2017 INCOME TAX GUIDE

◆◆*43rd Year of Publication*◆◆

The Arc Michigan®

2017 Income Tax Guide prepared for persons
supporting children and/or adults with intellectual impairment
and/or related developmental disabilities.

2017 INCOME TAX GUIDE

for use in preparing your federal return for tax year* ***2016*

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Introduction

This authoritative income tax guide has proven invaluable for families and individuals concerned about tax deductions and credits related to the care and support of a child or an adult with an intellectual or developmental disability. After forty-three issues, this booklet has become an annual "must-have" for the informed parent. Many of the figures contained within this guide are calculations by CCH, Inc., based on its Consumer Price Index estimates due to official IRS tables not being released in time for either publication.

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Special acknowledgments for on-going counsel and tax advice go to: **John Gideon,** C.P.A., of Buss & Company, P.C., Clinton Township, Michigan (586-263-8200); **Larry Larmee,** C.P.A., of Integrity Financial Planning and Asset Management, LLC, Bingham Farms, Michigan (248-646-6044); and, **Matthew Partyka**, C.P.A., (also: **Sue Tafa**, EA, Senior Tax Advisor, and **Phillip Partyka**, Associate) of Partyka and Company, P.C., Warren, Michigan (586-571-7100).

This guide is available free of charge on-line at http://www.arcmi.org or at http://www.thearcoakland.org. The guide may be printed without permission for use by members and friends of The Arc Michigan.

The information contained within the 2017 INCOME TAX GUIDE concerning your income tax and special deductions and/or credits is not intended to be all-inclusive. Although this guide is designed to provide accurate guidance, The Arc Michigan as publisher is not engaged in rendering legal, accounting or other professional service. Please refer to the sources referenced for complete information. Bring this Tax Guide to your appointment with a knowledgeable tax consultant to facilitate preparation of your return. Although multiple resources are used to research and confirm relevant information, current materials were also verified through the 2017 U.S. MASTER TAX GUIDE, Commerce Clearing House, Inc., Chicago, IL.

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Highlights of Tax Changes for Tax Year 2016

Congress, for once in the past four years, did not make any last-minute changes or updates to our tax laws. That being said, 2017 may turn out to be a significant year for tax planning and reform. The "Achieving a Better Life Experience (ABLE) Act" finally went live in Michigan (the 5th state to do so) on November 1, 2016; other states are quickly following suit. The ABLE Act [Internal Revenue Code (IRC) §529A] creates tax-favored savings accounts, similar to a Qualified Tuition Plan (commonly known as an IRC "§529 plan"), for individuals with disabilities along with some tax-related offsets. Please see page 28 for detailed information.

Services to those with disabilities are constantly under the threat of severe budget cuts or re-allocations of tax revenues. The election year of 2016 certainly proved to be quite interesting. Fundamental changes in how all levels of government fund mental health services may be on the horizon.

What are the answers? For starters, always keep the lines of communication open with your elected officials about the needs of those with intellectual impairment and other related developmental disabilities. Next, increase your volunteer and charitable financial support for the advocacy efforts of your local, state and national chapters of The Arc. And, finally, maintain a positive attitude about the future. The politics is, if anything else, cyclical. It will change.

This guide is for members of The Arc. It is not intended to cover every circumstance. The topics and information are provided as a "heads up" for taxpayers as we sit down during 2017 to figure our 2016 income taxes. This tax booklet updates the usual myriad of numbers and dollar amounts that have been changed due to automatic increases in the cost-of-living, or new legislative mandates.

Professional tax advice is always the key to detailed information. The highlights described below are important to every taxpayer. Read and discuss each carefully with your tax advisor to determine how it all relates to your specific tax situation. Once again, this listing is NOT intended to be all-inclusive.

★ **Individual Tax Rates** - The tax brackets for tax year 2016 are set at: 10%, 15%, 25%, 28%, 33%, 35%, and 39.6. During 2016, the 10% tax bracket, for married couples filing jointly, has the first $18,550 of taxable income subject to this rate ($9,275 for single persons). For married couples filing jointly, taxable income over $18,550 and up to $75,300 is subject to the 15% rate (over $9,275 and up to $37,650 for single persons). Likewise, income over $75,300 and up to $151,900 (over $37,650 and up to $91,150 for single persons) will be taxed at the 25% rate. Income over $151,900 for married filing jointly ($91,150 for single persons) and up to $231,450 ($190,150 for single persons) will be taxed at the 28% rate. Income over $231,450 for married filing jointly ($190,150 for single persons) and up to $413,350 (both for married-joint, and single) is taxed at the 33% rate. Income over $413,350 for married filing jointly and single persons, but up to $466,950 (for married-joint) and $415,050 (for singles) is taxed at the 35% rate. Finally, all income over $466,950 (married-joint) or $415,050 (singles) is taxed at the 39.6% rate. (§11 and §13 – 2017 U.S. Master Tax Guide)

★ **Personal Exemptions** - Adjusted annually for inflation, the personal exemption rate for tax year 2016 is $4,050. Senior citizens (65 and older) and persons who are blind are unable to claim extra exemptions, as these are already included within the standard deduction amount.

As a reminder, commencing with tax year 2013, higher income taxpayers must reduce the amount of their otherwise allowable personal and dependency exemption deduction. This is subject to an annual adjustment for inflation. The American Taxpayer Relief Act of 2012; [IRC §151(d)(3)]; and, (§§126, 133, 135 and 137 – 2017 U.S. Master Tax Guide)

★ **Personal Exemptions (Michigan)** - A parent of a dependent minor or adult child with a severe intellectual and/or physical disability is allowed to claim an additional "Totally and Permanently Disabled" exemption. The definition for what constitutes a disability is that used by the Social Security Administration (42 U.S.C. 416) for the Supplemental Security Income (SSI) and Social Security Disability Insurance (SSDI) programs. A special note: beginning with tax year 2012, Michigan terminated its special general exemption for children 18 and under.

★ **Earned Income Tax Credit (Michigan)** - there is a refundable Michigan Earned Income Tax Credit equaling 6% of the federal credit available for tax year 2016. You must file a Michigan income tax return to receive this credit.

