assessable penalty. However, it is not deductible as a business expense (Code Sec. 4980H(c)(7)).

2005. Penalty for Employers Offering Health Care Coverage. Applicable large employers (¶ 2001) are liable for a shared responsibility payment (assessable payment) if:

- the employer offers minimum essential coverage under an eligible employer-sponsored group health plan to its full-time employees and their dependents for any month, but
- at least one full-time employee is certified as having enrolled in a qualified health plan through a Health Insurance Exchange and eligible to receive an applicable premium tax credit (¶ 1331) or cost-sharing reduction payment because the coverage is not affordable to the employee or does not provide minimum value (Code Sec. 4980H(b); Reg. § 54.4980H-5; Notice 2013-45).[8]

Affordability. Coverage for an employee is affordable if the employee's share of the premium for self-only coverage, not family coverage, does not exceed 9.69 percent of the employee's annual household income for 2017 (9.56 percent for 2018) (Rev. Proc. 2016-24; Rev. Proc. 2017-36). The affordability test applies to the lowest-cost option available to the employee that also meets the minimum value requirement.

Safe harbors are provided for an employer to determine if coverage is affordable to an employee based on the employee's Form W-2 wages, the employee's rate of pay, or the federal poverty line. An employer may choose one or more safe harbors for all of its employees or any reasonable category of employees, so long as it is done on a uniform and consistent basis. The safe harbors only apply for purposes of the assessable payment; they do not affect an employee's eligibility for a premium tax credit.

Minimum Value. An employer-sponsored group health plan fails to provide minimum value if the plan's share of the total allowed costs of benefits provided under the plan is less than 60 percent of the costs, and generally fails to offer substantial coverage for in-patient hospitalization and physician services (Prop. Reg. § 1.36B-6).[9] An eligible employer-sponsored plan may determine whether it provides minimum value by: (1) a minimum value calculator provided by the IRS and the Department of Health and Human Services (HHS); (2) actuarial certification; (3) certain safe harbor plan designs; or (4) for plans in the small group market, meeting the requirements for bronze, silver, gold, or platinum level coverage.

Calculation of Assessable Payment. The assessable payment for an employer offering health care coverage with respect to any calendar month equals the number of the employer's full-time employees who receive a premium tax credit or cost-sharing reduction, multiplied by 1/12 of $3,390 in 2017 (Code Sec. 4980H(b) and (c)(5); Reg. § 54.4980H-5; Notice 2015-87).[10]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[8] ¶ 34,619ZA, ¶ 34,619ZBR, ¶ 34,619ZD.35; HEALTH: 6,054; § 42,130.15

[9] ¶ 4196U; HEALTH: 3,310; § 42,120

[10] ¶ 34,619ZA, ¶ 34,619ZBR; HEALTH: 6,054; § 42,130.15

The assessable payment for any calendar month is capped at the number of the employer's full-time employees for the month reduced by 30, multiplied by 1/12 of $2,260 for 2017. The cap ensures that the payment for an employer that offers coverage can never exceed the assessable payment the employer would owe if it did not offer coverage (¶ 2003).

An employer must pay the assessable payment upon notice and demand by the IRS; it is not required to be included with the employer's tax return (Code Sec. 4980H(d)). The payment is assessed and collected in the same manner as an assessable penalty. However, it is not deductible as a business expense (Code Sec. 4980H(c)(7)).

Health and Welfare Benefits

2011. Welfare Benefit Plans. A welfare benefit plan or welfare benefit fund is any fund through which an employer provides welfare benefits to employees, independent contractors, or their beneficiaries (Code Sec. 419).[11] Welfare benefits are benefits other than deferred compensation or transfers of restricted property, such as accident or health benefits, disability or death benefits, unemployment benefits, severance benefits, vacation, or similar benefits.

An employer may deduct contributions paid or accrued to a welfare benefit fund to the extent that the contributions do not exceed the qualified cost of the fund for the tax year, reduced by the after-tax income of the fund. If the employer's contributions to the fund are more than its qualified cost, the excess is carried over to the next tax year. Welfare benefits provided directly by an employer to an employee are deductible only in the tax year the employee includes the benefits in gross income or would include such benefits in gross income if they were taxable to the employee (¶ 906) (Code Sec. 404(b)(2)(A)).[12] An employer may not accrue and deduct unpaid welfare benefits.

A welfare benefit fund's qualified cost is the direct cost the employer would have been able to deduct using the cash method of accounting if it paid for the benefits directly (Code Sec. 419(c)). It also includes any addition to a qualified asset account—a reserve set aside for the payment of disability benefits, medical benefits, supplemental unemployment benefits (SUB) or severance pay benefits, and life insurance or death benefits (Code Sec. 419A).[13]

The allowable addition to a qualified asset account for a tax year is the amount that will bring the account to a level (the account limit) that is reasonably and actuarially necessary to fund the payment of incurred but unpaid benefits. In the case of post-retirement medical and life insurance benefits, the allowable addition is the amount required to fund the payment of such benefits on a level basis over the working lives of the covered employees based on current medical costs. For employers who do not support higher additions to a qualified asset account by actuarial certifications, there are safe harbor additions for the various benefits. Limits are placed on the level of disability, SUB, and severance pay benefits that may be considered in establishing the account limit for such benefits.

VEBAs. Collectively bargained voluntary employees' beneficiary associations (VEBAs) are exempt from the account limits applicable to welfare benefit funds (Code Sec. 419A(f)(5)). Thus, employer contributions to VEBAs are deductible and earnings are tax exempt. In addition, VEBAs that are funded solely with employee contributions are also exempt from the account limits if: (1) the VEBA covers at least 50 employees; and (2) no employee is entitled to a refund with respect to amounts in the fund, other than a refund based on the experience of the entire fund. VEBAs are tax-exempt trusts that provide life, sickness, accident, and other benefits to members, or their dependents or beneficiaries, and meet certain nondiscrimination requirements (Code Secs. 501(c)(9) and 505).[14]

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[11] ¶ 19,295; COMPEN: 42,100; § 9,345

[12] ¶ 18,330; COMPEN: 42,050; § 9,345

[13] ¶ 19,298; COMPEN: 42,150; § 9,345

[14] ¶ 22,602, ¶ 22,711; COMPEN: 54,100; § 33,005

2013. Employer Contributions to Accident and Health Plans. Contributions by an employer to an accident or health plan that provides coverage for personal injuries or sickness incurred by the employee and his or her spouse, dependent, or child under the age of 27, are excluded from the employee's gross income (Code Sec. 106; Reg. § 1.106-1).[15] If a plan provides other benefits in addition to accident and health benefits, the exclusion applies only to the part of the employer's contributions that is allocable to accident and health benefits. See ¶ 2015 for a further discussion of accident and health plans. See ¶ 322 and ¶ 421 for a discussion of accident and health insurance premiums paid by a partnership or S corporation.

An employer generally contributes to an accident or health plan by paying a portion of the premium for accident and health insurance, or by contributing to a separate trust or fund that provides benefits directly or through insurance. A qualified long-term care insurance contract is generally treated as an accident and health insurance contract for this purpose (¶ 2019). Employer contributions for the cost of long-term care insurance provided through a flexible spending account (FSA) or similar arrangement (¶ 2041) are included in the employee's wages for income tax purposes, but they are excluded from wages for FICA and FUTA purposes (Code Sec. 106(c)).

Employer contributions to an employee's health savings account (HSA) (¶ 2035) or Archer medical savings account (MSA) (¶ 2037) may be excluded from an employee's gross income as employer-provided coverage for medical expenses under an accident or health plan to the extent they do not exceed the HSA or MSA limits (Code Sec. 106(b) and (d)). If an employer makes such contributions, it must make comparable contributions on behalf of all employees with comparable coverage during the same period (Code Secs. 4980E and 4980G).[16] Payments or reimbursements made under a qualified small employer health reimbursement account (QSEHRA) (¶ 2039) are includible in gross income if in the month of which the medical expense is incurred the individual does not have minimal essential coverage (Code Sec. 106(g), as added by the 21st Century Cures Act (P.L. 114-255)). Employer contributions paid for COBRA continuation coverage of a former employee (¶ 2021) may also be excluded as coverage under an accident or health plan (IRS Pub. 15-B).

2015. Accident and Health Benefits. Amounts received by an employee under an employer-financed accident and health plan are generally excluded from gross income if received as:

- reimbursements for medical care of the employee, his or her spouse, dependent, or child under the age of 27 to the extent the medical expenses were not deducted by the employee in a prior tax year (Code Sec. 105(b); Reg. § 1.105-2);[17] or

- payments for permanent injury or loss of bodily function (i.e., disability) of the employee, spouse, or dependent, so long as the payments are based on the nature of the injury rather than length of time the employee is absent from work (Code Sec. 105(c); Reg. § 1.105-3).[18]

Amounts received by an employee through an accident and health insurance that are not reimbursements of medical expenses, but are instead payments for personal injuries or sickness, generally are included in gross income if they are attributable to contributions by the employer that were not included in the employee's gross income or paid directly by the employer (¶ 2014) (Code Sec. 105(a); Reg. § 1.105-1).[19] Amounts the employee receives that are not attributable to employer contributions, such as benefits attributable to the employee's own contributions, are not included in gross income. Payments or reimbursements made under a qualified small employer health reimbursement account (QSEHRA) (¶ 2039) are includible in gross income if in the month of

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[15] ¶ 6800, ¶ 6801; HEALTH: 12,102; § 42,220

[16] ¶ 34,615, ¶ 34,619B; HEALTH: 9,306; § 42,515.35, § 42,615.10

[17] ¶ 6700, ¶ 6703; HEALTH: 12,104; § 42,215

[18] ¶ 6700, ¶ 6705; HEALTH: 12,200; § 42,215

[19] ¶ 6700, ¶ 6701; HEALTH: 12,104; § 42,215

which the medical expense is incurred the individual does not have minimal essential coverage (Code Sec. 106(g), as added by the 21st Century Cures Act (P.L. 114-255)).

Employee. An employee for this purpose includes any current, retired, and former employee, as well as a widow or widower of a retired employee and any individual who dies while an employee. It also includes a leased employee who provides services on substantially full-time basis (IRS Pub. 15-B). Self-employed individuals are not considered employees and the cost of their employer-provided accident and health insurance is included in their gross income (Code Sec. 105(g); Reg. § 1.105-5(b)).[20] However, a self-employed individuals may deduct from gross income 100 percent of amounts paid for health insurance coverage (¶ 908). Partners in a partnership and two-percent or greater shareholders of an S corporation who are employees are considered to be self-employed.

