Supplement to J.K. Lasser's Small Business Taxes 2019

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The tax law is not static. Since the publication of this book, the IRS has provided guidance on some of the changes for 2018 returns that were made by the Tax Cuts and Jobs Act of 2017 (TCJA). And there's been additional legislation, court cases, and other IRS pronouncements that affect 2018 returns as well as planning for taxes in 2019.

For small business owners, it is important to take action based on what is known now, and to watch for any tax changes that may affect your business and personal taxes in the future. Pay attention to what is new and when it goes into effect. **At the time this Supplement posted, Congress had not yet addressed the tax rules that expired at the end of 2017. This Supplement notes those measures that could still be extended retroactively for 2018 and perhaps for 2019 as well.**

The changes presented in this Supplement are tied to the chapters in the book.

Introduction

Examples of tax definitions of small business. Some of the definitions in Table I.1 have changed for 2019 (not for 2018 returns) due to cost-of-living adjustments:

- Accrual method exception for small businesses: $26 million gross receipts test
- First-year expensing election: Qualified property of no more than $3.57 million
- Interest expense deduction limitation: $26 million gross receipts test.

Forms and schedules. When this edition was published, final versions of forms were not yet available. Find final versions of forms and schedules here.

Chapter 1—Business Organization

Eligibility to make an S election. There have been legislative proposals to change the 100-shareholder limit for purposes of equity crowdfunding. To date, nothing has been enacted.

Revoking an S election. If a calendar-year S corporation wants to become a C corporation for all of 2019 to take advantage of the flat 21% tax rate and other opportunities only for C corporations, it can revoke its S election by filing a statement with the IRS by March 15, 2019 (required information can be found here. A revocation effective on any other date (e.g., made after March 15, 2019) is effective on the date the revocation is filed. A new S election generally cannot be made for 5 years.

If the revocation of the S election means that the corporation must change from the cash method to the accrual method of accounting, a special rule means the change must be taken into account over 6 years. This rule applies to a corporation that had an S election in effect on December 21, 2017, have the same owners of stock in identical proportions on December 22, 2017, and on the date of revocation, and revoke the election after December 21, 2017, and before December 22, 2019. It is essential to review your entity choice with a CPA or other tax advisor to be sure that it works best with all of new law changes.

Chapter 4—Income or Loss from Business Operations

Income from farming. The IRS has extended the livestock replacement period for certain drought-affected areas. Counties for 2018 can be found in Notice 2018-79.

S corporation basis. The AICPA suggestion to the IRS to create a tax form for tracking a shareholder's basis in stock and debt has not yet been acted upon.

Income earned abroad. The time requirement for the foreign earned income exclusion is waived for certain countries. The list of countries for 2018 has not yet been released.

Chapter 5—Capital Gains and Losses

Taxable income breakpoints for capital gain rates in 2019. The following table (Table 5.1) shows the break points for capital gain rates for 2019.

Rate	**Married filing jointly**	**Head of household**	**Single**	**Married filing separately**
0%	Up to $78,750	Up to $52,750	Up to $39,375	Up to $39,375
15%	$78,750 - $488,850	$52,750 - $461,700	$39,375 - $434,550	$39,375 - $244,425
20%	Over $488,850	Over $461,700	Over $434,550	Over $244,425

Opportunity zone investments. The IRS has provided guidance in the form of proposed regulations for investment groups to set up qualified opportunity zone funds (QOFs). Look for funds to be launched in 2019.

The deferral election can be made by a partnership or S corporation or its owners. So, for example, if a partnership realizes a gain, the partnership can make an QOZ election; gain would not be included in the partners' distributive share. And there is no monetary limit on the amount of gain that can be deferred. Similar rules apply for S corporations.

Chapter 7—Employee Compensation

Stock options and restricted stock. Privately-held corporations can enable employees to defer the income resulting from the acquisition of stock pursuant to stock options or restricted stock units (RSUs). This is possible only if you make "qualified equity grants" which are explained by the IRS in Notice 2018-97. You must provide an escrow arrangement to hold the shares until the proper amount of income tax is withheld from the employees at the end of the deferral period.

Employees who wish to defer income recognition must make an election within 30 days that the stock becomes substantially vested or transferrable, whichever is earlier. The sample Sec. 83(b) election form on page 165 can be used for this purpose.

Adoption assistance. For planning purposes, the dollar limit on the exclusion for employer assistance for adoption costs in $14,080 for 2019 (up from $13,810 in 2018).

Flexible spending accounts for medical expenses. For planning purposes, the maximum elective deferral to medical FSAs in 2019 is $2,700, which is $50 more than in 2018.