★ **Social Security Tax Base** - The wage base for Social Security tax purposes is set at $118,500 for 2016. The tax rate for employees was 7.65% for 2016, while the employer's portion was also at 7.65%. The tax rate for the self-employed during 2016 was 15.3%. Self-employed workers may deduct from gross income half of the Social Security tax as a business expense. (§§47, 49 and 923 – 2017 U.S. Master Tax Guide)

All 2016 wages and salaries are subject to the MEDICARE portion of the Social Security tax. The first $250,000 of earned income (married filing jointly) and $200,000 (single persons) are taxed at a 1.45% rate (employees) and a 2.9% rate (self-employed). The rate increases by .9% to 2.35% for wages and 3.8% for self-employment income in excess of $250,000 (married filing jointly) and $200,000 (single persons). These thresholds are based on the combined wages for joint returns.

NEW: A large number of Medicare "Part B" recipients (i.e., single persons with annual incomes below $85,000, and married filing jointly below $170,000) will see their 2017 monthly premium increase slightly from $104.90 to $109.00 --- if already on Medicare prior to 1/1/2016. For all new enrollees after 1/1/2016, the Part B premium has been raised from $121.80 to $134.00 as of 1/1/17. Keep in mind that most persons with Medicaid coverage in Michigan do not pay either the $109.00 or $134.00 premium for Part B Medicare; this also applies to individuals who had to forego their Supplemental Security Income (SSI) benefits because they exclusively receive Social Security Disability Insurance (SSDI) as a "Disabled Adult Child" (a.k.a., "D.A.C.") based on a parent's Social Security Administration work record. If the state of Michigan pays the Part B premium due to your Medicaid eligibility, it must now pay, for all recipients, the new rate of $134.00. As always, persons with higher incomes will pay a significantly higher premium.

★ **Standard Deductions** - Adjusted annually for inflation, the flat standard deduction for non-itemizing taxpayers during 2016 is $12,600 for joint filers, $9,300 for heads of households, and $6,300 for both single persons and married filing separately.

An extra standard deduction of $1,250 in 2016 exists for each married person age 65 and over, and each blind taxpayer. This extra deduction is $1,550 for 2016 if the blind or elderly person is single or head of household. Two additional amounts will be allowed to an individual who is both over 65 and blind. Each is in addition to the full standard deduction. (§126 – 2017 U.S. Master Tax Guide)

An individual for whom a dependency deduction is allowed to another taxpayer during 2016 can use the greater of $1,050 or the sum of $350 and the single individual's earned income up to the applicable standard deduction amount ($6,300 in 2016) of his/her standard deduction to off-set unearned income. The next $1,050 is taxed at the individual's own tax rate, unless the following election is made [IRC §63(c)(5)] (§126 – 2017 U.S. Master Tax Guide):

> Parents may elect to include on their return the unearned income of a child under age 18 whose income is between $1,050 and $10,500 in 2016 and consists solely of interest and dividends. Parents making this election are taxed on their child's income in excess of $2,100 in 2016. The child is treated as having no gross income and does not have to file a tax return if the election is made for the tax year. The election is not available if estimated tax payments have been made in the child's name and taxpayer identification number for the tax year. Form 8814 is used to make this election and to report the child's interest and dividends on the parent's return. (§103 – 2017 U.S. Master Tax Guide)

★ **Social Security Number-Children** - Minors claimed as dependents must have a Social Security number. (§116 – 2017 U.S. Master Tax Guide)

★ **Return for Persons with a Disability -**A guardian for a minor or a legally disabled person is required to file a Form 1040, 1040A or 1040EZ as an agent for such person if the individual would be required to file a return. However, a minor may file a return for him/herself or have someone else do so to relieve the guardian of this obligation. An agent making the return for another should file Form 2848 ("Power of Attorney and Declaration of Representative") with the taxpayer's return. BEWARE: both the agent and the taxpayer for whom the return is made may be liable for penalties. (§504 – 2017 U.S. Master Tax Guide)

★ **Child Tax Credit ("CTC") -** Taxpayers of qualifying children (i.e., child, descendant, step-child, or eligible foster child who is a U.S. citizen and for whom the taxpayer may claim a dependency exemption and who is under age 17 at the close of the tax year) are entitled to a "Child Tax Credit." The credit amount is $1,000 per qualifying child for tax year 2016 (… made permanent by the American Taxpayer Relief Act of 2012, but without any automatic inflation adjustments for future years).

In 2005, the CTC adopted the uniform definition of a qualifying child under IRC §152, as amended by the Working Families Tax Relief Act of 2004 (see also: §137A – 2017 U.S. Master Tax Guide). Although the relationship requirements remain the same, a taxpayer no longer has to prove that they supplied over one-half the support but rather that the child did not provide more than one-half of his or her own support. The same is true for the residence requirement. A qualifying child need only have the same principal place of abode as the taxpayer for more than six months in the year. This same definitional language also applies to the Earned Income Credit (see Page 9), and the Child and Disabled Dependent Care Credit (see Page 22).

This credit begins to phase out when the modified adjusted gross income reaches $110,000 for joint filers, $55,000 for married couples filing separately, and $75,000 for single persons.

Taxpayers with three or more qualifying children are entitled to an alternative method for calculating this credit (§1305 – 2017 U.S. Master Tax Guide). Under §§101 and 103 of the 2010 Tax Reform Act, the $1,000 Child Tax Credit is allowed to be used as an off-set against regular income tax and the Alternative Minimum Tax ("AMT").

