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TAX in the News

Tax Information for Tax Practitioners

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TAX NEWS

Federal District Court in Texas Rules ACA Is Unconstitutional; No Changes At This Time—A federal judge in the Northern District of Texas ruled that the ACA individual mandate and thus all ACA provisions are unconstitutional. This is a "declaratory order" meaning that it determines the parties' rights but doesn't require either party to do anything. HHS has issued a statement that it will continue administering and enforcing the ACA. The decision is expected to be appealed. Page 2

Standard Mileage Rate Increases for 2019—Starting January 1, 2019, the optional standard mileage rate for business use of an automobile (including cars, vans, pickups, and panel trucks) will be 58 cents per mile, a 3½ cents increase from the 2018 rate. Page 2

QBI Deduction: The Taxable Income Limitation Explained—The final step in determining the QBID is to compare the preliminary calculation to 20% of the taxpayer's taxable income over net capital gain. This article explains what net capital gain consists of and where to find the amounts from forms and schedules that go into the net capital gain calculation. Page 3

QUESTION OF THE WEEK

A business client often brings customers to sporting events. Under what circumstances can he deduct the cost of meals? Is it only if they eat out before or after a game, or can he deduct the cost of meals at the game, such as food served in a baseball suite? Page 3

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FEDERAL DISTRICT COURT IN TEXAS RULES ACA IS UNCONSTITUITONAL; NO CHANGES AT THIS TIME

Texas v. United States, No. 4:18-cv-00167-O (N.D. Tex. Dec. 14, 2018).

Federal Judge Reed O'Connor in Ft. Worth, TX ruled last week that the individual mandate of the Affordable Care Act is unconstitutional and all other ACA provisions are invalid. Although the Supreme Court upheld the individual mandate in 2012, a coalition of 20 states, led by Texas, argued that because the TCJA reduced the ACA's individual penalty to $0, the mandate is unconstitutional and the remaining provisions of the law cannot be severed from it.

In this case, the district court order is a declaratory order that determines the rights of the parties without requiring either party to do anything or awarding any damages. Following the ruling, HHS issued a statement indicating that the decision is not an injunction halting enforcement of the law or a final judgment on the ACA. HHS will continue administering and enforcing the ACA.

A coalition of 16 states, led by California, plan to appeal the ruling to the Fifth Circuit Court of Appeals. The Fifth Circuit includes Texas, Louisiana, and Mississippi. It is likely that the ruling will eventually go to the Supreme Court.

Under the TCJA, the individual mandate and penalty for not having health insurance still apply for 2018. Most other provisions, including the business mandate, coverage for preexisting conditions, and other reforms were unchanged by the TCJA.

STANDARD MILEAGE RATE INCREASES FOR 2019

In news release IR-2018-251 and Notice 2019-02, the IRS announced that the standard mileage rate for business use of an automobile will *increase* by 3½ cents starting January 1, 2019 to 58 cents per mile. The mileage rate for medical/moving purposes will *increase* by two cents. The mileage rate for service to charitable organizations remains at 14 cents per mile.

The business mileage rate is determined by the price of gas and oil and also by other fixed and variable costs, including depreciation, repairs, insurance, and tires. Use of the standard mileage rate is limited to four or fewer vehicles used simultaneously. Also, the standard mileage rate may not be used if any MACRS depreciation or the §179 deduction was previously claimed for the vehicle. Under the TCJA, this and other automobile expense deductions are not available to employees (employees are no longer allowed to deduct employee business expenses on Schedule A).

The medical/moving rate is determined mostly based on gas and oil prices. Under the TCJA, moving expenses are deductible only by certain members of the armed forces.

The charitable mileage rate is a statutory rate and not indexed.

The standard mileage rates for 2019 and 2018 are summarized below:

	January 1, 2019 (until further notice)	**January 1, 2018 — December 31, 2018**
Business	58 cents/mile	54.5 cents/mile
Depreciation element	26 cents	25 cents
Medical/moving	20 cents/mile	18 cents/mile
Charitable	14 cents/mile	14 cents/mile

QBI DEDUCTION: THE TAXABLE INCOME LIMITATION EXPLAINED

When a taxpayer is eligible for the qualified business income deduction (QBID), the final step in figuring the QBID is to compare the calculated deduction to 20% of the taxpayer's taxable income. The QBID is the smaller of the two amounts. This is so whether the preliminary QBID includes REITs, PTPs, and/or the complicated phaseout calculation, or is simply 20% of QBI.