Employee use of company car. For planning purposes, in valuing employee use of a company car in 2019, the IRS standard mileage rate is 58¢ per mile, up from 54.5¢ per mile in 2018.

The fixed and variable rate allowance (FAVR) in 2019 is limited to $50,400 for cars, trucks, and vans. The rate in 2018 was $27,300 for cars and $31,000 for trucks and vans.

Car and truck values taken into account by employers using the cents-per-mile valuation rule or the fleet valuation rule for valuing personal use of a company vehicle in 2018 is $50,000. The value for 2019 for these vehicles has not yet been announced by the IRS.

Qualified transportation fringe benefits. Employers cannot deduct these fringe benefits, but if they choose to provide them or they permit employees to pay for these costs on a pre-tax basis, employees can exclude up to $265 for free parking, transit passes, and van pooling for 2019 (up from $260 in 2018). Since employers cannot deduct these fringe benefits, they may be barred from deducting rent payments related to free parking (see information below for Chapter 12).

Frequent flyer miles. To date, the IRS has not taken any action to tax frequent flyer miles.

Employment-related tax credits. As of February 1, 2019, the following tax credits, which expired at the end of 2017, have not yet been extended for 2018 (although there is still a possibility that they will be extended retroactively for 2018 and perhaps for 2019):

- Empowerment zone employment credit
- Indian employment credit

The following employment-related tax credits are scheduled to expire at the end of 2019 unless Congress extends them:

- Family and medical leave credit
- Work opportunity credit

Family and medical leave credit. The tax form for claiming the credit for paid family and medical leave is Form 8994, Employer Credit for Paid Family and Medical Leave.

Chapter 8—Travel, Meals, and Gift Expenses

Business travel per diem rates. The maximum federal per diem rate for travel starting October 1, 2018, through September 30, 2019, covering lodging and meals and incidental expenses (M&IE) within the continental United States (CONUS) in most locations is $149 per day ($94 for lodging and $55 for M&IE). These rates are higher than the prior 12-month period when the rate was $144 per day ($93 for lodging and $51 for M&IE). The per diem rates for travel to certain areas have been increased. These rates can be found here.

The high-low substantiation rates for areas within CONUS for the period October 1, 2018, through September 30, 2019, are $287 for travel to high-cost localities and $195 for travel to all other areas within CONUS. Of these rates, the meal portion is $71 for high-cost areas and $60 for all other areas within CONUS. The list of high-cost areas has been changed (see Notice 2018-77 for details).

Chapter 9—Car Expenses

Section 179 deduction and bonus depreciation. For 2019, the first-year expense (Section 179 deduction) applies to equipment purchases (e.g., new vehicles) up to $1.02 million. However, this dollar limit phases out dollar for dollar when purchases for the year exceed $2.55 million. Thus, no expensing deduction can be claimed if equipment purchases for the year are $3.57 million or more.

Heavy SUVs are not subject to the dollar limits, but the first-year expense deduction is limited to $25,500 in 2019 ($500 more than for 2018).

The IRS has not yet addressed the problem of how claiming 100% bonus depreciation for vehicles placed in service in 2018 or 2019 affects deductions after the first year. This is expected to be addressed in a technical corrections bill when Congress gets around to it.

Standard mileage rate. The IRS announced the standard mileage rate, used in lieu of deducting the actual costs of business driving; for 2018 it is 58¢ per mile (up from 54.5¢ per mile in 2018).

Those who own their vehicles and use the standard mileage rate for 2019 must reduce the vehicle's basis by 26¢ per mile (up from 25¢ per mile in 2018).

2-wheel vehicles. The tax credit for 2-wheel plug-in electric drive vehicles expired at the end of 2017; it has not yet been extended for 2018.

Chapter 10—Repairs, Maintenance, and Energy Improvements

Certain tax breaks that expired at the end of 2017; they have not yet been extended for 2018:

- ***Deduction for energy-efficient commercial buildings.*** The $1.80 per square foot deduction for commercial buildings that achieve at 50% energy-saving target.
- ***Alternative fuel vehicle refueling property credit.***

Chapter 12—Rents

If, as part of your rent, you pay for employee parking spots, you cannot deduct the portion of your monthly payments allocable to this expense. The IRS allows you to use any reasonable method to figure the disallowed amount. Costs related to providing parking for the general public are deductible (even if employees use them). The IRS has a 4-step process for determining the disallowed amount for employee parking and if you use it, then it is considered to be reasonable. The steps vary depending on whether or not the spots are reserved for employees.