★ **Volunteer Mileage -** The charitable deduction for individuals using their passenger cars in volunteer work for qualified charities is at 14¢ per mile (for 2016 and 2017) plus parking fees and tolls, instead of actual expenses. This rate is not indexed for inflation. (IR-2010-51; Notice 2016-79; §1061 – 2017 U.S. Master Tax Guide)

★ **Medical Deductions** – Medical expenses, which also include medical insurance premiums, are subject to a 10% of "adjusted gross income" (AGI) medical expense deduction floor for 2016. However, for tax years 2013 through 2016, if you are age 65 or older prior to the close of the tax year, the deduction floor is set at 7.5%. On a joint return, the percentage limitation is based on the total AGI of both spouses. (§1015 – 2017 U.S. Master Tax Guide)

★ **Tax Rates for Non-Grantor Trusts & Estates -** (§19 – 2017 U.S. Master Tax Guide):

2016

Taxable Income	Rate
0 - 2,550	15%
2,550 - 5,950	25%
5,950 - 9,050	28%
9,050 - 12,400	33%
12,400 - over	39.6%

★ **Estate Tax Chart -** (§§40, 41 and 2901 – 2017 U.S. Master Tax Guide):

Year	Top Estate Tax Rate	Exemption Amount
2014	40%	$5,340,000
2015	40%	$5,430.000
2016	40%	$5,450,000
2017	40%	$5,490,000

★ **Earned Income Credit ("EIC") -** The EIC is a refundable credit that is available to certain low-income individuals who have earned income, meet the adjusted gross income thresholds, and do not have investment income above a certain amount. Taxpayers claiming the credit must provide a Social Security number and that of their spouse. Failure to do so will be treated as a mathematical error.

The "Protecting Americans from Tax Hikes Act of 2015" made permanent certain enhancements to the EIC developed over the past two decades; most recently by the "American Taxpayer Relief Act of 2012." (see: Wolters Kluwer/CCHGroup "Tax Briefing" dated 12/18/15)

Different credit percentages and phaseout percentages are provided for low-income individuals who have no qualifying children (see CTC, Page 8, for definitional language), one qualifying child, and more than one qualifying child. An individual who is a qualifying child may not also claim such a credit in the same tax year.

An individual who does not have a qualifying child may be eligible for this credit if: (1) the principal residence of such individual is in the United States for more than one-half of the tax year; (2) the individual (or the spouse of the individual) is at least age 25 and under age 65 before the close of the tax year; and (3) the individual is not claimed as a dependent by another.

Married persons must file a joint return in order to claim this credit. A married person living apart from a spouse under certain circumstances need not file a joint return to claim the credit. Except in the case of death, the credit may be claimed only for the full 12-month tax year.

For 2016, the maximum credit is as follows: one qualifying child - $3,373; two - $5,572; three or more is $6,269; with no qualifying children, $506 is the maximum credit.

The EIC is reduced by a limitation amount determined by multiplying the applicable phase-out percentage by the excess of the amount of the individual's adjusted gross income (or earned income, if greater) over the phaseout amount. The earned income amount and the phaseout amount are adjusted yearly for inflation.

Taxpayers should complete Schedule EIC with Forms 1040 or 1040A, or Form 1040EZ to determine whether they are eligible for the credit. A taxpayer claiming the EIC must include their taxpayer identification number and that of their spouse (if married) and any qualifying children on their income tax return. (§1322 – 2017 U.S. Master Tax Guide)

★ **Adult Home Help Services** - Adult Home Help Services (AHHS) is not taxable as income to parents, and others, who are care providers within their own home. Details on page 20.

★ **Standard Business Mileage Deduction** - The amount is 54¢ per mile for 2016 and 53.5¢ for 2017 (IR-2010-51; Notice 2016-79; §947 – 2017 U.S. Master Tax Guide).

★ **Business Expenses** - Except for certain statutory employees (generally, salespersons soliciting orders), employees are unable to deduct unreimbursed business expenses in arriving at adjusted gross income (AGI). Instead, this deduction is a miscellaneous itemized deduction. Such deductions are deductible only to the extent they exceed 2% of AGI.

No deduction is allowed for travel or other costs of attending a convention, seminar or similar meeting **unless** the activity directly relates to a trade or business of the taxpayer. For example, expenses for registration fees, travel and transportation costs, meals and lodging expenses, etc., incurred in connection with attending an investment seminar or other activity not related to a taxpayer's trade or business are not deductible.

In addition, no deduction is allowed for expenses of attending a trade or business-connected convention, seminar, or similar meeting that does not offer significant business-related activities, such as participation in meetings, workshops, lectures, or exhibits held during the day. Thus, the cost of attending a seminar would not be deductible if participants are merely furnished videotapes of business-related lectures to be viewed at their own convenience.

Many other specific requirements exist relative to business expenses; so, it is always a good idea to seek the counsel of a qualified tax consultant for more detail. (§§910-919 and 1079 – 2017 U.S. Master Tax Guide)

★ **Individual Retirement Accounts ("IRAs")**

The rules for traditional IRAs are complex. Individuals also have access to Roth IRAs and Education IRA's. The word to the wise is to always consult a tax professional about this area.

Generally, an individual who receives compensation ("earned income" in the case of a self-employed individual) that is includable in gross income may establish and make contributions to his/her own IRA. Compensation includes alimony, but does not include pensions, annuities or other forms of deferred compensation.

For tax years 2016 and 2017, the maximum combined contribution to a traditional IRA and Roth IRA is $5,500 (see: IRC §219(b); IRS Notices 2015-75 and 2016-62). Any individual who will be at least 50 years old by the end of tax year 2016 is able to make an additional maximum contribution of $1,000 to either a traditional or Roth IRA.

IRA earnings are still tax-deferred for everyone until withdrawal. Distributions from an IRA to a participant before he or she has reached age 59½ are generally subject to a 10% penalty similar to such a requirement within qualified plans (e.g., 401(k)'s, 403(b)'s, or 457's). The distributions to an IRA owner must commence no later than April 1st following the calendar year in which the owner reaches age 70½. Finally, there are several penalty-free withdrawals allowed. For example: first-time home buyers, qualified higher education expenses, and unemployed individuals who pay medical premiums.

- **"Roth IRA"** - an alternative to the traditional IRA. Instead of the contributions being deductible, the tax advantages will be "back-loaded," that is, the buildup of interest, dividends and appreciation within this type of IRA may be tax-free depending on how and when the taxpayer withdraws money from the account. Tax-free withdrawals typically will not be allowed within the five-taxable-year period beginning with the first taxable year for which a contribution was made. A "Roth IRA" must be designated as such when it is first established.

Funds from a "Roth IRA" may be distributed tax-free if the individual has owned the IRA for five years prior to the year of withdrawal <u>and</u>: (1) the individual attains age 59½; (2) it is to the beneficiary or estate, after the death of the individual; (3) it is on account of the individual's becoming disabled; or (4) made for qualified first-time homebuyer expenses.