Dependents. A dependent for this purpose is the same as for claiming the dependency exemption, but without regard to whether the dependent claims dependency exemptions (¶ 137), files a joint return (¶ 138), or has gross income in excess of the exemption amount for the year (¶ 137A). If certain conditions are met, the IRS will treat the child of divorced or separated parents as a dependent of both parents under an employer accident and health plan (Code Sec. 105(b)).

Accident and Health Plan. An accident and health plan is any arrangement of an employer that provides benefits to employees and their spouses, dependents, and children under age 27 in the event of personal injury or sickness (Code Sec. 105(e); Reg. § 1.105-5(a)).[21] The plan may be insured or not insured, and does not need to be in writing. A qualified long-term care insurance contract is generally treated as an accident and health insurance contract for this purpose (¶ 2019). A sickness and disability fund for employees maintained by a state, the District of Columbia, or Indian tribal government are also treated the same as an employer accident and health plan (Code Sec. 7871(a)(6)(A)). Qualified health care benefits provided by an Indian tribal government may also be excluded from gross income (¶ 2027). An employer's accident and health plan must not discriminate in favor of highly compensated individuals (¶ 2017).

COBRA Coverage. A group health plan provided by an employer must offer each qualified beneficiary who would otherwise lose coverage as a result of a qualifying event, an opportunity to elect continuation coverage referred to as COBRA continuation coverage (¶ 2021).

Railroad Unemployment Insurance. Benefits paid to an employee under the Railroad Unemployment Insurance Act for sick days are included in the employee's gross income unless an illness is due to an on-the-job injury (Code Sec. 105(i)).[22]

Annuity Rules. Amounts received as accident or health benefits are generally not taxable under the annuity rules of Code Sec. 72 (Reg. § 1.72-15).[23] However, some employer-established plans pay participants both amounts taxable under the annuity rules (¶ 817) and amounts excludable from gross income as payments under an accident or health plan. Specific rules are provided for determining which amounts are excludable in these cases. Benefits attributable to the employee's contributions are excludable from gross income under the rules at ¶ 851.

2017. Nondiscrimination Requirements for Employer Health Plans. An employer's self-insured medical reimbursement plan must not discriminate in favor of highly compensated individuals in terms of eligibility for coverage or benefits offered under the plan (Code Sec. 105(h); Reg. § 1.105-11).[24] For plan years beginning on or after September 23, 2010, similar nondiscrimination requirements apply to group health plans other than self-insured plans. However, compliance for group health plans will not be required until additional guidance is issued (Code Sec. 9815; Notice 2011-1). For a discussion of employer health reimbursement arrangements (HRAs), see ¶ 2039.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[20] ¶ 6700, ¶ 6708; HEALTH: 12,100; § 42,215

[21] ¶ 6700, ¶ 6708; HEALTH: 12,104; § 42,225

[22] ¶ 6700; HEALTH: 12,104

[23] ¶ 6124; INDIV: 30,152.05; § 42,225

[24] ¶ 6700, ¶ 6711; HEALTH: 9,050; § 42,155.10

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Excess reimbursements paid to a highly compensated individual under a plan that fails to meet the nondiscrimination requirements are includible in the individual's gross income. A highly compensated employee for this purpose is an employee who is one of the five highest paid officers, among the highest paid 25 percent of all employees, or a shareholder owning more than 10 percent in value of the company's stock.

The entire amount of a reimbursement with respect to a benefit that is available only to highly compensated individuals is treated as an excess reimbursement includible in income. In the case of a plan that discriminates in terms of eligibility, the includible excess reimbursement is equal to all the medical expenses for which the highly compensated individual was reimbursed times a fraction—the numerator of which is the total amount reimbursed to all participants who are highly compensated individuals and the denominator is the total amount reimbursed to all employees under the plan for the plan year. If the plan discriminates in terms of eligibility *and* benefits, any amount which is included in income by reason of the benefits not being available to all other participants is not to be taken into account in determining the excess reimbursements that result from the plan being discriminatory in terms of eligibility.

There is no eligibility discrimination if the plan benefits: (1) at least 70 percent of all employees or 80 percent of all eligible employees if at least 70 percent of all employees are eligible; or (2) a class of employees found by the IRS not to be discriminatory in favor of highly compensated individuals. Certain employees, such as part-time workers, employees with less than three years of service, employees under age 25, and employees excluded as a result of a collective bargaining agreement, may be excluded from coverage. There is no benefits discrimination if the self-insured medical expense plan provides the same benefits for non-highly compensated employees as it does for highly compensated employees.

2019. Long-Term Care Insurance. A qualified long-term care insurance contract is treated as an accident and health insurance contract, and any employer plan providing coverage under a qualified long-term care insurance contract is treated as an accident and health plan (Code Sec. 7702B).[25] Amounts received under the contract other than dividends and refunds are excluded from the recipient's gross income as amounts received for personal injuries and sickness (¶ 2015). The exclusion does not apply to long-term care insurance coverage provided under a cafeteria plan (¶ 2045) or flexible spending arrangement (¶ 2041) (Code Secs. 106(c) and 125(f)).[26] Premiums paid by an individual for a qualified long-term care insurance contract may be deducted as a medical expense (¶ 1019).

A qualified long-term care insurance contract is an insurance contract that only provides coverage of qualified long-term care services, including necessary diagnostic, preventive, and treatment services, or personal care services required by a chronically ill individual and prescribed by a licensed health care practitioner (Code Sec. 7702B(b) and (c)).[27] In addition, the contract must be guaranteed renewable, must not provide a cash surrender value, and must meet certain consumer protection provisions.

2021. COBRA Continuation Coverage. A group health plan provided by an employer with 20 or more employees must offer each covered employee, as well as his or her spouse and dependent, who would lose coverage as a result of a qualifying event, an opportunity to elect to continue coverage referred to as COBRA coverage (Code Sec. 4980B).[28] A qualifying event with respect to a covered employee includes death, termination of employment or reduction of hours, divorce or legal separation, eligibility for Medicare, a dependent child ceasing to be a dependent, or bankruptcy of the employer. Group health plans that fail to provide COBRA coverage to qualified beneficiaries are subject to an excise tax.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[25] ¶ 43,166; HEALTH: 12,150; § 7,240.15

[26] ¶ 6800, ¶ 7320; HEALTH: 12,150

[27] ¶ 43,166; HEALTH: 12,150; § 7,240.15

[28] ¶ 34,600; HEALTH: 24,100; § 42,801

The option to elect COBRA coverage must allow the qualified beneficiary to purchase medical coverage under the company plan at group, rather than individual, rates for at least 18 months for most qualified beneficiaries (36 months in limited circumstances). The plan may require the beneficiary to pay premiums for the continuation coverage not to exceed 102 percent of the applicable premium for the coverage period. The continuation coverage must be identical to the coverage provided to similarly situated beneficiaries under the plan for whom no qualifying event has occurred.

2023. Wellness Programs; Employee Assistance Programs. Wellness programs or employee assistance programs (EAPs) are generally part of an employer's overall health promotion for employees and may be one of several methods used to reduce health care costs. Although many EAPs are initiated to deal with drug and alcohol abuse, EAPs may also address family problems, stress, job termination, finances, and retirement. Because EAPs commonly provide treatment for drug and alcohol abuse and other similar health and medical problems, they often qualify as employee welfare benefit plans (¶ 2011). However, if an EAP merely provides referrals and does not pay for any services or benefits, the EAP will not be deemed to be an employee welfare benefit plan (Pension Welfare Benefits Administration (PWBA) Opinion Letter 91-26A).

2025. Disability Benefits Under Employer Insurance Plan. Disability income plans are employer plans, some mandated by state law, that provide full or partial income replacement for employees who become disabled. To the extent an employer offers such coverage under an accident and health plan, whether benefits received by employees are taxable depends on who pays for the premiums and whether they are paid on an after-tax basis (¶ 2015) (Code Sec. 105(a)).

2027. Indian Health Care Benefits. Qualified health care benefits provided by Indian tribal governments to a member of an Indian tribe, or to a member's spouse or dependent, are excluded from the beneficiary's gross income (Code Sec. 139D).[29] A qualified health care benefit includes:

- any health service provided or purchased by the Indian Health Service through a grant, contract or compact with an Indian tribe or tribal organization, or through a program funded by the Indian Health Service;
- medical care provided or purchased, or reimbursements for such medical care, by an Indian tribe or tribal organization for a member of an Indian tribe, the member's spouse or dependent;
- coverage under an accident or health insurance plan provided by an Indian tribe or tribal organization for medical care to a member of an Indian tribe, the member's spouse or dependent; and
- any other medical care provided by an Indian tribe or tribal organization that supplements, replaces or substitutes for medical care programs and services provided by the federal government to Indian tribes or their members.

The exclusion does not apply to Indian health care benefits that are not includible in the beneficiary's gross income under another provision in the Code or to any benefit for which the beneficiary may claim a deduction.

2028. Indian General Welfare Benefits. Indian general welfare benefits provided to, or on behalf of, a member of an Indian tribe, the member's spouse, or dependents are excluded from the recipient's gross income (Code Sec. 139E).[30] An Indian general welfare benefit is any payment made, or services provided, under an Indian tribal government program administered under specific guidelines and which does not discriminate in favor of members of the governing body of the Indian tribe. A program will not fail to be treated as an Indian tribal government program solely by reason of it being established by tribal custom or government practice. Benefits under the program must be available to any tribal member and must be for the promotion of general welfare. In

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[29] ¶ 7649N; INDIV: 33,512; § 3,715

[30] ¶ 7649V; INDIV: 33,364; § 4,050

addition, benefits must not be lavish or extravagant, and not provided as compensation for services. Any items of cultural significance, reimbursement of costs, or cash honorarium for participation in cultural or ceremonial activities for the transmission of tribal culture will not be treated as compensation.

2029. Subsidies for Retiree Prescription Drug Plans. An employer that provides a qualified retiree prescription drug plan to its retired employees is eligible for a special subsidy payment each year from the federal government based on the cost of providing the coverage to qualified retirees (Social Security Act, § 1860D-22). The subsidy payment is excludable from the employer's gross income for both regular income tax and alternative minimum tax (AMT) purposes (Code Sec. 139A).[31] The amount otherwise allowable as a deduction to the employer for retiree prescription drug costs is reduced by the amount of the excludable subsidy received by the employer.