- Step 1: Calculate the disallowance for reserved employee spots

- Step 2: Determine the primary use of remaining spots (the “primary use test”)
- Step 3: Calculate the allowance for reserved nonemployee spots
- Step 4: Determine remaining use and allocable expenses if there is any remaining parking expense

Example: An accounting firm leases a parking lot adjacent to its office building and incurs $10,000 in total parking expenses related to the lease payments. The lot has 100 spots used by employees and clients. Parking is not provided to the general public. About 60 employees use non-reserved spots during normal business hours.

- Step 1: Because there are no reserved spots, there is no amount allocated to reserved employee spots.
- Step 2: 60% of the lot is used by employees (60/100 = 60%).
- Step 3: Because none of the spots are reserved for nonemployees, there is no amount allocated to nonemployee spots.
- Step 4: The firm must reasonably determine the expenses allocable to employee parking. Because 60% of the parking spots are used by employees, a reasonable allocation would be that $6,000 of the total $10,000 cost is nondeductible.

Example: Same as above except that one part of the lot is restricted for employee parking (“reserved parking”).

- Step 1: Because there are 60 reserved spots out of the total 100 spots, $6,000 (60/100 spots x $10,000 = $6,000).
- Step 2: The primary use of remaining spots is for public parking so there is no disallowance for the remaining $4,000
- Step 3: There is nothing to figure here
- Step 4: There is nothing to figure here

Chapter 13—Taxes and Interest

Self-employment tax. The Social Security wage base limit, which applies for self-employment taxes, is $132,900 in 2019 (up from $128,400 in 2018). The tax rate for the Social Security portion of self-employment tax is 12.4% on net earnings up to this dollar limit. The tax rate for the Medicare portion of self-employment tax is 2.9% on all net earnings. The tax deduction is limited to one-half of the self-employment tax.

For those with net earnings over the applicable threshold amount of $200,000 for singles and $250,000 for joint filers (these dollar limits are not adjusted annually for inflation), there is also a Medicare surtax of 0.9% on excess earnings. This applies only to the so-called employee portion, so it is *not* deductible.

Employment taxes—FICA. The wage base limit for the Social Security portion of FICA in 2019 is $132,900. The rate for the employee’s Social Security portion of FICA is unchanged at 6.2%.

Employment taxes—FUTA tax. For purposed of FUTA in 2018, there are no "credit reduction states."

Interest payments. Net business interest expense over 30% of adjusted taxable income is not deductible. This net interest disallowance rule applies at the owner level for pass-through entities, but there is a special rule that applies at the entity level. However, there is an exemption from the interest limit for small businesses, which in 2019 are those with average annual gross receipts for the 3 prior years not exceeding $26 million.

Farming businesses and real estate businesses that do not qualify for the small business exception (their gross receipts are too high) but want to elect out of the interest deduction limitation must use the ADS recovery periods in depreciating property that is already owned as well as newly-acquired property. The IRS has said that businesses making the election do not have to file for a change in accounting method.

Chapter 14—First-Year Expensing, Depreciation, Amortization, and Depletion

First-year expensing. The expensing limit for 2019 is $1.02 million. The limit phases out when purchases for the year exceed $2.55 million. Thus, no expensing can be used if purchases for the year exceed $3.57 million.

Modified accelerated cost recovery system—recovery periods. Special recovery periods for the following types of property expired at the end of 2017; they have not yet been extended:

- The 3-year recovery period for all race horses.
- The 7-year recovery period for motorsports entertainment complexes.

Chapter 16—Retirement Plans

Contribution limits. Various limits have been increased for 2019, although some are unchanged from 2018:

- 401(k) plan elective deferrals: $19,000 (up $500), plus $6,000 for those who are age 50 and older by December 31, 2019 (unchanged).
- Savings incentive match plan for employees (SIMPLE) elective deferrals: $13,000 (up $500), plus $3,000 for those who are age 50 and older by December 31, 2018 (unchanged).
- Defined contribution plans (profit-sharing plans and simplified employee pension plans [SEPs]): the limit is $56,000 (up from $55,000 in 2018).
- Defined benefit (pension) plans: the limit is $225,000 (up from $220,000 in 2018).
- Compensation taken into account in figuring contributions and benefits: the limit is $280,000 (up from $275,000 in 2018).

- IRAs: the contribution limits for 2018 are $6,000 (up $500), plus $1,000 for those age 50 or older by December 31, 2019 (unchanged). However, the adjusted gross income limits for making deductible contributions for those who are active participants in qualified retirement plans have been increased slightly.

Special loan rules for certain disasters. As of yet, Congress has not created any special rules for victims of 2018 disasters (e.g., Hurricanes Florence and Michael and the November 2018 California wildfires).