Contributions to "Roth IRAs" are subject to income limitations. The maximum yearly contribution that can be made to a "Roth IRA" is phased out for single taxpayers with modified adjusted gross income during 2016 above $117,000 ($184,000 for married filing jointly). No contribution to a "Roth IRA" is allowed once the modified adjusted gross income exceeds $132,000 for the single taxpayer ($194,000 for married filing jointly).

"Roth IRA" contributions may be made even after the individual for whom the account is maintained has reached age 70½. The regular IRA rules requiring minimum distributions to persons over 70½ do not apply.

>>> (§§2155 - 2179 – 2017 U.S. Master Tax Guide; also, "1997 Tax Law Summary" by NPI)

- **Coverdell Education Savings Account (CESA) (formerly: Education IRA)** - designed to be used by those saving for a child's (under age 18 or any age if the adult child has special needs) future educational expenses. Generally speaking, contributions to CESA's are treated as gifts to the beneficiaries, but distributions are excludable from gross income once a distribution for education expenses is made. Annual non-deductible contributions of up to $2,000 per year (excluding rollovers) per beneficiary may be made until the time the beneficiary turns age 18.

Withdrawals to pay qualified higher education expenses of the child (the designated account beneficiary) during the year are tax-free. For tax year 2016, the annual contribution is phased-out for joint filers with modified adjusted gross income at or above $190,000 and less than $220,000 (at or above $95,000 and less than $110,000 for single filers).

"Qualified education expenses" are those incurred within public or private (including religious-based) elementary, secondary, undergraduate, and graduate level education settings. Such expenses incorporate services in the case of a special needs beneficiary, which includes tutoring and expenses for room, board and/or transportation. Although the IRS has not released a formal definition of a "special needs beneficiary," it may use something along the lines of the following: "*an individual who because of a physical, mental or emotional condition (including a hearing disability) requires more time to complete his or her education*." Please consult IRS Publication 553 in January 2017. The age limit mentioned earlier in this section does not apply to beneficiaries with special needs. Always consult a qualified tax professional for specific details on this topic. (§867 – 2017 U.S. Master Tax Guide) (Publication 970)

★ **Dependency Exemption for Students** – Generally, an adult child who is a full-time student and under the age of 24 at the end of the calendar year may be claimed as a "qualifying child" dependent. At age 24 and over, a "qualifying relative" exemption may be taken if that adult child's gross earned income is less than the exemption amount ($4,050 for 2016 and 2017) and the parent has furnished over half of that individual's total support during the calendar year. (§§137A, B, and 143 – 2017 U.S. Master Tax Guide)

★ **Self-Employed Health Insurance Deduction -** Persons in this situation may deduct from gross income 100% of amounts paid for health insurance coverage for themselves, spouses, and dependents (§908 – 2017 U. S. Master Tax Guide). For premiums paid through an insurance exchange, the amount paid is the gross premium less the credit calculated on 2016 IRS Form 8962 ("Premium Tax Credit") (§1331 – 2017 U.S. Master Tax Guide). Children under the age of 27 will be considered dependents of a taxpayer for purposes of the deduction for the health insurance costs of a self-employed person, spouse, and dependents [IRC §162(l)]. A child includes: a son, daughter, stepson, or stepdaughter of the taxpayer; a foster child placed with the taxpayer by an authorized placement agency or by judgment, decree, or other order of any court or competent jurisdiction; and a legally adopted child of the taxpayer or a child who has been lawfully placed with the taxpayer for legal adoption [IRC §152(f)(1)].

★ **Domestic Employees** – The cash wage threshold for reporting and paying ***Social Security*** taxes (i.e., F.I.C.A.) for domestic workers, (e.g., babysitters, housekeepers, gardeners) during 2016 is $2,000 a year. Employers must report Social Security and federal unemployment tax obligations on their federal income tax forms (1040 or 1040A) using Schedule H. (§2650 and 2652 – 2017 U. S. Master Tax Guide)

The general wage threshold for reporting and paying Michigan and federal ***unemployment*** taxes on a quarterly basis is $1,500 in a calendar quarter during 2016 or preceding year, except if the total wages are paid to household employees (i.e., "domestic labor"). That wage threshold then becomes $1,000 per calendar quarter in the current or preceding year where state and federal unemployment taxes are due on all wages. (§2649 – 2017 U.S. Master Tax Guide)

Beware! This section may also apply to families that receive respite care dollars (or other such payments termed "vouchers") either directly from a county Community Mental Health Agency/Authority ("CMHA") or through a contracted services entity. If the CMHA or contracted services entity pays the money directly to the parent, who in turn pays a respite provider, the threshold of $1,000 may be exceeded not only by virtue of the CMHA dollars, but also by the parents' own money spent to supplement respite services.

CHARITABLE CONTRIBUTIONS

NEW: The "Protecting Americans from Tax Hikes Act of 2015" made permanent a long-standing provision that allows donors to make certain charitable gifts from a traditional IRA (or in certain circumstances a Roth IRA) without having to pay income tax on the distribution.

To make a gift of an IRA to a non-profit organization and not incur income tax on the donation:

- the donor must be at least 70½ years of age;
- the gift must be made directly from the IRA to the public charity (such as, The Arc);
- the amount donated from the IRA cannot exceed $100,000 in any one year; and,
- the gift must be made in 2016.

The charity must provide the donor with a specific and contemporaneous written acknowledgement of the gift. [IRC §408(d)(8)] (§§1058 and 2165 – 2017 U.S. Master Tax Guide) (see also: Wolters Kluwer/CCHGroup "Tax Briefing" dated 12/18/15)

A. Deduction for Itemizers

Only persons who itemize deductions are allowed to deduct their charitable contributions. If a contribution is $250 or more, it must be substantiated by a contemporaneous written acknowledgment from the charitable organization. The taxpayer must obtain this written confirmation *before* filing the tax return. Generally, the acknowledgment must include the amount of cash and a description of non-cash contributions, together with a description and a good-faith estimate of the value of any goods or services received for the contributions.