2031. Medical Loss Ratio Rebates. Health insurance issuers may be required to pay medical loss ratio (MLR) rebates to policyholders in the form of either cash payments or premium reductions. For policies purchased on the individual insurance market, MLR rebates are taxable or nontaxable depending on whether the individual deducted the premium payments (www.irs.gov, IRS FAQs, Medical Loss Ratio (MLR)). If the individual did not deduct the premiums for the year, an MLR rebate received in the following year is excluded from income whether received as cash or premium reduction. If the individual deducted the premiums, then an MLR rebate received in the following year is treated as the recovery of an itemized deduction under the tax benefit rule (¶ 799).

For policies purchased by an employee through an employer-sponsored group health plan, MLR rebates are taxable or nontaxable depending on whether the employee used pre-tax or after-tax dollars to pay the health insurance premiums. If the employee used pre-tax dollars, then any MLR rebate received is subject to income and employment taxes. If the employee used after-tax dollars and MLR rebates are paid only to employees who participated in the plan both in the year the premiums were paid and in the year the rebates are received, then a rebate is not included in income if the employee did not deduct the premiums. If, however, MLR rebates are provided to all employees participating in the group health plan in the year the rebates are paid, regardless of whether the employee participated in the plan in the year the premiums were paid, then the rebates are not included in income if the employee used after-tax dollars.

HSAs, HRAs, and FSAs

2035. Health Savings Accounts (HSAs). A health savings account (HSA) is a trust or custodial account established for the exclusive purpose of paying for qualified medical expenses of the account beneficiary (Code Sec. 223).[32] HSAs can be established by an employee through an employer's cafeteria plan (¶ 2045) or by individual outside the employment context.

Eligibility. To be eligible to establish an HSA in any month, an individual:

- must be covered by a high-deductible health plan (HDHP) on the first day of the month,
- must not be covered by any other plan that is not a HDHP,
- must not be enrolled in Medicare, and
- cannot be claimed as a dependent on another person's tax return (Code Sec. 223(c)(1)).[33]

Exceptions exist for permitted coverage under certain non-HDHPs including coverage for accidents, disability, dental care, vision care, long term care, or prescription drugs. Also allowed is permitted insurance for a specified disease or illness, insurance paying a fixed amount per day (or other period) for hospitalization, and insurance if substantially all the coverage relates to liabilities for workers' compensation, ownership

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[31] ¶ 7649; HEALTH: 9,250

[32] ¶ 12,776; HEALTH: 18,050; § 42,501

[33] ¶ 12,776; HEALTH: 18,056; § 42,510.05

or use of property (for example, auto insurance), or torts. An individual will not fail to be treated as an eligible individual solely because he or she receives hospital care or medical services under any law administered by the Department of Veterans Affairs for a service-connected disability (Code Sec. 223(c)(1)).

While covered by an HSA, an individual generally may not be covered by a health flexible spending arrangement (FSA) (¶ 2041) or health reimbursement account (HRA) (¶ 2039) sponsored by the individual's employer or spouse's employer unless it is a limited purpose FSA or HRA, a suspended HRA, a post-deductible health FSA or HRA, or a retirement HRA. Coverage under a general purpose health FSA during a grace period is disregarded in determining if tax deductible contributions can be made to an HSA for that period if the balance in the health FSA at the end of the plan year is zero or the entire remaining balance in the health FSA at the end of the plan year is contributed to an HSA in a qualified HSA distribution.

A taxpayer who is an eligible individual for an HSA on the first day of the last month of a tax year is treated as eligible during every month of the year. If the taxpayer ceases to be eligible during the period beginning with the last month of the tax year and ending on the last day of the 12th month following that month, he or she must include in gross income an amount equal to the amount actually contributed minus the sum of the monthly contribution limits to which the individual would otherwise have been entitled. An additional 10-percent tax is imposed on this amount. Recapture does not apply if the taxpayer is ineligible due to death or disability (Code Sec. 223(b)(8); Notice 2008-52).[34]

Dependent. The definition of a dependent for purposes of an HSA is the same as for claiming a dependency exemption, but determined without regard to whether the dependent claims dependency exemptions (¶ 137), files a joint return (¶ 138), or has gross income in excess of the exemption amount for the year (¶ 137A) (Code Sec. 223(d)(2)(A)). If certain conditions are met, the IRS will treat the child of divorced or separated parents as a dependent of both parents, without a declaration by the custodial parent releasing the claim to the dependency exemption (¶ 139A) (Rev. Proc. 2008-48).[35]

Contributions. Cash contributions may be made to an HSA by the eligible individual, the individual's employer, or any other person on behalf of the eligible individual. Contributions made by an individual outside the employment context are deductible as an above-the-line deduction in calculating adjusted gross income (AGI) (Code Secs. 62(a)(19) and 223(a)). Employer contributions to an employee's HSA may be excluded from the employee's gross income (¶ 2013). An individual must report all contributions to his or her HSA on Form 8889.

The maximum amount that can be contributed for 2017 is $3,400 for self-only coverage or $6,750 for family coverage (Rev. Proc. 2016-28). The maximum amount that can be contributed for 2018 is $3,450 for self-only coverage or $6,900 for family coverage (Rev. Proc. 2017-37). The contribution limit is increased $1,000 if the individual reaches age 55 by the end of the tax year. The annual limit applies to all HSAs of the eligible individual combined, and all contributions made by anyone to the accounts. The limit is decreased for any month the participant is not an eligible individual. Excess contributions are subject to a six-percent excise tax. Contributions cannot be made after the participant attains age 65 or is enrolled in Medicare (Notice 2008-59, amplifying Notice 2004-2; Notice 2004-50).[36]

Married Taxpayers. For married individuals, if either spouse has family coverage under any health plan, then both will be treated as having only family coverage under the plan. If each spouse has family coverage under different plans, then both spouses are treated as having coverage under the plan with the lowest deductible (Code Sec. 223(b)(5)). If only one spouse is an eligible individual, only that spouse may contribute to an HSA (Notice 2004-50). If one or both spouses have family coverage, the contribution limit is the lowest deductible amount, divided equally between the spouses unless they agree on a different division, and further reduced by any contribution to an Archer

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[34] ¶ 12,776, ¶ 12,785.25; HEALTH: 18,058; § 42,515.10

[35] ¶ 6702.27; HEALTH: 18,062; § 1,215.40

[36] ¶ 12,785.25, ¶ 12,785.50; HEALTH: 18,058, HEALTH: 18,060; § 42,540

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medical savings account (MSA) (¶ 2037). Both spouses may make the catch-up contributions for individuals age 55 or over without exceeding the family coverage limit (Notice 2008-59, amplifying Notice 2004-2).

If a husband and wife are each eligible to make catch-up contributions, each spouse can make such contributions only to his or her own HSA. The maximum annual contribution limit for a married couple is the statutory maximum for family coverage where: (1) one spouse has family coverage and the other spouse has self-only coverage, regardless of whether the family coverage includes the spouse with self-only coverage; or (2) both spouses have family coverage, regardless of whether each spouse's family coverage covers the other spouse. A married taxpayer covered under an HDHP can contribute to an HSA for use with qualifying out-of-pocket medical expenses even if his or her spouse's coverage is nonqualifying family coverage, as long as the taxpayer is not covered by the spouse's policy (Rev. Rul. 2005-25).

HDHP Defined. An HDHP is a plan with (1) an annual deductible of at least $1,300 for 2017 ($1,350 for 2018) for self-only coverage, or $2,600 for 2017 ($2,700 for 2018) for family coverage; and (2) an annual out-of-pocket expenses limit of $6,550 for 2017 ($6,650 for 2018) for self-only coverage or $13,100 for 2017 ($13,300 for 2018) for family coverage (Rev. Proc. 2016-28; Rev. Proc. 2017-37). Out-of-pocket expenses include deductibles, co-payments and other amounts (other than premiums) that must be paid for plan benefits (Code Sec. 223(c)(2); Notice 2008-59, amplifying Notice 2004-2).[37]

Distributions. Distributions from an HSA are excluded from the account beneficiary's gross income only if used to pay or be reimbursed for qualified medical expenses incurred during the coverage period (Code Sec. 223(f)).[38] Qualified medical expenses are those specified in the plan that would generally qualify as an itemized deduction and incurred by the account beneficiary, his or her spouse, or dependents (¶ 1016). Nonprescription medicines (other than insulin) are not considered qualified medical expenses under an HSA (Code Sec. 223(d)(2)). In addition, health insurance premiums are not qualified medical expenses under an HSA unless for long-term care insurance, COBRA continuation coverage, health care coverage while receiving unemployment compensation, or Medicare. Distributions from an HSA not used for qualified medical expenses are included in the account beneficiary's gross income and subject to a 20 percent additional tax, unless made after the beneficiary reaches age 65, dies, or becomes disabled. The additional tax is not treated as a tax liability for purposes of the alternative minimum tax (¶ 1420).

Contributions by Partnership or S Corporation. Contributions made by a partnership or S corporation to a partner's or shareholder's HSA are generally treated as payments to the partner or shareholder and includible in gross income. The individual partner or shareholder may treat the contribution as an above-the-line deduction (an adjustment to gross income). However, a contribution to the partner's HSA by the partnership for services rendered is treated as a guaranteed payment, and the partnership may deduct the contribution as a business expense. Similarly, a contribution by a S corporation to a two-percent shareholder's HSA for services rendered is deductible by the S corporation and included in the shareholders income (Notice 2005-8).[39]

Distributions to Fund HSAs. An eligible individual can make a one-time qualified HSA distribution directly from his or her IRA to his or her HSA (¶ 2165). The amount that can otherwise be contributed to the HSA for the tax year of the distribution is reduced by the amount contributed from the IRA, and the individual cannot deduct the distribution amount as an HSA contribution (Code Sec. 223(b)(4)(C); Notice 2008-51).[40] An eligible individual can also roll over distributions from another HSA or Archer MSA into an HSA. The taxpayer does not have to be an eligible individual to make a rollover contribution from an existing HSA to a new HSA (Code Sec. 106(e)).

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[37] ¶ 12,776, ¶ 12,785.25, ¶ 12,785.50; HEALTH: 18,074; § 42,510.10

[38] ¶ 12,776; HEALTH: 18,062; § 42,520.10, § 42,525

[39] ¶ 12,785.25; HEALTH: 18,054; § 42,515.05

[40] ¶ 12,776; HEALTH: 18,072; § 42,515.40

2037. Archer Medical Savings Accounts (MSAs). An Archer medical savings account (MSA) is a trust or custodial account established for the exclusive purpose of paying for qualified medical expenses of the account beneficiary, his or her spouse, or dependents (Code Sec. 220).[41] Archer MSAs operate almost exactly the same as health savings accounts (HSAs) (¶ 2035), except that new Archer MSAs may *not* be established after 2007. An individual can still utilize an Archer MSA if he or she was an active participant in the MSA before 2008, or he or she became an active participant for a tax year ending after 2007 by reason of coverage under a high deductible health plan (HDHP) of an Archer MSA participating employer.