Cost of plan maintenance. The SEC's proposed Fiduciary Rule has not yet been finalized.

PBGC premiums. For planning purposes, in 2019 the flat-rate premium for each participant is $80 (up from $74 in 2018). The variable rate premium for underfunded plans is $43 per $1,000 of unfunded benefits per employee, with a cap of $541 per participant.

State-sponsored plans for the private sector. California's CalSavers launched a pilot program in November 2018 and expects it to be open to all eligible employers beginning July 1, 2019. Eventually, any employer in the state with at least 5 employees and no other retirement plan will be required to participate in the state plan. The deadline is June 30, 2020, for businesses with 100 employees, by June 30, 2021, for those with 50 employees, and by June 30, 2022, for employers with 5 or more employees.

Illinois' Secure Choice plan also began a pilot program in 2018 for employers with 25 or more employees. This plan will auto-enroll employees, withholding 5% of their pay as required employee contributions. The Connecticut Retirement Security plan for companies with 5 or more employees began in January 2019 and requires employers to offer enrollment to its staff. For those who do not, withholding is 3% of taxable wages (unless they opt out).

Oregon's program—OregonSaves—is continuing to be phased in. On December 15, 2018, required coverage was mandated for employers with 20-49 employees (larger firms had earlier compliance dates). On May 15, 2019, it will extend to employers with 10-19 employees. On November 15, 2019, employers with 5-9 employees will have to offer enrollment, and on May 15, 2020, employers with fewer than 4 employees will have to do so.

Note: None of these state-sponsored plans permit any employer contributions and are viewed as non-ERISA plans.

Chapter 17—Casualty and Theft Losses

Disaster losses. Find a list of all federal disaster areas for 2018 from FEMA here. Designated disasters in 2019 will be listed here on FEMA.

Chapter 19—Medical Expenses

Health care mandates. A U.S. district court has ruled that all of the Affordable Care Act is unconstitutional (the opinion can be found here), although the law technically remains in effect through the appeals process. Whether the appellate court and the U.S. Supreme Court will agree with the district court and what impact these decisions will have on the employer mandate, as well as the individual shared responsibility payment for 2018, remains to be seen (the individual mandate penalty is repealed as of January 1, 2019).

Deducting health coverage for more-than-2% S corporation shareholders. The IRS has not provided any further guidance for S corporations paying for health coverage for their owners.

Small employer health care credit. Small employers that pay more than half the cost of employees' medical insurance may be eligible for a tax credit, provided they obtain coverage through the Small Business Health Insurance Option (SHOP) (government exchanges). Certain small employers whose principal business address is in a county with no qualified health plan through a Small Business Health Plan Options Program (SHOP) Marketplace may be able to claim the credit for small employer health insurance premiums (see Notice 2018-27).

The credit is reduced if premiums are more than the average premiums for the small group market in your state. The IRS has released the average premiums for small group markets in states for 2018 on a county by county basis. These average premium amounts can be found in the instructions to the 2018 Form 8941.

Note: For tax years beginning after 2013, the credit is allowed only for two consecutive tax years, so if the small employer health care credit is claimed for 2016 and 2017, no credit will be allowed for 2018, even if other requirements for the credit are met.

Looking ahead for 2019, a small employer can take the credit only if average annual payroll is below a set amount. This has been adjusted for inflation so that the full credit applies if the average annual payroll in 2019 is $27,100. No credit can be claimed for 2019 if the average annual payroll is $54,200 or more.

Using reimbursement plans. Under proposed regulations issued jointly by the U.S. Departments of Treasury (i.e., the IRS), Labor, and Health and Human Services, employers will have more latitude in offering health reimbursement arrangements (HRAs), starting in 2020 (not in 2019). Two types of HRAs will become allowable:

1. HRAs integrated with individual health insurance coverage (referred to as individual coverage HRAs). These allow employers, both large and small, to reimburse employees for the cost of their individually-obtained health coverage purchased from an insurer or through a government Marketplace, provided certain conditions are met. For example, an employer cannot use this option if it offers group health coverage to the same class of employees.

2. Standalone excepted-benefit HRAs. Employers with group health coverage can also offer these reimbursement plans up to a set dollar amount that's adjusted annually for inflation ($1,800 in 2020). This reimbursement plan can allow employees to pay premiums for COBRA, excepted-benefit coverage (e.g., limited dental or vision plans), and short-term insurance coverage.

Despite these new HRAs, QSEHRAs for small employers continue to be available. So too will retiree-only HRAs that are integrated with Medicare, Tricare, or other group health plans.

Qualified small employer health reimbursement arrangements (QSEHRAs). These reimbursement plans are a way for small employers to help employees pay for the cost of health coverage. For 2019, reimbursements to employees are capped at $5,150 for self-only coverage and $10,450 for family coverage.