The Pension Protection Act of 2006 changed the cash-contributions-to-charities substantiation rules. Deductions are not allowed for contributions of cash, checks or other monetary gifts, *regardless of the amount*, unless the donor maintains either: (1) a bank record (e.g., canceled check; financial institution or credit card statements), or (2) a receipt, letter, or other written communication from the charity, indicating the charity's name, the contribution date and amount. [IRC §170(f)(17)] (Publication 526) (§1070A – 2017 U.S. Master Tax Guide)

Contributions charged to a bank credit card are deductible in the year charged even though paid in a later year. Contributions made by payroll deduction may be substantiated with an employer-provided document, (e.g., a pay-stub or W-2) showing the amount deducted and a donee-prepared document stating that there were no goods or services provided, in whole or part, as consideration for such contributions. Substantiation is required only if $250 or more is deducted from a single paycheck. (§§1058-1071 – 2017 U.S. Master Tax Guide)

B. Volunteer Activities

The value of services rendered to a charitable institution/organization is not deductible as a contribution, however, an out-of-pocket, unreimbursed expense, such as for transportation, travel, uniform, telephone, equipment, etc., incurred in rendering such a service is deductible as a contribution. This includes reasonable payments for necessary meals and lodging while away from home overnight donating services to a "qualified" charitable organization (The Arc Michigan is a qualified charitable organization and this section applies to volunteer advocates.)

The cost of travel on behalf of charitable organizations is deductible as long as there is no significant amount of personal pleasure, recreation or vacation involved. In general, miscellaneous business/travel expenses are allowable for individuals only to the extent that the expenses exceed 2% of adjusted gross income. [IRC §170] (Refer: Section 166, CCH Explanation of Tax Reform Act of 1986, p. 87)

In lieu of deducting the actual expenses incurred while using a vehicle for transportation, the IRS standard volunteer mileage rate is 14¢ per mile (2016 and 2017). A taxpayer must use this rate when computing the cost of operating an automobile where this expense is deductible as a charitable contribution. Parking fees and tolls are also deductible, but depreciation and insurance are not. (IR-2010-51; Notice 2016-79; §1061 – 2017 U.S. Master Tax Guide)

C. Convention Delegates

Persons representing The Arc, their church, or an American Legion Post, for example, at a convention for that qualified charitable organization, may deduct as charitable contributions the unreimbursed costs of attending the convention. However, the mere fact a member of a particular church or charitable organization attends a convention "on his/her own" rather than as delegate, does not provide an entitlement to deduct expenses unless incurred while actually performing some service at the convention. [IRC §170]

D. Clothing and Household Items

A deduction for a donation of clothing and household items will be allowed only if the donated property is in good, used condition or better. “Household items” do not include food, paintings, and antiques, other objects of art, jewelry, gems or collections. The IRS can deny a deduction for donated property that is of minimal value. These restrictions do not apply if: (1) a deduction of more than $500 is claimed for the single clothing or household item; and (2) a qualified appraisal for that item is attached to the income tax return. (§1061 – 2017 U.S. Master Tax Guide)

MEDICAL EXPENSE DEDUCTIONS

A. In General

Unless otherwise noted, information on most medical deductions can be located in the latest version of *IRS Publication 502*.

It is well-established that, under current tax law, taxpayers may include in computing their medical expense deductions amounts paid on behalf of a dependent or a person who could be claimed as a dependent, unless that person had annual earned income of $4,050 or more.

<u>REMINDER</u>: Medical expenses, which also include medical insurance premiums, are now subject to a 10% (formerly 7.5%) of “adjusted gross income” (AGI) medical expense deduction floor for 2013 and subsequent years. However, for tax years 2013 through 2016, if you are age 65 or older, the deduction floor remains at 7.5%. For premiums paid through an insurance exchange, the amount paid is the gross premium less the credit calculated on 2016 IRS Form 8962 (“Premium Tax Credit”). On a joint return, the percentage limitation is based on the total AGI of both spouses. (§1015 – 2017 U.S. Master Tax Guide)

B. Special Schools and Special Training for Children with Disabilities

As you consider this area of “medical expenses,” keep in mind that some deductions may be proper under the IRS rules, but may not necessarily conform to the receipt of Supplemental Security Income (SSI) benefits or Medicaid due to income limits. *(Refer also to page 17, part “O,” and page 25, “Amounts Expended by State ...”)*

You may deduct as “medical expenses” the costs of:

1. A special school attended by your child if the principal purpose of the schooling is to *alleviate his or her disability* (including tuition, room and board as applicable); [IRC §213]; [Rev. Rul. 78-340]; (§1016 – 2017 U.S. Master Tax Guide)
2. Tests and evaluations at the special school;
3. Special instruction or training such as Braille, lip reading, speech instruction;

4. Tutoring fees paid on a doctor's recommendation for your child's tutoring by a teacher specially trained and qualified to work with children who have severe learning disabilities; and,
5. Other medical expenses that your student-child may require, even though the child may have earned more than $4,050 in annual earned income.

C. Medicine, Drugs and Vitamins

A deduction for the cost of medicine and drugs (including insulin) is limited to those that may be obtained **ONLY** by prescription. Vitamins and other medicines or preparations normally purchasable over-the-counter, notwithstanding a prescription from a doctor, are non-deductible. However, an over-the-counter medicine or drug qualifies for tax-free reimbursement through a flexible spending plan or a health reimbursement arrangement if a prescription is obtained. (Federal Tax Coord. 2d; K-2102) (Publication 502) (§1017 – 2017 U.S. Master Tax Guide).

D. Sheltered Workshop Cost

If you must pay out-of-pocket for your adult dependent child to attend a sheltered workshop (or, "special school"), you may deduct as a "medical expense" the cost of the workshop if that program's primary purpose is to *alleviate the disability*. If the service of the workshop is designed to "alleviate" a disability, it will generally constitute "medical care" within the Internal Revenue Code. Usually, the service of teaching someone to perform a job is not considered "medical care." However, services, which assist a person with an intellectual impairment toward the goal of achieving everyday community living skills, may be considered to "alleviate" the disability and therefore qualify as deductible "medical care." This service is comparable to the service of teaching Braille to a child who is blind, thus alleviating the blindness, or teaching lip reading and sign language to a child with a hearing impairment, thereby alleviating the child's inability to hear. (§§59 and 1016 – 2017 U.S. Master Tax Guide) (Publication 502)

E. Transportation

Transportation costs are deductible as a "medical expense" if they are incurred going to and from the following locations:

1. Special schools (as defined by IRS);
2. Institutions and hospitals;
3. Special therapy programs that have been prescribed; or,
4. Pharmacies or drugstores.