To qualify for an Archer MSA, an individual or spouse must be either an employee of a small employer or self-employed person that maintains an HDHP. A small employer for this purpose is generally an employer who had an average of 50 or fewer employees during either of the last two calendar years. Like HSAs, the individual can have no other health care coverage, including under Medicare.

An HDHP under an Archer MSA has higher annual deductibles and lower out-of-pocket limits than under an HSA: (1) for self-only coverage, the minimum deductible is $2,250 for 2017 ($2,300 for 2018), the maximum deductible is $3,350 for 2017 ($3,450 for 2018), and the maximum out-of-pocket limitation is $4,500 for 2017 ($4,600 for 2018); and (2) for family coverage, the minimum deductible is $4,500 for 2017 ($4,600 for 2018), the maximum deductible is $6,750 for 2017 ($6,850 for 2018), and the maximum out-of-pocket limitation is $8,250 for 2017 ($8,400 for 2018) (Rev. Proc. 2016-55; Rev. Proc. 2017-58).

Contributions. Cash contributions may be made to an Archer MSA by the eligible individual or the individual's employer. Contributions made by the individual outside of the employment contact are deductible as an above-the-line deduction in calculating adjusted gross income (AGI) (Code Secs. 62(a)(16) and 220(a)). Employer contributions to an employee's MSA may be excluded from the employee's gross income (¶ 2013). An individual must report all contributions to an MSA on Form 8853. Annual contributions to an Archer MSA are limited to 75 percent of the deductible of the required health insurance plan (65 percent if a self-only plan). Contributions are also limited by an employee's compensation or the income earned from a self-employed individual's business (Code Sec. 220(b)). Excess contributions are subject to an excise tax.

Distributions. Distributions from an Archer MSA are excluded from the account beneficiary's gross income only if used to pay or be reimbursed for qualified medical expenses incurred during the coverage period (Code Sec. 220(f)). Qualified medical expenses are those specified in the plan that would generally qualify as an itemized deduction and incurred by the account beneficiary, his or her spouse, or dependents (¶ 1016). Nonprescription medicines (other than insulin) are not considered qualified medical expenses under an MSA. In addition, health insurance premiums are not qualified medical expenses under an MSA unless for long-term care insurance, COBRA continuation coverage, and health care coverage while receiving unemployment compensation. Distributions from an MSA not used for qualified medical expenses are included in the account beneficiary's gross income and subject to a 20 percent additional tax, unless made after the beneficiary reaches age 65, dies, or becomes disabled. The additional tax is not treated as a tax liability for purposes of the alternative minimum tax (¶ 1420).

Medicare Advantage MSAs. Medicare Advantage MSAs are medical savings accounts that must be used in conjunction with a high deductible Medicare Advantage MSA health plan (Code Sec. 138).[42] Individuals eligible for Medicare are permitted to have their Medicare benefits deposited directly into a Medicare Advantage MSA and can make trustee-to-trustee transfers from Archer MSAs to these MSAs. Income earned on the account and withdrawals used to pay health care expenses are not included in the individual's income.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[41] ¶ 12,670; HEALTH: 18,200; § 42,601

[42] ¶ 7630; HEALTH: 18,250; § 42,615

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2039. Health Reimbursement Arrangements (HRAs). A health reimbursement arrangement (HRA) is an employer-funded plan that reimburses employees for qualified medical care expenses (Notice 2002-45, amplified by Rev. Rul. 2006-36).[43] An HRA is funded solely by employer contributions and may not be funded through employee salary deferrals under a cafeteria plan (¶ 2045). The plan must provide reimbursements up a maximum dollar amount for a coverage period. Any unused amounts in an HRA can be carried forward for reimbursements in later years. To the extent an HRA constitutes an employer-provided accident or health plan (¶ 2015), coverage and reimbursements of qualified medical care expenses are generally excludable from the employee's gross income.

An HRA may be offered in conjunction with other provided health benefits, such as a group health plan or health FSA (¶ 2041). An HRA is generally subject to an excise tax for failing to meet group health plan requirements unless they are integrated with an employer's minimum essential coverage, and reimbursements cannot be used to obtain individual coverage on a health exchange. Exceptions are provided for stand-alone retiree plans and plans with fewer than two participants.[44]

An exception is also provided for a qualified small employer health reimbursement arrangement (QSEHRA) effective for years beginning after December 31, 2016 (Code Sec. 9831(d), as added by the 21st Century Cures Act (P.L. 114-255)).[45] As a result, a small employer may offer a stand-alone HRA and reimburse employees with pre-tax dollars for the cost of individual health care coverage through a QSEHRA without incurring the penalty for failing to meet the group health plan requirements. A QSEHRA must limit payments or reimbursements for the year to $4,950 for employee-only coverage or $10,000 for family coverage ($5,050 and $10,250, respectively, for 2018) (Rev. Proc. 2017-58). Under transitional relief, small employers are also exempted from the penalty for an HRA failing to meet group health care requirements for plan years beginning after 2013 and before 2017 (Notice 2015-17; Act Sec. 18001(a)(7)(B) of P.L. 114-255)). An eligible employer must furnish a written notice to its eligible employees at least 90 days before the beginning of a year for which the QSEHRA is provided. However, the notice requirement is suspended for a QSEHRA provided to eligible employees for a year beginning in 2017 (Notice 2017-20).

Distributions from an HRA can only be used to reimburse the employee for his or her qualified medical expenses incurred during the coverage period. Qualified medical expenses are those specified in the plan that would generally qualify as an itemized deduction and incurred for the employee, spouse, dependent, or child under the age of 27 (¶ 1016). Nonprescription medicines (other than insulin) are not considered qualified medical expenses under an HRA (Code Sec. 106(f)).[46]

2041. Flexible Spending Arrangements (FSAs). A flexible spending arrangement (FSA) is an employer-established benefit program under which amounts credited to an employee's account may be used to reimburse the employee for health care, dependent care, or adoption expenses that would otherwise be excludable from the employee's gross income if paid by the employer (Prop. Reg. § 1.125-5).[47] An FSA may be funded by employer contributions or by a salary reduction agreement with pre-tax dollars as part of a cafeteria plan (¶ 2045).

The plan must provide either a maximum dollar limit or maximum percentage of compensation that can be contributed through a cafeteria plan. In the case of a health FSA, the maximum contribution is limited to $2,600 for 2017 ($2,650 for 2018) (Code Sec. 125(i); Rev. Proc. 2016-55; Rev. Proc. 2017-58).[48] If the plan allows salary reduction contributions to a health FSA in excess of the annual dollar amount, then the employee will be subject to tax on distributions from the health FSA. In the case of an adoption or dependent FSA, the maximum contribution is limited to the amount the employee could exclude under a adoption assistance program (¶ 2063) or dependent care assistance program (¶ 2065).

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[43] ¶ 6702.73; HEALTH: 18,100; § 42,401
[44] ¶ 34,963.054; HEALTH: 18,108; § 42,405
[45] ¶ 44,089K.35, ¶ 44,090; HEALTH: 18,108; § 42,405.
[46] ¶ 6800; HEALTH: 18,100; § 42,401
[47] ¶ 7323F; COMPEN: 51,200; § 42,701
[48] ¶ 7320, ¶ 7324.45; COMPEN: 51,200; § 42,701

An FSA may not be used to defer compensation; any balance remaining in the account at the end of the plan year is generally forfeited (use-it-or-lose-it rule) (Prop. Reg. § 1.125-5(c); Notice 2005-42).[49] However, a plan may permit a grace period of up to 2½ months after the end of the plan year (March 15 for calendar year plans) during which qualified expenses incurred during the period can be paid from any amounts left in the account at the end of the previous year. The employer is not permitted to refund any balance in an FSA account to an employee.

A cafeteria plan may also allow up to $500 of any balance remaining in a health FSA at the end of the year to be carried over to pay or reimburse qualified medical expenses incurred in the next year (Notice 2013-71). The carried over amount does not count against the maximum contribution an employee can make to the health FSA. Any unused amount in a health FSA at the end of the year in excess of $500 (or lower amount specified in the plan) is forfeited. A plan that adopts the carryover option may not also provide the 2½ month grace period.

Special Rules for Health FSAs. Health FSA plans must comply with the rules applicable to other accident and health plans, including the nondiscrimination requirements for highly compensated employees (¶ 2017). Distributions from a health FSA can only be used to reimburse the employee for qualified medical expenses incurred during the coverage period. Qualified medical expenses are those specified in the plan that would generally qualify as an itemized deduction and incurred for the employee, spouse, dependent, or child under the age of 27 (¶ 1016). Nonprescription medicines (other than insulin) are not considered qualified medical expenses under an FSA (Code Sec. 106(f)).[50]

Qualified Reservist Distribution. A cafeteria plan may allow for distribution of any remaining balance of a health FSA for any reason to a participant who is called to active duty for a period of at least 180 days due to his or her membership in a reserve unit of the military (Code Sec. 125(h)). The distribution must be made between the date of the order and the last day for which reimbursements can be made during the plan year.

Family and Medical Leave Act. The Family and Medical Leave Act (P.L. 103-3) (FMLA) imposes certain requirements on employers regarding coverage, including family coverage, under group health plans for employees taking FMLA leave and regarding the restoration of benefits to employees who return from FMLA leave. Reg. § 1.125-3 provides guidance on the effect of the FMLA on the operation of cafeteria plans.

Cafeteria Plans

2045. Cafeteria Plans. Cafeteria plans are employer-sponsored benefit packages that offer employees a choice between taking cash and receiving qualified benefits which may be excluded from gross income (Code Sec. 125; Prop. Reg. § 1.125-1).[51] If a participant chooses cash, it is includible in gross income as compensation. If qualified benefits are chosen, they are excludable to the extent allowed under the Code. A cafeteria plan cannot offer anything other than cash or qualified benefits. An employer who maintains a cafeteria plan is required to file an information return, but the reporting requirement has been suspended indefinitely (Code Sec. 6039D; Notice 2002-24).[52]

Cafeteria plan elections must be made before the start of the plan year and are generally irrevocable unless the employee experiences a change in status (i.e., marital status, number of dependents, etc.). However, an employer may permit elections regarding health care coverage to be revoked for employees expected to average less than 30 hours of service per week who nevertheless are still eligible for coverage under the employer plan, and employees who would like to cease employer coverage and buy health care coverage through an American Health Benefit Exchange (see later) without a period of duplicate or no coverage (Notice 2014-55).