Health savings accounts. The contribution limit for 2019 increases to $3,500 for self-only coverage; the limit for family coverage increases to $7,000. Those who are age 55 or older by the end of 2019 can add another $1,000 for the year (this additional contribution limit is unchanged).

To contribute to a health savings account, the person must be covered by a high-deductible health plan. For 2019, this means that the plan has a minimum deductible of $1,350 for self-only coverage and $2,700 for family coverage. The cap on annual out-of-pocket expenses (deductibles, co-payments, and other amounts) cannot exceed $6,750 for self-only coverage and $13,500 for family coverage. These amounts are unchanged.

Flexible spending arrangements. The maximum amount that employees can add to a medical FSA in 2019 is $2,700 (up $50 over the 2018 limit).

Reporting health coverage on W-2s. As yet, the IRS has not changed the exception for employers that issued fewer than 250 forms in the previous year; they do not have to report health coverage on Forms W-2.

Reporting health coverage on 1095s. The deadlines for filing Form 1095-C for applicable large employers and Form 1095-B for small employers with self-insured plans is supposed to mirror the deadlines for W-2s. However, the IRS extended the deadline for furnishing forms to employees to March 4, 2019 (just as it did in the previous year); this extension is automatic. The due date for transmittals of these forms to the IRS has not been changed. Paper returns are due on February 28, 2019; those filed electronically are due on April 1, 2019.

Chapter 20—Deductions for Farmers

Depreciation. The depreciation recovery period for all race horses fixed at 3 years expired at the end of 2017; it has not yet been extended for 2018.

Chapter 21—Qualified Business Income Deduction

Qualified trade or business. The meaning of the term "qualified trade or business" is not clearly spelled out in Code Sec. 199A governing the QBI deduction. But there is some additional clarification.

Real estate activities. There has been some concern about when real estate activities amount to a qualified trade or business so that owners can claim the QBI deduction. The IRS has provided a safe harbor for treating a **real estate enterprise** as a qualified trade or business.

Real estate enterprise An interest in real property held for the production of rents and may consist of an interest in multiple properties. Taxpayers must either treat each property held for the production of rents as a separate enterprise or treat all similar properties held for the production of rents as a single enterprise. But commercial and residential real estate can't be part of the same enterprise. And taxpayers may not vary this treatment from year-to-year unless there has been a significant change in facts and circumstances.

If the safe harbor is not applicable, a taxpayer can still try to establish that the real estate activities amount to a trade or business.

There are 3 conditions for the safe harbor to apply:

1. Separate books and records are maintained to reflect income and expenses for each rental real estate enterprise;

2. For taxable years beginning prior to January 1, 2023, 250 or more hours of rental services are performed per year with respect to the rental enterprise. For taxable years beginning after December 31, 2022, in any 3 of the 5 consecutive taxable years that end with the taxable year (or in each year for an enterprise held for less than 5 years), 250 or more hours of rental services are performed per year with respect to the rental real estate enterprise; and
3. The taxpayer maintains contemporaneous records beginning after December 31, 2018, including time reports, logs, or similar documents, regarding the following: (i) hours of all services performed; (ii) description of all services performed; (iii) dates on which such services were performed; and (iv) who performed the services. Such records are to be made available for inspection at the request of the IRS.

Rental services include:

- Advertising to rent or lease the real estate;
- Negotiating and executing leases;
- Verifying information contained in prospective tenant applications;
- Collecting rents;
- Daily operation, maintenance, and repair of the property;
- Management of the real estate;
- Purchasing materials; and
- Supervising employees and independent contractors.

Rental services do not include:

- Financial or investment management activities (such as arranging financing; procuring property; studying and reviewing financial statements or reports on operations; planning, managing, or constructing long-term capital improvements).
- Hours spent traveling to and from the real estate.

Rental services may be performed by owners or by employees, agents, and/or independent contractors of the owners.

Excluded rental real estate arrangements. Certain types of arrangements are not treated as real estate enterprises:

- A taxpayer's home if it is rented out at any time during the year.
- Real estate rented or leased under a triple net lease (i.e., one that requires the tenant or lessee to pay taxes, fees, and insurance, and to be responsible for maintenance activities of a property in addition to rent and utilities).

Relying on the real estate safe harbor. If a taxpayer or a real estate enterprise is relying on the safe harbor, a statement must be attached to the return on which the QBI deduction is claimed. The statement must be signed under penalty of perjury by the taxpayer or an authorized representative.