Medical transportation costs for taxicabs or other public transportation modes must be verified with proof of all expenditures, such as receipts or canceled checks. The transportation costs to a parent accompanying a sick child to obtain medical care are also deductible. If a parent pays for the transportation costs of a nurse to attend a sick child --- that too is a deductible expense. If a child who attends a special school cannot travel alone, the cost of someone to accompany the child to the special school is deductible. A further deduction is available for persons with physical disabilities who utilize taxicabs to and from work where a physician as part of a therapy program recommended the employment.

The costs of transportation for all of the above by private car are a deductible "medical expense" and include (IR-2010-51; Notice 2016-79; §1016 – 2017 U.S. Master Tax Guide):

1. The rate for 2016 is 19¢, and for 2017 it is set at 17¢;
2. Parking fees; and
3. Tolls.

If your child with a disability lives away from home, transportation costs to visit your child may be deductible as a "medical expense" if medical experts deem your visit a necessary part of treatment. This applies only to transportation costs and not to meals and/or lodging. (Rev. Rul. 58-533; 1958-2 CB 108)

Away-from-home lodging expenses, such as for hospital stays, are deductible up to $50 per night, per person primarily for and essential to medical care provided by a physician in a licensed hospital, including a medical care facility related to or the equivalent of a licensed hospital. This expense is also available to certain eligible persons accompanying the person seeking medical care.

F. Cost of Special Equipment to Alleviate a Disability (Including Installation)

In the examples of elevators for heart patients, air conditioning for persons with asthma, ramps for persons who use wheelchairs, and the like, medical experts must deem the items necessary to alleviate the disabling condition. This deduction is allowed to the extent that it exceeds the improved value of your property [IRC §213]. Example #1: if air conditioning your home improves its value by $700 and the actual cost is $1,000; you are allowed to deduct the difference of $300. If the special equipment does not increase the value of the home, the entire cost is deductible. Example #2: The additional cost to modify a van for a wheelchair lift and raising the vehicle roof is deductible; depreciation of the van is not. *Henderson* v. *Commissioner*, T.C. Memo 2000-321. A 1987 ruling enumerates a listing of special equipment that qualifies for this type of deduction and it indicates which items will not be considered as increasing the value of property (Rev. Rul. 87-106) (§59 – 2017 U.S. Master Tax Guide)

G. Lifetime Care Payments

Non-refundable advance payments to a private institution for lifetime care, supervision, treatment, and training of your dependent with physical and intellectual disabilities in the event of your death, or other inability to care for your dependent, are deductible in the year paid, provided the payments are required as a condition for the institution's future acceptance of your dependent. (Publication 502) (§1015 – 2017 U.S. Master Tax Guide)

H. Aids for Persons with Visual Impairments

Costs of specific aids to assist in the education of a child becoming blind, such as an audio recorder, special typewriter, projection lamp for enlarging written material, and special lenses are deductible as medical expenses because the use of such things mitigates the condition of losing the sense of sight. (Rev. Rul. 58-223, 1958-1 CB 156)

I. Expenses for Patterning Exercises

Amounts paid to a non-professional for administering "patterning" exercises --- coordinated physical manipulation of limbs to stimulate normal movement in a child with an intellectual impairment --- qualifies as deductible medical care expense. (Rev. Rul. 70-170, 1970-1 CB 51)

J. Wages for Nursing Service

Payments of wages for an attendant who provides nursing services are deductible medical expenses. You may also include as medical expenses the out-of-pocket amounts paid for the attendant's meals. Divide the total food expense among the household members to find the cost of the attendant's food. If you have to pay additional out-of-pocket amounts for household up-keep because of the attendant, include as a medical expense the extra amount you paid. This includes such items as extra rent you paid because you moved to a larger apartment to provide space for the attendant or extra cost of utilities for the attendant; if the attendant also provides personal and household services, you must further divide these amounts between the time spent on performing household and personal services. (Publication 502)

K. Special Telephone

The repair cost of special telephone equipment that allows a person who is deaf to communicate over a regular telephone is a medical deduction. (Publication 502)

L. Close-Captioned TV

The extra cost of a specially-equipped television set and the cost of an adapter that provides sub-titles for a person who is deaf are deductible as a medical expense. (Publication 502)

M. Removal of Lead-Based Paint

The cost of removing lead-based paints from walls and woodwork in a home to prevent a child who has lead poisoning or had lead poisoning from eating the paint is a deductible medical expense. The areas covered with lead-based paint have to be in poor repair or be within the child's reach. (Publication 502)

N. Disposable Diapers

Disposable diapers are deductible as a medical expense when verified by a physician as being necessary for a child or adult who is totally incontinent as the result of a neurological disease or brain damage. (Fed. Tax Coord. 2d, K-2192)

O. Expenses Incurred for a Person with an Intellectual Impairment Residing in a Group Home or Other Community Setting

The cost to a person or family of maintaining a person with an intellectual impairment in a specially selected home, to aid in the adjustment from institutional to community living, qualifies as a medical expense and is deductible. (Rev. Rul. 69-499, 1967-2 CB 39) (IRS Publication 502) Please refer to page 14, part "B" of this tax guide for possible SSI and Medicaid considerations.

P. Special Food and Beverages

The IRS has held that the cost of special foods and beverages may qualify as a deductible medical expense if prescribed by a physician for alleviation or treatment of an illness and are in addition to the taxpayer's (or dependent's) normal diet. The special food or beverage must not be a part of the nutritional needs of the patient. But, the Tax Court has allowed as a medical deduction the *additional* cost of special foods or beverages (e.g., Osmolite®, for persons requiring tube feeding) over the cost of a normal diet where prescribed by a physician for alleviation or treatment of an illness. [Randolph (1976) 67 TC 481; Cohn (1962) 38 TC 387 (NA); Rev. Rul. 76-80; Fed. Tax Coord. 2d, K-2138].