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[49] ¶ 7323F; COMPEN: 51,212; § 42,710
[50] ¶ 6800; HEALTH: 18,150; § 42,710
[51] ¶ 7320, ¶ 7321; COMPEN: 51,000; § 20,801
[52] ¶ 35,660, ¶ 35,661.50; COMPEN: 51,058; § 39,155.25

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A cafeteria plan may include any of the following qualified benefits: accident and health benefits (¶ 2015) including benefits under a flexible spending arrangement (FSA) (¶ 2041), adoption assistance benefits (¶ 2063), dependent care assistance benefits (¶ 2065), disability coverage (¶ 2025), group-term life insurance (¶ 2055), and health savings accounts (HSAs) (¶ 2035). A qualified benefit does *not* include benefits under an Archer medical savings accounts (MSAs) (¶ 2037), scholarships and fellowship grants (¶ 865), educational assistance benefits (¶ 2067), long-term care insurance (¶ 2019), or statutory fringe benefits under Code Sec. 132 (¶ 2085). A plan that provides deferred compensation is generally *not* included in the definition of a cafeteria plan. However, elective contributions under a qualified cash or deferred arrangement, profit-sharing plan, stock bonus plan, such as a 401(k) plan (¶ 2121), or contributions by an educational institution for post-retirement group life insurance are permitted.

Highly compensated employees (¶ 2114) are not entitled to exclude any benefit under a cafeteria plan attributable to a plan year in which the plan discriminates in favor of the highly compensated employees with respect to participation, contributions, and benefits. Key employees (¶ 2132) are not entitled to exclude any benefit attributable to a plan year in which the statutory qualified benefits provided to all key employees exceed 25 percent of the total of such benefits provided to all employees under the plan. In such cases, the benefits must be included in the gross income of the highly compensated employees or key employees for the tax year in which the plan year ends (Code Sec. 125(b)).

American Health Benefit Exchange Plans. An American Health Benefit Exchange (otherwise known as a Marketplace Exchange) and Small Business Health Options Program (SHOP) Exchange, run either by a state or the federal government, are generally available in every state and provide qualified individuals and small businesses with access to health plans, possibly at subsidized prices. Qualified health plans offered through such an exchange cannot be provided by employers through a cafeteria plan unless the employer is exchange-eligible (Code Sec. 125(f)(3)). An exchange-eligible employer is a small employer electing to make all of its full-time employees eligible for one or more qualified health plans offered in the small group market through an exchange (Act Sec. 1312(f)(2)(A) of the Patient Protection and Affordable Care Act (P.L. 111-148)).

A small employer is an employer who employed an average of at least one, but not more than 50, employees on business days during the preceding plan year and employs at least one employee on the first day of the current plan year. States have the option to treat employers with 51 to 100 employees as small employers (Act Sec. 1304(b)(2) of P.L. 111-148, as amended by Act Sec. 2(a) of the Protecting Affordable Coverage for Employees (PACE) Act (P.L. 114-60)). The small group market is the health insurance market under which employees obtain health insurance coverage through a group health plan maintained by a small employer (Act Sec. 1304(a)(3) of P.L. 111-148). Beginning in 2017, states may expand the definition of an exchange-eligible employer to include large employers in addition to small employers (Act Sec. 1312(f)(2)(B) of P.L. 111-148).

2047. Simple Cafeteria Plans. Certain small employers can establish simple cafeteria plans under which the nondiscrimination requirements applicable to regular cafeteria plans (¶ 2045), as well as the nondiscrimination rules applicable to group-term life insurance (¶ 2055), accident and health plans (¶ 2015), and dependent care assistance programs (¶ 2065), are considered satisfied (Code Sec. 125(j)).[53] A simple cafeteria plan is a cafeteria plan established and maintained by an eligible employer that meets certain contribution, eligibility, and participation requirements.

Eligible Employers. To be eligible to establish a simple cafeteria plan, an employer must have employed an average of 100 or fewer employees on business days during either of the two preceding years. An employer that was not in existence throughout the preceding year may be considered as an eligible employer if it reasonably expects to

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[53] ¶ 7320; COMPEN: 51,250; § 20,840.05

average 100 or fewer employees on business days during the current year. If an employer has 100 or fewer employees for the year and establishes a simple cafeteria plan, then it is treated as an eligible employer for any subsequent year even if the employer employs more than 100 employees in the subsequent year, unless the employer employs an average of 200 or more employees during the subsequent year.

For purposes of determining the qualification of a business that has changed ownership, the fact that the previous owner had 100 or fewer employees in a preceding year is used to determine eligibility of the current ownership to establish a simple cafeteria plan. Also, all persons treated as a single employer for purposes of the work opportunity credit (¶ 1365G) or the deferred compensation rules for leased employees under Code Sec. 414(n) or Code Sec. 414(o) are treated as one person for purposes of simple cafeteria plans.

Contribution Requirements. The contribution requirements of a simple cafeteria plan are met if the employer is required by the plan to make a contribution to provide qualified benefits on behalf of each qualified employee in an amount equal to: (1) a uniform percentage of at least two percent of the employee's compensation for the year; or (2) at least six percent of the employee's compensation for the plan year or twice the amount of the salary reduction contributions of each qualified employee, whichever is less (Code Sec. 125(j)(3)). If the employer bases the satisfaction of the contribution requirements on the second option, it will not be treated as met if the rate of contributions with respect to any salary reduction contribution of a highly compensated (¶ 2114) or key employee (¶ 2132) is greater than that with respect to any other employee.

Employee Eligibility and Participation Requirements. The minimum eligibility and participation requirements of a simple cafeteria plan are met if all employees who had at least 1,000 hours of service for the preceding plan year are eligible to participate. In addition, each employee eligible to participate may elect any benefit under the plan, subject to terms and conditions applicable to all participants (Code Sec. 125(j)(4)). An employer may elect to exclude from the plan, regardless of the satisfaction of the 1,000 hour requirement, employees: (1) who have not attained the age of 21 before the close of the plan year; (2) who have less than one year of service with the employer; (3) who are covered under a collective bargaining agreement; or (4) who are nonresident aliens working outside the United States whose income did not come from a U.S. source.

Other Employee Benefits

2055. Group-Term Life Insurance. An employee may exclude from gross income the cost of the first $50,000 of group-term life insurance on his or her life provided under a policy carried directly or indirectly by the employer (Code Sec. 79(a) and (c); Reg. §§ 1.79-1 and 1.79-3).[54] The cost of coverage in excess of $50,000 is included in the employee's gross income and subject to employment taxes, reduced by any amount the employee paid toward the insurance. The cost in excess of $50,000 is not the employer's actual cost in providing coverage. Instead, the cost is determined under a Uniform Premium Table (see below) which provides a per-month premium cost for $1,000 of insurance based on the employee's age as of the end of the employee's tax year. The $50,000 limit relates to the group-term life insurance coverage which the employee receives during any part of the tax year.

In the case of a disabled or retired employee, the full cost of employer-provided group-term life insurance coverage is excluded from the employee's income (Code Sec. 79(b) and (d); Reg. § 1.79-2; Temp. Reg. § 1.79-4T).[55] A full exclusion is also available if the employer or a charity is the beneficiary of the insurance benefits. On the other hand, a key employee (¶ 2132) must include the cost of all benefits he or she receives under a plan that does not satisfy nondiscrimination requirements. In addition, coverage on the life of the employee's spouse or dependents is not excluded unless it qualifies as a *de minimis* fringe benefit (¶ 2089).

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[54] ¶ 6360, ¶ 6362, ¶ 6364; COMPEN: 48,100; § 21,005.05

[55] ¶ 6360, ¶ 6363, ¶ 6366; COMPEN: 48,100; § 21,005.05

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Group-term life insurance is insurance that provides for a general death benefit that is excluded from gross income (¶ 803) and provided to a group of at least 10 full-time employees at some time during the year (Reg. § 1.79-1; IRS Pub. 15-B). An employee includes any current common-law employee, former employee, or leased employee, as well as a statutory employee who is a full-time salesperson. An employee does not include a self-employed person, partner, or two-percent or more S corporation shareholder. The amount of insurance provided to each employee must be computed under a formula that precludes individual selection. In addition, the policy must not provide any permanent benefits.

Table 1

Cost Per $1,000 of Protection for One-Month Period

Age	*Cost*
Under 25	5 cents
25 through 29	6 cents
30 through 34	8 cents
35 through 39	9 cents
40 through 44	10 cents
45 through 49	15 cents
50 through 54	23 cents
55 through 59	43 cents
60 through 64	66 cents
65 through 69	$1.27
70 and above	$2.06

Example: X Corp. pays the premiums on a $70,000 group-term insurance policy on the life of its president, Fox, who is 51 years old at the end of 2017. The IRS-established uniform cost for $1,000 of group-term coverage for twelve months is $2.76 ($0.23 × 12) (Reg. § 1.79-3(d)(2)). The cost of the policy includible in Fox's gross income is computed as follows:

Total insurance coverage	$70,000.00
Tax-free insurance	50,000.00
Insurance coverage subject to tax	$20,000.00
Taxable cost of policy includible in Fox's gross income ($2.76 × 20)	$55.20

2057. Split-Dollar Life Insurance. A split-dollar life insurance arrangement is an arrangement where the premiums, cash-surrender value, or death benefits are split between an owner and non-owner of a life insurance policy (Reg. § 1.61-22).[56] Ownership and benefits are most often split between an employer and an employee, but they may also be split between a corporation and shareholder, or between family members. A split-dollar arrangement entered into, or materially modified after, September 17, 2003, is taxed under either the economic benefit rule or the loan rule depending upon which party owns the contract, and the relationship of the owner to the non-owner.

Owner of the Contract. The owner of a contract is generally the person named as the policy owner (Reg. § 1.61-22(c)). If two or more persons are named as policy owners and each has an undivided interest in every right and benefit, those persons are treated as owners of separate contracts. However, an employer is treated as the owner of the policy if the only benefit available under the arrangement is the value of the current life insurance protection (i.e., non-equity arrangement).