Statutory employees. Being an employee is not treated as a trade or business for purposes of the QBI deduction. However, some tax professionals have argued that statutory employees who file Schedule C to report their income and deductions can use the QBI deduction. This is bolstered by the fact that the IRS has specifically said W-2 wages used in figuring the QBI deduction does not include wages paid to statutory employees.

Employees turned independent contractors. The trade or business of being an employee does not make a taxpayer eligible for the QBI deduction (i.e., the QBI deduction cannot be based on wage income). Final regulations have a presumption that an employee who becomes an independent contractor and continues to provide the same services for the same company is still in the business of being an employee and is not in a trade or business for purposes of the QBI deduction. There is a 3-year lookback for purposes of this presumption.

Aggregation of multiple trades or businesses. An individual can aggregate certain multiple trades or businesses for purposes of applying the W-2 wage and UBIA of qualified property deduction limit as long as at least one person in the ownership group holds at least 50% ownership, directly or indirectly, in each trade or business being aggregated. This ownership test must be met for the majority of the year (including the last day of the year). What's more, the trades or businesses being aggregated must satisfy various tests, including 2 of the following 3 listed factors:

1. The businesses provide products, property, or services that are the same (for example, a restaurant and a food truck) or customarily provided together (for example, a gas station and a car wash);
2. The businesses share facilities or share significant centralized business elements (for example, common personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources); or

3. The businesses are operated in coordination with, or reliance on, other businesses in the aggregated group (for example, supply chain interdependencies).

No aggregation is permitted with a specified service trade or business (SSTB).

The fact that there is no aggregation in one year does not preclude aggregation in a subsequent year. An initial aggregation usually cannot be made on an amended return, but because acknowledging that individuals and pass-through entities may be unaware of the aggregation rules, the IRS will permit aggregation on amended 2018 returns. Note that once there is an election to aggregate, it must continue unless there is a material change in circumstances that would cause a change to the aggregation (e.g., common ownership falls below 50%). But disaggregation isn't permanent, although trades or businesses that are disaggregated by the Commissioner may not be re-aggregated for the three subsequent taxable years.

Qualified business income. QBI isn't merely business profits for the year. In addition to information in Chapter 21 about the meaning of the term "qualified business income," there has been additional clarification:

Payments to partners. QBI does not include guaranteed payments for the use of capital or payments to partners for services performed.

Net capital gain. For purposes of QBI, net capital gain means the excess of the net long-term capital gain over the net short-term capital loss, plus any qualified dividend income.

Losses and deductions previously disallowed. Such amounts which are allowed in the current year generally are taken into account for purposes of computing QBI to the extent the disallowed loss or deduction is otherwise allowed by Section 199A. These losses are used on a first-in, first-out (FIFO) basis. They are treated as losses from a separate trade or business. However, losses or deductions that were disallowed, suspended, limited, or carried over from taxable years ending before January 1, 2018, are not taken into account in a later taxable year for purposes of computing QBI.

Above-the-line deductions. Deductions related to a trade or business are taken into account for the QBI deduction (one-half of self-employment tax, the self-employed health insurance deduction, and the deduction for qualified retirement plan contributions on behalf of self-employed individuals as entered on lines 27, 28, and 29 on Schedule 1 of Form 1040).

Fiscal year entities. Owners of fiscal-year partnerships and S corporations with tax years beginning in 2017 take into account all QBI from the entity's 2018 fiscal year as reported on their Schedule K-1. No allocation of income to the period prior to January 1, 2018 (the effective date of the QBI deduction).

W-2 wages. There are 3 methods for calculating W-2 wages for QBI purposes:

- *Method 1: Unmodified Box method.* This is a simplified calculation. It is the lesser of total wages in Box 1 or 5 of all Forms W-2 filed with the Social Security Administration.

- *Method 2: Modified Box method*. This is the amount under Method 1 adjusted by subtracting amounts that are not wages for federal income tax withholding purposes (e.g., supplemental unemployment benefits) and adding amounts reported in Box 12 of the W-2.
- *Method 3: Tracking wages method*. This is actual wages subject to federal income tax withholding with certain modifications. More specifically, W-2 wages under method 3 are amounts subject to federal income tax withholding reported on W-2s filed with the Social Security Administration, plus amounts reported in Box 12 which are coded D, E, F, G, and S.

Wages listed on Form W-2 for statutory employees are not treated as part of W-2 wages for the QBI deduction. Wages taken into account for the QBI deduction are not determinative for purposes of FICA and FUTA taxes. Wages for the QBI deduction include wages under Code Sec. 3401(a), elective deferrals, and designated Roth contributions.

If a business has a short taxable year, only take into account wages paid and employee elective deferrals made during that period. Method 3 must be used for this purpose.

