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IRS Rules for Deducting Your Business Gym

If you have been thinking about the fitness of your employees and the possibility of a gym or other athletic facility, then you need to know the tax rules. To be tax deductible, your gym or other athletic facility must be primarily for the benefit of your employees—other than employees who are officers, shareholders, or other owners who own a 10 percent or greater interest in the business, or other highly compensated employees.

For the 10 percent ownership test, the law treats an employee as owning any interest owned by a member of his or her family. Family includes brothers and sisters, spouses, ancestors (such as parents and grandparents), and lineal descendants (such as children and grandchildren).

The highly compensated group consists of employees who earned more than $120,000 for the preceding year. The gym or other athletic facility must benefit the rank-and-file employee group more than the owner and the highly compensated group. Think of this primary-benefit test as a 51-49 test.

This means that the rank-and-file employee group must use the facility on more days than the owner and highly compensated group does. To see if you pass the 51-49 test, look only at days of use of the facility.

Example. Rank-and-file employees use the gym 235 days during the year and you, the business owner, use it 137 days. The gym passes the 51-49 test; accordingly, it's deductible as an employee recreational facility.

Tax Planning for Snowbirds

You can plan your tax-deductible business life to avoid cold winters and hot summers. Spend a moment examining the following four short paragraphs that contain the basic facts from the *Andrews* case.

For six months of the year, from May through October, Edward Andrews lived in Lynnfield, Massachusetts, where he owned and operated Andrews Gunite Co., Inc., a successful pool construction business. During the other six months, Mr. Andrews lived in Lighthouse Point, Florida, where he owned and operated a sole proprietorship engaged in successful horse racing and breeding operations. In addition, he, his brother, and his son owned a successful Florida-based pool construction corporation from which Mr. Andrews took no salary, but where he did assist with operations.

Instead of renting hotel rooms while in Florida, Mr. Andrews purchased a home, claimed 100 percent business use of the Florida home, and depreciated the house and furniture as business expenses on his Schedule C for his horse racing and breeding business. Mr. Andrews then allocated his other travel expenses and costs of owning and operating this house in Florida on his individual income tax return as

- personal deductions on his Schedule A for a portion of the mortgage interest and taxes,
- business deductions on his Schedule C for the horse racing and breeding business, and

- employee business expenses on IRS Form 2106 for the pool construction business.

(Tax reform under the Tax Cuts and Jobs Act eliminates employee business expense deductions for tax years 2018 through 2025—so Mr. Andrews would replace his old strategy with a corporate reimbursement of employee business expenses strategy.)

Just as Mr. Andrews did, you can tax plan your life to spend your winters in one state and your summers in a different state. In this scenario, your tax-deductible home takes the place of your staying in hotels. The other home is likely your principal residence located near your tax home.

Your travel expenses between the homes are deductible because you do business in both places. You also deduct your meals and other living costs while at the deductible travel destination. You can have separate businesses in each state or a branch business in the second state.

Tax Reform Destroyed State and Local Tax Deductions—Fight Back

Tax reform put the screws to your state and local income tax deductions, capping them at $10,000. Many states disliked that and have been putting together workarounds.

But now the IRS is creating regulations to put the kibosh on your state's creative plans. Unless federal lawmakers change their minds, your federal deductions for state income taxes face that $10,000 ceiling.

But you have planning opportunities to make more of your property taxes deductible by

- creating or enlarging a home office,
- establishing or expanding a rental activity inside your home,
- having your trade or business activity incur the property taxes, or
- capitalizing the property taxes.

If you are being hurt by the $10,000 ceiling and would like to make more of your property taxes deductible, you can do some tax planning and make that happen.

Tax Reform Expands Your Section 179 Deduction Privilege

The new and improved Section 179 deduction gives you more ways to take advantage of immediate tax deductions. It's somewhat like having a flexible tax shelter in your back pocket for when you need it (and also need the property, of course).

As in years past, the Section 179 deduction is available for both new and used assets and offers you deduction flexibility, unlike bonus depreciation. Now, thanks to the Tax Cuts and Jobs Act, you have up to $1 million in Section 179 deduction availability. You also have new Section 179 qualifying asset possibilities such as

- depreciable tangible personal property used predominantly to furnish lodging;
- non-residential qualified real property; and
- non-residential roofs; heating, ventilation, and air-conditioning property; fire protection and alarm systems; and security systems.

The big advantage to Section 179 deductions over bonus depreciation is flexibility. But bonus depreciation has its place as a tax strategy.

Reduce Your Taxes by Making Your Spouse a Business Partner

Tax reform changed the rules of the game when choosing your best tax structure. In looking over the possibilities, a properly structured spousal partnership could be your best choice.

Here are the tax benefits to you:

- Your spouse's income is free from self-employment tax.
- You and your spouse both still qualify for the new pass-through income deduction under Section 199A.

- The IRS audits partnerships at a much lower rate than proprietorships (Schedule Cs).
- You don't have to worry about the costs or hassle of running payroll or determining your reasonable compensation as you would if you operated the business as an S corporation.

Here are the potential issues:

- The passive activity rules limit your spouse's use of any losses against regular income.
- You have the cost of preparing a partnership return (but you'd have this cost with an S corporation too).

If you would like to discuss how your choice of business entity works in today's tax environment, please don't hesitate to contact us.

Sincerely,

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