Q. Legal Fees

Legal fees and other related costs arising with respect to the commitment for treatment of an individual with a mental health disability at an institution for special care are deductible as medical expenses (Rev. Rul. 71-281, 1971-2 CB 165; distinguished by Rev. Rul. 78-266). You cannot include in medical expenses fees for the management of a guardianship estate, fees for conducting the affairs of the person being treated, or other fees that are not necessary for medical care. (Publication 502)

R. Medical Conferences Attended by Parent

Amounts paid by an individual for expenses of admission and transportation to a medical conference relating to the chronic disease of the individual's dependent is deductible as a medical expense; meals and lodging are not. (Rev Rul. 2000-24).

S. Miscellaneous *

1. Dental care;
2. Eyeglasses, contacts, examinations;
3. Hearing aid; examination, batteries;
4. Wheelchair, braces or other adaptive equipment;
5. Birth control pills;
6. Psychologist fees.

**For a complete listing of available medical deductions, please consult the current edition of IRS Publication 502, or §59 – 2017 U.S. Master Tax Guide.*

TAXABILITY OF SUPPLEMENTAL SECURITY INCOME (SSI)

SSI is **not** taxable for the person receiving the benefit. If the SSI recipient in Michigan is receiving benefits at the Sharing/Independent level ($749.00 for 2017) and is paying his/her "pro-rata share" of the household expenses, then that share is not taxable income to the householder who receives the money. This is true whether the householder is a parent or other relative or an unrelated person. The share is not taxable income because it is merely a reimbursement to the householder for that portion of expenses attributed to the SSI recipient. This situation may be more easily understood by likening it to the situation where four college students share an apartment. Each student is responsible for one-fourth of the household's expenses and no one's individual share is considered as income to anyone else.

In a different set of circumstances, if the SSI recipient is paying either "rent" or "room and board" to his/her parents (or anything else for that matter), then those "rent" or "room and board" payments (minus expenses incurred) are considered income to the parent (or other landlord).

CAN SSI RECIPIENTS BE CLAIMED AS A DEPENDENT?

Any SSI recipients in Michigan who receive benefits at either the Sharing/Independent level ($749.00 for 2017) or Personal Care (adult foster care home or group home) level ($892.50 for 2017) **cannot** be claimed as dependents for income tax purposes. This is because a person on SSI at a rate other than the Household of Another level ($499.33 for 2017) is by SSI regulations defined as someone who is **not** someone else's dependent. If the SSI recipient is claimed as a dependent according to the I.R.S. regulations, then the SSI program will consider such support against the SSI recipient and only the Household of Another level of benefits will be paid.

Adult SSI recipients who receive benefits at the Household of Another level ($499.33 for 2017) may be claimed as dependents by persons who can show that they provided more than half the SSI recipient's support. In figuring total support, the SSI income must be counted. If the yearly total of SSI received is less than the amount of support provided by a parent or another person, the SSI recipient can be claimed as a dependent if all other dependency requirements are met.

SPECIAL NOTE: Michigan provides a monthly state SSI supplement for both the Household of Another and the Sharing/Independent rates. Although recipients of SSI in Michigan will receive a check or a direct deposit from the **federal** government (either $490.00 – Household of Another, or $735.00 – Sharing/Independent) on the first of every month, the State of **Michigan** sends its monthly supplement amount (either $9.33 – Household of Another, or $14.00 – Sharing/Independent) on a quarterly basis included within one state check, or via direct deposit, on March 10th, June 10th, September 10th and December 10th. Individual recipients in Michigan who only qualify for a "state supplement" amount of SSI each month (due to the receipt of other income like Social Security disability benefits, and/or some work earnings) must forego not only this money, but they are required to go through a local Michigan Department of Health and Human Services office (or, on-line) and annually re-apply for Medicaid benefits.

TAXABILITY OF SOCIAL SECURITY BENEFITS

Social Security benefits have the **possibility** of becoming taxable income. This applies to benefits [**not** Supplemental Security Income ("SSI")] received by retired persons, disabled workers, disabled adult children, survivors of deceased workers, or spouses of beneficiaries. In specific terms, up to 50% of Social Security benefits **could** become taxable if combined with other income, such as bank interest, annuities, private pensions, wages, *et cetera*, and the total is more than an adjusted base amount ($25,000 single; $32,000 married filing jointly).

A married couple whose "combined income" is more than $44,000 and single persons with income over $34,000 will pay income tax on up to 85% of their Social Security benefits.

The "combined income" mentioned above is an individual's or married couple's adjusted gross income as reported on the IRS Form 1040, plus one-half (50%) of the total Social Security benefits received for the year, plus non-taxable interest.

For beneficiaries whose income is below the $25,000 or $32,000 levels during 2016, Social Security benefits are not taxed. (§716 – 2017 U.S. Master Tax Guide)

This provision will not affect persons receiving Supplemental Security Income (SSI) benefits or those receiving both SSI and Social Security checks, since substantial outside income will terminate eligibility for SSI benefits long before income levels became taxable (IRS Notice 703, August 1984).

Recipients of Social Security benefits will receive a yearly statement showing the sum of all benefits received during the year. This statement may then be used when figuring taxable income on the worksheet the Social Security Administration will enclose with its mailing.

Any questions should be directed to a qualified tax advisor.

PAYMENTS FROM THE MICHIGAN D.H.H.S.

A. GA, ADC, ENP, SNAP

Someone who has a disability may be receiving payments from Michigan's "Department of Health and Human Services" (DHHS) under General Assistance (GA), Aid to Dependent Children (ADC), Emergency Needs Program (ENP), or the Supplemental Nutrition Assistance Program [(SNAP); a.k.a. "food stamps"], among others. **NONE** of these payments are considered taxable (gross) income to the person with a disability, even if the checks come to a parent or other person as payee on behalf of the person with a disability.

The federal government will consider these payments as **OUTSIDE SUPPORT** for purposes of determining whether parents or another person can claim the person with a disability as a dependent. As with SSI, if a parent or anyone else provides more financial support than the yearly total of any DHHS payment(s) and all other dependency tests are met, then the parent or other person may claim the DHHS payment recipient as a dependent.

B. Independent Living Services Program (Formerly, "Adult Home Help" or "Chore")

NOTE: ***AHHS payments are no longer considered taxable income for parent-caregiver providers of such services. The IRS changed its position at the beginning of 2014.***

Independent Living Services Program ("ILSP") or Adult Home Help Services ("AHHS") payments are provided through the Michigan Department of Health and Human Services ("DHHS") to persons who deliver unskilled and non-specialized service or personal care activities essential to a person with a disabling condition who cannot perform such things without assistance. The goal of the AHHS program is to maintain the person with the disability in his/her natural home instead of in a more costly alternative residential care arrangement.