UBIA. In the case of property contributed to a partnership or S corporation in a nontaxable transfer (e.g., upon the creation of an S corporation through the transfer of property in exchange for stock), the property retains its UBIA on the date it was first placed in service by the contributing partner or shareholder. In other words, the transferee's UBIA in the qualified property is the same as the transferor's UBIA in the property, decreased by the amount of money received by the transferee in the transaction or increased by the amount of money paid by the transferee to acquire the property in the transaction.

For like-kind exchanges, the UBIA of like-kind property that a taxpayer receives is the UBIA of the relinquished property. However, if a taxpayer either receives money or property not of a like kind to the relinquished property (other property) or provides money or other property as part of the exchange, the taxpayer's UBIA in the replacement property is adjusted:

- Downward by the excess of any money or the fair market value of other property received by the taxpayer in the exchange over the taxpayer's appreciation in the relinquished property (excess boot). Appreciation for this purpose is the excess of the relinquished property's fair market value on the date of the exchange over the fair market value of the relinquished property on the date of acquisition by the taxpayer.
- Upward by the amount of money or the FMV of other property transferred to reflect additional taxpayer investment.

The same rules apply for involuntary conversions.

For qualified property acquired from a decedent and immediately placed in service, the UBIA generally is the FMV at the time of the decedent's death. Also, this begins a new depreciable period for the property.

Correction. The example on page 474 should read as follows:

Example

You are single and the sole owner of an S corporation in the construction business. You have taxable income of $500,000 and QBI of $600,000. Your corporation's W-2 wages are $300,000 and it has $1 million of unadjusted basis immediately after acquisition (UBIA) in qualified property. Your QBI deduction is $120,000, which is the lesser of:

- 20% of QBI ($600,000 x 20% = $120,000), or
- The greater of 50% of W-2 wages of $150,000 ($300,000 x 50%) or UBIA of $25,000 (2.5% of $1 million).

Chapter 22—Miscellaneous Business Deductions

Personal education incentives for 2019:

- ***American opportunity credit.*** The basic credit amount and modified adjusted gross income limit on eligibility are unchanged.
- ***Lifetime learning credit.*** The modified adjusted gross income limit threshold for phasing out the credit increases to $58,000 to $68,000 ($116,000 to $131,000 on a joint return).

- ***Above-the-line deduction for tuition and fees.*** This break expired at the end of 2017; it has not yet been extended for 2018.

- ***Student loan interest.*** The 2019 modified adjusted gross income range over which the deduction limit of up to $2,500 of interest is phased out is $140,000 to $170,000 on a joint return (up $5,000); for singles it is $70,000 to $85,000 (up $5,000).

Legal and professional fees. If you win a dispute with the IRS in which the government was not substantially justified, you may be able to recover costs up to a set dollar amount. For 2019, the dollar amount is $200 per hour (unchanged from 2018).

Meal costs for day care providers. For 2019, the rates for standard meals and snack rates have decreased slightly for Hawaii; they are unchanged for Alaska and the other 48 states:

Breakfast:

- States other than Alaska and Hawaii: $1.31
- Alaska: $2.09
- Hawaii: $1.53

Lunch and dinner:

- States other than Alaska and Hawaii: $2.46
- Alaska: $3.99
- Hawaii: $2.88

Snacks:

- States other than Alaska and Hawaii: $0.73
- Alaska: $1.19
- Hawaii: $0.86

Chapter 23—Roundup of Tax Credits

Some tax credits expired at the end of 2017; they have not yet been extended for 2018:

Employment-related credits:

- *Empowerment zone employment credit.*
- *Indian employment credit.*

Capital construction-related credits:

- *Energy-efficient home credit.*

Other tax credits:

- *Alternative fuel vehicle refueling property credit.*

Family and medical leave credit. In 2019, the credit can only be claimed for an employee earning up to $72,000 in 2018.

Chapter 25—Strategies for Opening or Closing a Business

Shareholder basis in stock. The AICPA suggestion to the IRS to provide a new tax form for tracking a shareholder's basis in S corporation stock and debt has yet to be acted upon.

Debt versus equity financing. In informal guidance, the IRS clarified the tax treatment of crowdfunding. Crowdfunding that constitute loans, contributions to capital ("equity crowdfunding"), or gifts (without any quid pro quo) are not taxable to the business. However, amounts received through a crowdfunding portal for services rendered or gains from the sale of property are taxable.