Exactly *what* taxable income is used to figure this final limitation? Under §199A(a)(2), the limitation is 20% of the excess of the taxpayer's taxable income over net capital gain. In turn, net capital gain is defined in §§1(h) and 1222(11) as the excess of net long-term capital gain over net short-term capital loss.

Form 1040 instructions (starting on page 34) include information on the QBID and a "simplified worksheet."* The instruction for the QBI worksheet, line 12 (net capital gains) instruct the taxpayer to add:

a) Qualified dividends (Form 1040, line 3a) *plus*

b) If *not* required to filed Schedule D, the net capital gain reported on Schedule 1, line 13, *or*

   If *required* to file Schedule D, the smaller of Schedule D line 15 or 16.

The result is backed out of taxable income (AGI less the standard or itemized deductions) and multiplied by 20% to arrive at the amount to compare to the preliminary or tentative QBID.

Generally, a taxpayer is not required to file Schedule D if the taxpayer has no capital losses and capital gain consists only of capital gain distributions reported in box 2a of Form 1099-DIV, *Dividends and Distributions*. Other Schedule D exceptions are on page 87 of the Form 1040 instructions.

For Schedule D filers, Schedule D, line 15 is for net long-term capital gain or loss and line 16 combines that amount with net short-term capital gain or loss. Thus, the instruction serves to reduce net long-term capital gain only if there is a net short-term capital loss. The instruction also states that if either line 15 or 16 is blank or a loss – which means the taxpayer does not have a net long-term capital gain (or the net long-term gain is eliminated by a net short-term capital loss) – net capital gain from Schedule D is zero.

To reiterate, the QBID taxable income limitation means 20% of the taxpayer's taxable income over (or minus or less) net capital gain. Any shorthand way of referencing the limitation, such as taxable income net of capital gain, or net taxable income, is imprecise and thus not correct. We've corrected any such language in all the QBI deduction articles in TAX in the News and combined the articles in one digest on TTI.com.

* *Note*: There will be two worksheets for the QBID: the simplified worksheet in the Form 1040 Instructions and a "complex" worksheet that will appear in the 2018 version of IRS Pub. 535, *Business Expenses*.

QUESTION OF THE WEEK

Q. A business client frequently brings customers and potential customers to sporting events. We know that entertainment expenses are no longer deductible, but what about food? Is the meal deductible only if they eat in a restaurant before or after the game, or is it possible to deduct the meal expense if they eat at the game? For instance, he has baseball suite tickets and they usually have food served at the game.

A. The IRS addressed this very situation in Notice 2018-76. Under the guidance in this notice, a taxpayer may deduct 50% of business meal costs if *all* of the following are true:

1. The expense is an ordinary and necessary business expense paid or incurred during the taxpayer's taxable year.
2. The expense is not lavish or extravagant under the applicable facts and circumstances.

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3. The taxpayer, or an employee of the taxpayer, is present when the food or beverages are furnished.
4. The food and beverages are provided to a current or potential business customer, client, consultant, or other business contact.
5. When food and beverages are provided as part of an entertainment activity, the food and beverages are purchased separately from the entertainment or the cost is stated separately from the entertainment costs on bills, invoices, receipts, etc.

The first four criteria are the general requirements for deducting business meals. The fifth takes care of the TCJA change disallowing entertainment expenses but continuing to allow qualified business meal expenses. If the fifth requirement is not met, food and beverage costs are treated as nondeductible entertainment expenses rather than deductible business meals. Entertainment activities may include going to a night club, theater, sporting event, etc.

Applying this principle to your client's situation, if he purchases food separately, or the facility bills or separately states the cost of food and beverages on the billing for the suite tickets, then your client may deduct 50% of the business meal cost, assuming all of the other criteria are met. Otherwise, the cost of food and beverages is treated as part of nondeductible entertainment expenses.

Notice 2018-75 is transitional guidance that taxpayers may rely on until the Treasury Department and IRS publish proposed regulations on §274 as amended by the TCJA.