Economic Benefit Rule. Under the economic benefit rule, the owner of the life insurance contract is treated as transferring economic benefits to the non-owner (Reg. § 1.61-22(d)). Depending on the relationship between the parties, the economic benefits may constitute compensation, a distribution under Code Sec. 301, a gift, or another type

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

56 ¶ 5906E; COMPEN: 48,150; § 21,010.05

of income. Both the owner and non-owner must account for the economic benefits fully and consistently, reduced by any consideration paid by the non-owner for the economic benefits. The economic benefit rule generally applies to compensatory arrangements in which the employer is the owner of the contract—for example, endorsement split-dollar arrangements, in which the employer is formally designated as the owner of the insurance contract and endorses the contract to specify the portion of the insurance proceeds payable to the employee's beneficiary (Reg. § 1.61-22(b)(3)(ii)). The value of the benefit provided under such an arrangement is the cost of any current life insurance protection provided to the employee (Reg. § 1.61-22(d)).

Loan Rule. Under the loan rule, the non-owner is treated as lending premium payments to the owner (Reg. § 1.7872-15). The rule generally applies to collateral assignments in which the employee is designated as the owner of the contract and the employer pays all or a portion of the premiums, the payment is a loan under general principals of federal tax law, and repayment is secured by the insurance policy's death benefits or cash surrender value. If a split-dollar loan does not provide for sufficient interest, the loan is a below-market split-dollar loan and is subject to the below market interest rules (¶ 795).

Deferred Compensation. Because certain types of split-dollar life insurance arrangements provide for deferred compensation, the requirements of Code Sec. 409A may apply (¶ 2197).

Pre-September 18, 2003, Arrangements. For a split-dollar arrangement entered into on or before September 17, 2003, or not materially modified thereafter, an employee is taxed on the value of economic benefits received. The economic benefit primarily consists of the value of the protection the employee receives over the premiums the employee pays. Certain other benefits might also be taxed, such as policy dividends received by the employee. The value of the economic benefit is determined using the P.S. 58 rate table contained in Rev. Rul. 55-747, the insurance company's lower published term rates, or the Table 2001 group-term rates (¶ 2055) (Notice 2002-8).[57]

2059. Employer-Provided Vehicle. An employee who uses an employer-provided vehicle for more than *de minimis* personal use receives a taxable fringe benefit from his or her employer (Reg. § 1.61-21(a)).[58] The fair market value (FMV) of the fringe benefit is included in the employee's wages for income and employment tax purposes, and may be deducted by the employer as compensation. The FMV is generally the cost to the employee of leasing a comparable car at a comparable price for a similar period in an arms-length transaction (Reg. § 1.61-21(b)(4)). Under certain conditions, however, the employer may elect to use one of the following special valuation rules: automobile lease valuation, cents-per-mile valuation, or commuting valuation (Reg. § 1.61-21(c)). Separate rules are used for valuing flights by an employee on employer-provided noncommercial aircraft.

Automobile Lease Valuation. The value of the personal use of an employer-provided car may be computed under annual lease value tables (Reg. § 1.61-21(d)).[59] The annual lease value of an automobile is computed by first determining the FMV of the automobile on the first date it was made available to any employee for personal use. Under a safe-harbor, the employer's cost can be substituted for FMV, provided certain conditions are met. FMV is reduced when an employee contributes an amount toward the purchase or lease of the automobile. In addition, if the automobile is part of a fleet of at least 20, then the FMV of each automobile can be treated as equal to the fleet-average value. The maximum fleet-average value for employer-provided vehicles first made available for personal use by employees in calendar year 2017 is $21,100 for passenger automobiles and $23,300 for a truck or van (Notice 2017-3).

Once the FMV is established, the annual lease value table prepared by the IRS and reproduced below, is used to determine the annual lease value that corresponds to the FMV. The annual lease values include the FMV of maintenance and insurance for the automobile but do not include the cost of gasoline provided by the employer. The fuel provided can be valued either at its FMV or at 5.5 cents per mile for all miles driven

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References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

57 ¶ 5508.24; COMPEN: 48,150; § 21,005.20

58 ¶ 5906; COMPEN: 33,150; § 8,035

59 ¶ 5906; COMPEN: 33,152; § 8,055.10

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within the United States, Canada, or Mexico by the employee. If continuous personal use of a company car is for less than a year, but at least 30 days, the employee may prorate the car's annual lease value. The values in the table are based on an assumed four-year lease term.

Automobile fair market value (1)	*Annual Lease Value (2)*
$ 0 to 999	$600
1,000 to 1,999	850
2,000 to 2,999	1,100
3,000 to 3,999	1,350
4,000 to 4,999	1,600
5,000 to 5,999	1,850
6,000 to 6,999	2,100
7,000 to 7,999	2,350
8,000 to 8,999	2,600
9,000 to 9,999	2,850
10,000 to 10,999	3,100
11,000 to 11,999	3,350
12,000 to 12,999	3,600
13,000 to 13,999	3,850
14,000 to 14,999	4,100
15,000 to 15,999	4,350
16,000 to 16,999	4,600
17,000 to 17,999	4,850
18,000 to 18,999	5,100
19,000 to 19,999	5,350
20,000 to 20,999	5,600
21,000 to 21,999	5,850
22,000 to 22,999	6,100
23,000 to 23,999	6,350
24,000 to 24,999	6,600
25,000 to 25,999	6,850
26,000 to 27,999	7,250
28,000 to 29,999	7,750
30,000 to 31,999	8,250
32,000 to 33,999	8,750
34,000 to 35,999	9,250
36,000 to 37,999	9,750
38,000 to 39,999	10,250
40,000 to 41,999	10,750
42,000 to 43,999	11,250
44,000 to 45,999	11,750
46,000 to 47,999	12,250
48,000 to 49,999	12,750
50,000 to 51,999	13,250
52,000 to 53,999	13,750
54,000 to 55,999	14,250
56,000 to 57,999	14,750
58,000 to 59,999	15,250

For vehicles having a fair market value in excess of $59,999, the Annual Lease Value is equal to: (0.25 × the fair market value of the automobile) + $500.

Cents-Per-Mile Valuation. The value of the personal use of an employer-provided vehicle may be determined by multiplying personal use mileage, provided it is at least 10,000 miles, by the standard mileage rate (53.5 cents per mile in 2017) if certain requirements are satisfied (Reg. § 1.61-21(e); Rev. Proc. 2010-51; Notice 2016-79).[60] For a passenger automobile first made available to an employee in calendar year 2017, the FMV of the vehicle cannot exceed $15,900, and for a truck or van, the FMV cannot exceed $17,800 (Notice 2017-3). Fuel provided by the employer must be valued separately, at either its FMV or at 5.5 cents per mile for miles driven in North America (Reg. § 1.61-21(d)(3)(ii)(B)).

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[60] ¶ 5906; COMPEN: 33,154; § 8,055.15

Commuting Valuation. If certain requirements are met, the use of an employer-provided commuting vehicle is valued at $1.50 each way (i.e., to and from work), per employee (Reg. § 1.61-21(f)).[61] Even if two or more employees commute in the vehicle such as a car pool, each employee includes $1.50 each way in income. To qualify, personal use of the vehicle must be ***de minimis*** and the employer must require the employee or employees to commute to and/or from work in the vehicle for bona fide noncompensatory business reasons.

Employer-Provided Transportation Due to Unsafe Conditions. If it is unsafe for an employee, who would normally do so, to walk or use public transportation to get to work and certain other requirements are met, the employee includes only $1.50 per one-way commute ($3.00 per round trip commute) in income with respect to cab fare or an employer-provided vehicle (Reg. § 1.61-21(k)).[62]

Chauffeur Services. The FMV of chauffeur services is determined separately from the value of the availability of an employer-provided automobile (Reg. § 1.61-21(b)(5)). The services of a chauffeur may generally be valued by reference to either (1) the FMV of these services as determined in an arm's-length transaction, or (2) the compensation of the chauffeur.

Noncommercial Aircraft Flights. The value of personal flights, domestic or international, on employer-provided noncommercial aircraft is determined under the base aircraft valuation formula by multiplying the Standard Industry Fare Level (SIFL) flight mileage for the applicable period by an aircraft multiple based on weight, and adding a terminal charge (Reg. § 1.61-21(g); Rev. Rul. 2017-19; Rev. Rul. 2017-10).[63] For flights taken during the period from January 1, 2017, through June 30, 2017, the terminal charge is $38.85, and the SIFL rates are: $.2125 per mile for the first 500 miles, $.1620 per mile 501 through 1,500 miles, and $.1558 per mile over 1,500 miles. For flights taken during the period from July 1, 2017, through December 31, 2017, the terminal charge is $40.63, and the SIFL rates are: $.2222 per mile for the first 500 miles, $.1694 per mile 501 through 1,500 miles, and $.1629 per mile over 1,500 miles.

If a trip made primarily for business purposes includes business and personal flights, the excess of the value of all the actual flights over the value of the flights that would have been taken if there had been no personal flights is includible in gross income. If the trip is primarily personal, the value of the personal flights that would have been taken if there had been no business flights is includible in gross income. No amount is included in income if the employee takes a personal trip on a noncommercial aircraft and at least one-half of the aircraft's seating capacity is occupied by employees whose flights are primarily business related and excludable from income.

Frequent Flyer Miles. The IRS will not tax the personal use of airline frequent flyer miles or other in-kind promotional benefits attributable to the taxpayer's business or official travel. This relief does not apply to travel or other promotional benefits that are converted to cash, to compensation that is paid in the form of travel or other promotional benefits, or to other circumstances where these benefits are used for tax-avoidance purposes (Announcement 2002-18).[64]

2063. Adoption Assistance Programs. Qualified adoption expenses incurred by a taxpayer for the adoption of an eligible child and paid to a third party or reimbursed to an employee by an employer under a written adoption assistance program are excludable from the employee's gross income (Code Sec. 137).[65] An adoption assistance program is a written plan that: (1) benefits employees who qualify under rules set up by the employer which do not favor highly compensated employees (¶ 2114) or their dependents (¶ 152); (2) does not pay more than five percent of its payments each year to

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[61] ¶ 5906; COMPEN: 33,156; § 8,055.20

[62] ¶ 5906; COMPEN: 33,152.20, COMPEN: 33,156, COMPEN: 33,160; § 21,130.10, § 21,130.15

[63] ¶ 5906, ¶ 5907.50; COMPEN: 33,202; § 21,105.10

[64] ¶ 5907.35; BUSEXP: 24,906.15; § 3,085

[65] ¶ 7600; COMPEN: 36,650; § 4,025

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shareholders or owners of more than five percent of the employer; (3) provides for adequate notice to employees of their eligibility; and (4) requires employees to provide reasonable substantiation of qualified expenses that are to be paid or reimbursed.