Chapter 28—Alternative Minimum Tax

Exemption amounts. The AMT exemption amounts for 2019 are:

Filing status	2019 exemption
Married filing jointly/surviving spouse	$111,700
Single/head of household	$71,700
Married filing separately	$55,850

Exemption phase-out. The exemption amounts for 2019 start to phase out when alternative minimum taxable income (AMTI) exceeds $1,020,600 for married filing jointly and surviving spouses and $510,300 for other filers.

Chapter 27—Tax Strategies for Multiple Businesses

Employer mandate. See the discussion in Chapter 19.

Chapter 29—Other Taxes

State income taxes. While no new states have enacted a gross receipts tax, Portland, Oregon enacted one effective January 1, 2019.

Employment and self-employment taxes. The 2019 wage base limit for the Social Security tax portion of FICA and self-employment tax is $132,900 (up from $128,400 in 2018).

While the issue of whether net earnings of LLC members are subject in whole or in part to self-employment tax remains on the IRS's Priority Guidance Plan for 2018-2019 found here. As yet, no guidance has been issued.

Sales taxes. Following the Supreme Court's decision in *Wayfair,* a number of states announced they would begin to require remote sellers to collect and remit sales tax. There is an exemption for small sellers, which varies from state to state (e.g., sales of no more than $100,000 in some states or $250,000 in others, or 200 or more separate transactions; Massachusetts has a $500,000/100 transaction exception). Check for effective dates, which vary from July 1, 2018, through January 1, 2019.

At the time this Supplement was prepared, Congress was considering a law to bar states (such as Massachusetts, Oklahoma, Pennsylvania, and Rhode Island) from retroactively imposing sales tax on remote sellers. Check to see whether this law is enacted.

Chapter 32—Working with CPAs and Other Tax Professionals

Fees for PTINs. Litigation on whether the IRS must refund previously-collected fees paid by paid tax return preparers for PTINs has not yet been settled.

Appendix B—Tax Penalties

The following penalties apply to 2018 returns filed in 2019:

Failure to file a tax return. The penalty is $210 or 100% of the amount required to be shown on the return.

Failure of a partnership to file a return. The penalty is $200. The penalty is per month (or part-month) that the return is late, up to a maximum of 12 months, and is multiplied by the number of partners during any part of the year.

Failure of an S corporation to file a return. The penalty is $200. The penalty is per month (or part-month) that the return is late, up to a maximum of 12 months, and is multiplied by the number of shareholders during any part of the year.

Administrative waivers. To date there have been no developments on an SB/SE Division program for self-correcting errors.

Appendix D—Dollar Limits and Amounts Adjusted for Inflation

Items Adjusted Annually for Inflation. The following adjustments apply for 2019 (and do not factor into the preparation of 2018 returns).

> ***Adoption assistance***—excludable employer-provided adoption assistance for employees ($14,080 for 2019).
>
> ***Cash method of accounting***—the gross receipts test for eligibility of C corporations and partnerships with C corporation partners to use the cash method of accounting is average annual gross receipts in the 3 prior years not exceeding a set amount ($26 million in 2019).
>
> ***Excess business losses***—the threshold used in determining whether an owner of a pass-through entity has such losses is capped at a set amount

($510,000 for joint filers and $255,000 for other filers in 2019).

First-year expensing (Sec. 179 deduction)—the dollar limit on the deduction, as well as the phase-out on property placed in service. For 2019, the limits are $1.02 million and $2.55 million, respectively.

Foreign earned income exclusion—the amount of wages or self-employment income earned abroad eligible for the exclusion is limited ($105,900 in 2019).

Medical flexible spending accounts (FSAs)—the most that employees can add annually on a pretax basis is capped at $2,700 for 2019.

Qualified business income deduction—the taxable income limit for the 20% deduction before application of a formula is required (and a phase-out for owners in specified service trades or businesses) is $321,400 on joint returns ($160,725 if married filing separately) and $160,700 for other filers.

Small employer health insurance credit—the amount of average compensation, originally fixed at $25,000, is $27,100 for 2019.

Social Security wage base—the amount that is used to figure the Social Security portion of FICA and self-employment tax ($132,900 for 2019).

Transportation fringe benefits—the amount excludable for free parking, and the aggregate

amount excludable for transit passes or van pooling, is $265
per month in 2019.

Items Set by the IRS. The following adjustments apply for 2019 (and do not factor into the preparation of 2018 returns):

Deemed depreciation for business vehicles—if the deduction for expenses for business use of a personal vehicle owned by the taxpayer is figured using the IRS's standard mileage allowance, then the basis of the vehicle is reduced by a set amount per mile (e.g., 26¢ per mile in 2019).

Mileage allowance—the rate per mile used to determine the deduction for business use of a personal vehicle instead of deducting the actual costs is 58¢ per mile in 2019.