The rules for the exclusion generally parallel the rules for the adoption expense credit. Thus, an eligible child and qualified adoption expenses are defined as they are for purposes of the credit (¶ 1307). The aggregate amount of payments that may be excluded from income (for both special needs adoptions and other adoptions) is $13,570 for 2017 ($13,840 for 2018) (Rev. Proc. 2016-55; Rev. Proc. 2017-58). The exclusion is phased out for higher income taxpayers the same as for the adoption credit when modified adjusted gross income is between $203,540 and $243,540 for 2017 ($207,580 and $247,580 for 2018).

2065. Dependent Care Assistance Benefits. An employee may exclude from gross income amounts paid or incurred by an employer for dependent care assistance services provided to the employee under a written plan (Code Sec. 129).[66] The maximum amount excluded cannot exceed $5,000 for the tax year ($2,500 if married filing separately). Any amount exceeding the limit is includible in the employee's gross income for the year in which the services are provided, even if the payment for the services is received in a subsequent year. The exclusion also cannot exceed the employee's earned income if unmarried, or earned income of the lower-earning spouse if married.

Dependent care assistance means the payment for services (or providing services) which if paid by the employee would entitle him or her to claim the child and dependent care credit (¶ 1301). Thus, the expenses must be incurred for household services for care of a child or other dependent to enable the employee to work. A dependent care assistance plan generally must not discriminate in favor of employees who are highly compensated (¶ 2114). If a plan would qualify as a dependent care assistance program except for the fact that it fails to meet discrimination, eligibility, or other requirements, it may still be treated as a dependent care assistance program in the case of employees who are not highly compensated.

The exclusion of dependent care assistance benefits does not apply unless the name, address, and taxpayer identification number (i.e., employer identification number) of the person performing the child or dependent care services are included on the return of the employee benefiting from the exclusion. The exclusion may be claimed even though the information is not provided if it can be shown that the taxpayer exercised due diligence in attempting to provide this information.

2067. Educational Assistance Programs. Up to $5,250 of payments received by an employee for tuition, fees, books, supplies, etc., under an employer's educational assistance program may be excluded from gross income (Code Sec. 127; Reg. §§ 1.127-1 and 1.127-2).[67] This benefit is available for both undergraduate and graduate-level courses. Excludable assistance payments may not cover tools or supplies that the employee retains after completion of the course or the cost of meals, lodging, or transportation. Although the courses covered by the plan need not be job related, an exception applies to courses involving sports, games, or hobbies. These courses may only be covered if they involve the employer's business or are required as part of a degree program.

An educational assistance program is a separate written plan that provides educational assistance only to employees, subject to various limitations. An employee for this purpose includes a current employee, as well as a former employee who retired, left on disability, or was laid off. It also includes a partner who performs services for a partnership and a leased employee who has provided services on a substantially full-time basis for at least a year (Rev. Rul. 96-41). A program that provides benefits to a spouse or dependent of an employee is not a qualified program.

Reports and Records. An employer who maintains an educational assistance plan must maintain records and file an information return for the plan, but the reporting requirement has been suspended indefinitely (Code Sec. 6039D; Notice 2002-24).[68]

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References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[66] ¶ 7380; COMPEN: 36,600; § 20,001

[67] ¶ 7350, ¶ 7351, ¶ 7352; COMPEN: 36,554; § 20,101

[68] ¶ 35,660, ¶ 35,661.50; PENALTY: 3,208.20; § 39,155.25

2069. Employee Achievement Awards Excluded from Gross Income. An employee achievement award is excludable from an employee's gross income to the extent the cost of the award is deductible by the employer ($400 for nonqualified awards or $1,600 for qualified awards) (Code Sec. 74(c); Prop. Reg. § 1.74-2).[69] See ¶ 919 for a discussion of the employer's deduction and the definition of an employee achievement award. If the cost of an award exceeds the dollar limitations, then the employee must include in gross income the greater of excess of the fair market value or the cost to the employer of the award over the dollar limitation, but not in excess of the fair market value of the award. The exclusion is not available for any award made by a sole proprietorship to the sole proprietor.

2071. Vacation Pay. A vacation pay plan is an employer plan that provides compensation to employees for specified periods of vacation, including vacation time that has been earned but not actually taken. Such a plan also generally includes compensation for specified holidays, whether or not those days are actually taken.[70]

Vacation pay plans, like other employee benefit plans, can take a wide variety of forms: the benefits may be vested or unvested; the plan may be funded or unfunded; and the plan may be a single-employer plan or a multiemployer plan. Vacation pay is taxable and is subject to income tax withholding (Code Sec. 61; Reg. § 31.3401(a)-1(b)(3)). It is also subject to FICA and FUTA taxes (Code Secs. 3121(a) and 3306(b)).

Vacation pay is generally deductible by an employer as reasonable compensation for prior services rendered (Code Sec. 162; SeeReg. § 1.162-7). See ¶ 1549 for a discussion of the accrual of vacation and sick leave pay. See ¶ 2073 for a discussion of employer-sponsored leaving programs.

2073. Leave Sharing Programs. An employee who deposits accrued leave in an employer-sponsored leave-sharing program for use by other employees adversely affected by a major disaster does not realize income or wages with respect to the deposited leave, provided the plan treats the amounts paid to the leave recipient as wages subject to income tax withholding and employment taxes (Notice 2006-59).[71] The employee may not claim a charitable contribution, business expense, or loss deduction on account of the deposit of the leave or its use by a leave recipient.

Similarly, if an employee participates in a leave donation program under which he or she may elect to forgo vacation, sick, or personal leave in exchange for employer making cash contributions to charitable organizations, the contributing employee may not claim charitable contribution, business expense, or loss deduction for the contributed leave. However, the IRS will not assert that such cash payments constitute gross income or wages of the employee with respect to donations made to a charitable organization: (1) before January 1, 2019, for relief of victims of Hurricane Harvey, Hurricane Irma, or Hurricane Maria in 2017; (2) before January 1, 2018, for relief of victims of Hurricane Matthew; (3) before January 1, 2018, for relief of victims of severe storms and flooding in Louisiana that began on August 11, 2016; (4) before January 1, 2016, for the relief of victims of the Ebola virus disease outbreak in Guinea, Liberia, and Sierra Leone; and (5) before January 1, 2014, for the relief of victims of Hurricane Sandy (Notice 2017-62; Notice 2017-52; Notice 2017-48; Notice 2016-69; Notice 2016-55; Notice 2014-68; Notice 2012-69).[72]

Amounts deposited in a leave bank to be used by employees experiencing medical emergencies are not taxable to contributing employees but they are included in the gross income of the recipients subject to income tax withholding and employment taxes (Rev. Rul. 90-29). The IRS has not granted favorable tax treatment to other leave-sharing plans.

2075. Severance Pay. A severance pay plan is a plan that provides payments to employees upon termination of employment. Depending upon the facts and circum-

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[69] ¶ 6200, ¶ 6203; INDIV: 33,154; § 3,060.15

[70] ¶ 5507.47; COMPEN: 12,212; § 22,110.10

[71] ¶ 11,620.522; COMPEN: 6054; § 3,005.25, § 22,110.10

[72] ¶ 11,620.1005; INDIV: 27,208; § 22,110.10

stances, severance pay arrangements can qualify as a welfare benefit plan (¶ 2011) or retirement plan (¶ 2111), or may be exempt from certain federal requirements. Generally, the payments are proportionate to length of employment.[73] The plan may be a permanent program or a limited program—e.g., an "open-window" program that offers a group of employees cash payments, increased pension benefits, or both as inducements to voluntarily retire or to separate from employment within a certain time period. The plan may cover voluntary separations, involuntary separations, or both, and may place conditions on payment of benefits—e.g., no benefits are provided if the employee goes to work for a competitor or for a successor employer. In addition, the plan may deny benefits if the employee is terminated for cause.

Golden Parachutes. In a golden parachute agreement, a corporate employer states that it will pay a key employee (¶ 2132) or a number of key employees an amount over and above other compensation in the event of a change in ownership or control of the corporation or a substantial portion of the corporation's assets (¶ 907). The tax consequences applicable to golden parachute payments are triggered merely by the payment of the requisite amount of compensation, and a termination of employment is not literally required. As a practical matter, however, golden parachute payment provisions in an employment agreement or employer's benefits plan usually are designed to be triggered upon loss of employment within a designated period of time following the acquisition of the employer.

2077. Domestic Partner Benefits. Employers may offer benefits to an employee's domestic partner, including health care insurance (medical, dental, vision), access to an employee assistance plan, and dependent life insurance. Employers often require a written affidavit affirming the relationship and may require various documentation, such as joint mortgage or lease, proof of registration under a local ordinance, drivers' license, tax returns, bank statements, or joint credit statements.

A marriage of two individuals is recognized for federal tax purposes if the marriage would be recognized by the state, possession, or territory of the United States in which the marriage was entered into, regardless of where the individuals are domiciled (¶ 152). However, a marriage for federal tax purposes does not include registered domestic partnerships, civil unions, or other similar relationships recognized under state law that are not denominated as a marriage under that state's law (Reg. § 301.7701-18).[74] Thus, while employer-provided health benefits are tax free for spouses (including same-sex spouses) and dependents of an employee (¶ 2015), the cost of providing the benefit to a domestic partner who is not legally married to the employee or cannot be claimed as the employee's dependent (¶ 137) is included in the employee's gross income. Additionally, if a domestic partner is not the employee's spouse or dependent, contributions for a partner's coverage must be on an after-tax basis, and the domestic partner is not eligible for reimbursement from health care FSAs.

Specific guidance has been provided for employers and employees to make claims for refunds or adjustments of overpayments of employment taxes and income tax withholding for benefits provided to same-sex spouses (Notice 2013-61).[75]

Fringe Benefits Under Code Sec. 132

2085. Fringe Benefits Under Code Sec. 132. Certain fringe benefits provided by an employer to an employee are excluded from an employee's gross income for income tax purposes, and from wages for purposes of income tax withholding and FICA and FUTA taxes (Code Sec. 132).[76] These include: no-additional-cost services (¶ 2087), qualified employee discounts (¶ 2088), *de minimis* fringe benefits (¶ 2089), working condition fringe benefits (¶ 2090), qualified transportation fringe benefits (¶ 2091), qualified moving expense reimbursements (¶ 2092), qualified retirement planning services (¶ 2093), on-premises athletic facilities (¶ 2094), and qualified military base realignment and closure fringe benefits (¶ 2095). Employers providing fringe benefits must meet certain nondiscrimination requirements in order for such benefits to apply to favored groups.

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[73] ¶ 5507.297; COMPEN: 27,202; § 9,345

[74] ¶ 43,166; FILEIND: 3,202; § 45,901

[75] ¶ 38,519.395, ¶ 38,770.13; PAYROLL: 9,352; § 22,235.25

[76] ¶ 7420; COMPEN: 36,000; § 21,101

Any fringe benefit that does not qualify for exclusion under Code Sec. 132, or any other Code provision, is includible in the recipient's gross income and wages at the excess of its fair market value over any amount paid by the employee for the benefit (unless excluded under another specific statutory provision) (¶ 713). Employers are generally allowed a trade or business expense deduction for the value, or a portion of the value, of the fringe benefit provided to employees (¶ 906).

For purposes of no-additional-cost services, qualified employee discounts, and on-premise athletic facilities, the exclusion under Code Sec. 132 applies to benefits provided to: (1) employees, their spouses, and dependent children; (2) former employees who separated from service because of retirement or disability, as well as their spouses and dependent children; (3) the widow or widower of a deceased employee; and (4) the dependent children of deceased employees (Code Sec. 132(h); Reg. § 1.132-1(b)).[77] For purposes of working condition fringe benefits, the exclusion applies to benefits provided to employees, independent contractors, directors, and partners who perform services for a partnership.

2087. No-Additional-Cost Services. No-additional-cost services provided by an employer to employees are excluded from gross income and wages as a fringe benefit (¶ 2085) (Code Sec. 132(b); Reg. § 1.132-2).[78] No-additional-cost services are free services provided to all employees by an employer where the employer incurs no substantial additional cost in providing the service, and the service is normally offered to the employer's customers in the line of business, such as free travel on a standby basis for airline employees. The exclusion is available only if the service is available to employees on a nondiscriminatory basis.

2088. Qualified Employee Discounts. Discounts provided to employees on their purchase of qualified property or services of their employer are excluded from gross income and wages as a fringe benefit (¶ 2085) (Code Sec. 132(c); Reg. § 1.132-3).[79] Qualified employee discounts are discounts provided to all employees on the selling price of certain property or services in the ordinary line of business. In the case of merchandise, the discount cannot exceed the gross profit percentage of the price at which the property is offered to customers. For services, the discount cannot exceed 20 percent of the price at which the service is offered to customers. In order to be excluded, the discounts must be available to employees on a nondiscriminatory basis. Moreover, employees do not receive income if they pay at least fair market value for damaged, distressed, or returned property.

2089. *De Minimis* Fringe Benefits. If the value of any property or service provided to an employee is so minimal that accounting for the property or service would be unreasonable or administratively impracticable for an employer, it is a *de minimis* fringe benefit that is excluded from the employee's gross income and wages (¶ 2085) (Code Sec. 132(e); Reg. § 1.132-6).[80] Examples include limited use of copy machines, occasional parties or picnics, meal money or transit fare due to overtime work, holiday gifts with a small market value, tickets occasionally provided for entertainment events, and employer-furnished coffee and doughnuts. In determining whether the *de minimis* exclusion applies, the frequency with which similar fringe benefits are provided by an employer to its employees is taken into account. A subsidized eating facility operated by an employer for the benefit of employees is treated as a *de minimis* fringe benefit if the eating facility is located on or near the employer's business premises, and the revenue derived from such facility normally equals or exceeds the direct operating costs of such facility (Reg. § 1.132-7).

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[77] ¶ 7420, ¶ 7422; COMPEN: 33,050; § 21,101

[78] ¶ 7420, ¶ 7423; COMPEN: 36,050; § 21,105.05

[79] ¶ 7420, ¶ 7424; COMPEN: 36,100; § 21,110.05

[80] ¶ 7420, ¶ 7427; COMPEN: 36,300; § 21,120.05

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Meals and Lodging. Meals are excluded from an employee's gross income and wages as a *de minimis* fringe benefit if furnished on the business premises of the employer for the convenience of the employer (Code Sec. 119; Reg. § 1.119-1).[81] Lodging is also excluded from an employee's gross income and wages if furnished for the convenience of the employer on the business premises of the employer, and as a condition of employment.

Meals are regarded as furnished for the convenience of the employer if they are furnished for a substantial noncompensatory business reason of the employer (even if the meals also serve a compensatory purpose). If more than one-half of the employees who are furnished meals by the employer are furnished meals for the convenience of the employer, then all meals furnished on the premises of the employer are considered to be for the convenience of the employer. Therefore, the meals are fully deductible by the employer, instead of possibly being subject to the 50-percent limit on business meal deductions, and excludable by the employees (¶ 916). The business premises of the employer for this purpose generally means the place of employment of the employee. It can include a camp located in a foreign country if an employee is furnished lodging (¶ 2406).

Faculty Housing. The value of campus lodging furnished to employees by educational or medical research institutions is excludable from the employee's gross income and wages if an adequate rental is charged. A rental is considered *inadequate* and thus the exclusion will not apply to the extent of the excess of: (1) the lesser of (a) five percent of the appraised value of the lodging or (b) an amount equal to the average of the rentals paid by nonemployees or nonstudents during the year for comparable lodging provided by the institution; over (2) the rent paid by the employee for the calendar year (Code Sec. 119(d)).[82] The appraised value of lodging will be determined as of the close of the calendar year in which the tax year begins or, in the case of a rental period not greater than one year, at any time during the calendar year in which such period begins.

2090. Working Condition Fringe Benefits. Working condition fringe benefits provided to an employee may be excluded from gross income and wages as a fringe benefit (¶ 2085) provided the cost of the property or service would have been deductible by the employee as a business expense or depreciation had the employee paid for it on his or her own (Code Sec. 132(d); Reg. § 1.132-5).[83] The general nondiscrimination rules applicable to fringe benefits do not apply to working condition fringes; therefore, they can be provided exclusively, or on more favorable terms, to executives. Examples of working condition fringes include use of a company vehicle, airplane transportation, travel expenses including meals and lodging, allowances for business use of cell phones, computers, internet service, entertainment, and club dues. Denial of a deduction to an employer for its payment of travel expenses of a spouse, dependent, or other individual accompanying an employee on business travel does not preclude those items from qualifying as working condition fringe benefits.

Employer-Provided Cell Phones. An employer-provided cell phone and similar equipment provided to an employee for noncompensatory business purposes is excluded from an employee's gross income and wages as a working condition fringe benefit (Notice 2011-72).[84] In addition, the business substantiation requirements for the working condition fringe exclusion are automatically satisfied for a employer-provided cell-phone. A noncompensatory business purpose is any substantial reason relating to the employer's business, other than providing compensation, such as the employer's need to contact employees during work-related emergencies, or the employer's requirement that the employee be available to speak with clients away from the office or outside normal workday hours. Personal use of an employer-provided cell-phone, provided primarily for noncompensatory business purposes, is excluded from an employee's gross income and

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[81] ¶ 7220, ¶ 7221; COMPEN: 36,500; § 21,205, § 21,210

[82] ¶ 7220; COMPEN: 36,508; § 21,230

[83] ¶ 7420, ¶ 7426; COMPEN: 36,250; § 21,115.05

[84] ¶ 7438.80; COMPEN: 36,258; § 21,115.22

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wages as a *de minimis* fringe benefit (¶ 2089). Employers that require employees to use their personal cell phones primarily for noncompensatory business reasons may treat reimbursements of the employees' reasonable expenses as nontaxable. This does not mean, however, that cell phones used for primarily personal reasons are exempt from tax or from the substantiation requirements.

Employer-Provided Vehicles. The value of an employee's *business use* of an employer-provided automobile is excludable from the employee's gross income and wages as a working condition fringe benefit. The value of employee's *personal use* of an employer-provided automobile is generally included in the employee's income and wages (¶ 2059). The employer, however, may elect not to withhold income tax on the value of the employee's personal use (Code Sec. 3402(s)).[85] The employer must notify the employee of the election, and must include the value of the benefit on a timely filed Form W-2. An employer who elects not to withhold income tax for an employer-provided automobile is still required to withhold FICA taxes.

2091. Qualified Transportation Fringe Benefits. Commuting expenses to and from a place of business and home are generally not deductible. However, qualified transportation fringe benefits provided by an employer to an employee may be excluded from the employee's gross income and wages as a fringe benefit (¶ 2085) (Code Sec. 132(f)); Reg. § 1.132-9).[86] A qualified transportation fringe benefit includes employer-provided transit passes, qualified parking, van pooling, and qualified bicycle commuting reimbursement.

For 2017, the maximum that may be excluded for qualified parking, transit passes, and van pooling is $255 per month (Rev. Proc. 2016-55). For 2018, the maximum that may be excluded for qualified parking, transit passes, and van pooling is $260 per month (Rev. Proc. 2017-58). The exclusion for qualified bicycle commuting reimbursement is limited to a per employee limitation of $20 per month, multiplied by the number of qualified bicycle commuting months during the calendar year.

An employer may simultaneously provide an employee with a transit pass, qualified parking, and van pooling. However, an employee may not receive a bicycle commuting expense reimbursement for any month in which he or she receives any other qualified transportation fringe benefit. An employer who provides any qualified transportation fringe benefits to its employees may offer them a choice between cash and one or more qualified transportation benefits without causing the employees to lose the exclusion from income for noncash transportation fringe benefits. The amount of cash offered is includible in the employee's income only to the extent that the employee chooses the cash option.

Qualified parking for this purpose is parking provided on or near the business premises of the employer, or on or near a location from which the employee commutes to work by mass transit, in a commuter highway vehicle, or by car pool. It does not include parking on or near property used by the employee for residential purposes. Van pooling is transportation in a qualifying commuter highway vehicle if that transportation is in connection with travel between the employee's residence and the place of employment. A qualifying commuter vehicle must seat at least six adults (excluding the driver) and at least 80 percent of its mileage use must be reasonably expected to be for employees' commuting purposes and for trips when the vehicle is at least one-half full (excluding the driver).

2092. Qualified Moving Expenses Reimbursements. An employee may exclude any qualified moving expenses reimbursement from gross income and wages as a fringe benefit (¶ 2085) (Code Sec. 132(g)).[87] A qualified moving expense reimbursement includes any amount received, directly or indirectly, by the employee from the employer as payment or reimbursement of expenses that would be deductible as moving expenses if directly paid or incurred by the employee (¶ 1073). It does not include a payment for, or a reimbursement of, an expense actually deducted by the employee in a prior tax

References are to Standard Federal Tax Reports; Tax Research Consultant; and Practical Tax Explanations.

[85] ¶ 33,542; COMPEN: 33,350; § 22,110.10

[86] ¶ 7420, ¶ 7429B; COMPEN: 36,350; § 21,125.05

[87] ¶ 7420; COMPEN: 33,116; § 21,135