These "personal care services" are defined by the Centers for Medicare and Medicaid Services as: assistance with eating, bathing, dressing, toileting, transferring, maintaining continence, personal hygiene, light housework, laundry, meal preparation, transportation, grocery shopping, using the telephone, medication management, and money management. Most of these personal care services are also found in the listing of "chores" under Michigan's AHHS rules contained within the DHHS "Adult Services Manual" at §101.

The local area Internal Revenue Service ("IRS") policy until tax year 1990 was that parents could exclude AHHS payments from their gross income each year. However, that stance was eventually reversed by the IRS national office because of a contrary decision from the U.S. Tax Court. In *Bannon v. Commissioner of Internal Revenue*, 99 T.C. No. 3, Docket No. 26900-90 (July 20, 1992), Dorothy Bannon lost her bid to have AHHS payments declared non-taxable income to a parent or relative caregiver. The Tax Court held that under California law, Ms. Bannon's daughter was the welfare recipient under that state's version of AHHS and was "... intended to be the ultimate beneficiary..." of the welfare payments. The parent in this case was employed by her daughter to provide supportive services. Therefore, the AHHS payments were includable in the parent's income for federal income tax purposes.

On January 3, 2014, the IRS issued its Notice 2014-7 addressing the income tax treatment of certain payments to an individual care provider under a state Home and Community-Based Waiver (Medicaid Waiver) program. The notice provides that the IRS will treat "qualified Medicaid Waiver payments" as "difficulty-of-care" payments excludable from gross income under §131 of the Internal Revenue Code. (see also: §883 – 2017 U.S. Master Tax Guide) Accordingly, the IRS stated that it will no longer assert the position of its own "Program Manager Technical Advice" memorandum (PMTA 2010-007) where it held that "*a biological parent of a disabled child may not exclude payments under §131 because the ordinary meaning of foster care excludes care by a biological parent*." For purposes of IRS Notice 2014-7, qualified Medicaid Waiver payments are those issued by a state, a political subdivision of a state, or a certified Medicaid provider under a Medicaid Waiver program to an individual care provider for non-medical support services provided under a plan of care to an individual (whether related or unrelated) living in the individual care provider's home. (see IRS FAQ's at: https://www.irs.gov/individuals/certain-medicaid-waiver-payments-may-be-excludable-from-income)

IMPORTANT NOTE: although the IRS Notice 2014-7 primarily involves the Medicaid Waiver program, it also clearly states that the IRS would no longer apply §131 to the 1992 *Bannon* case decision, which dealt exclusively with the income taxability of AHHS payments.

Until further notice, this is how a parent (or other) live-in caregiver must account on their federal IRS form 1040 (see: page 31 of IRS 1040 2016 Instructions) for the funds from the Michigan W-2 that is received each year for the AHHS payments from the DHHS:

- On line 7 enter the W-2 amount.
- On line 21 enter (on the dotted line) ---- **"Notice 2014-7"** - then enter the W-2 amount with a minus ("-") sign in front of it.

If you received such payments (including AHHS) described in IRS Notice 2014-7 in an earlier year, you may file an amended return via IRS Form 1040X to exclude the payments from gross income. Generally, for a credit or refund, you must file an amended return within 3 years (including extensions) [4 years for Michigan returns] after the date you filed your original return or within 2 years after the date you paid the tax, whichever is later. (see: IRS 1040x Instruction booklet; IRC §6511; and, https://www.irs.gov/individuals/certain-medicaid-waiver-payments-may-be-excludable-from-income)

IRS Notice 2014-7 does not address whether qualified Medicaid Waiver (and/or AHHS) payments excluded from income under this IRS Notice may be subject to tax under the Federal Insurance Contributions Act (FICA) or the Federal Unemployment Tax Act (FUTA) in certain circumstances. There appears to be an arguable position about whether a parent who is the provider/caregiver must pay the FICA at all. In the Federal Tax Advisor; Section 58,655; 1992, Commerce Clearing House, Inc., it states:

> *" . . . services performed by a parent for a child generally are covered employment for FICA purposes and are subject to withholding. However, an exception is provided for domestic services performed by a parent. That is, in most cases, a parent performing services of a household nature in the private home of a son or daughter will not be engaged in covered employment under FICA and will be exempt from withholding."*

On a related area, the same section of the Federal Tax Advisor goes on to state:

> *" . . . services performed by an individual for a son, daughter, husband or wife, and services performed by a child under the age of 21 in the employ of a parent, are specifically excluded from the statutory definition of "employment" under FUTA [("Federal Unemployment Tax Act")]."*

The FICA and FUTA issues are rather complex and the taxpayer is strongly advised to seek professional assistance for individual situations.

Finally, it is important to keep in mind that AHHS payments remain income taxable to third-party caregivers, that is, those who live elsewhere but provide these chore services at the home of the individual with special needs.

FAMILY SUPPORT SUBSIDY (Michigan)

Since 1984, Michigan has had a Family Support Subsidy program that provides monthly payments to qualified families. These are families that have a member who is a special education student with the educational label of either a Cognitive Impairment – Severe (CI-S), Severe Multiple Impairment (SXI) or Autism Spectrum Disorder (ASD), **and** have a taxable income of less than $60,000 on their state of Michigan tax return. Please also note that children with ASD must be receiving special education services in a program that qualifies under the Family Support Subsidy law.

Family Support Subsidy payments ($222.11 per month) are not counted as income for any programs administered by the Michigan Department of Health and Human Services (GA, ADC, ENP, SNAP, etc.), the federal SSI Program, or Michigan Children's Special Health Care Services. Family Support Subsidy payments are also considered non-taxable to parents for both federal and Michigan state income tax purposes. This non-taxability situation results from the payments being considered as those made by a governmental unit. (Michigan Mental Health Code, §R330.1611)

Note: During the 2016 Michigan legislative year, no bill was introduced that would expand the coverage beyond those children having the special educational labels of Cognitive Impairment – Severe (CI-S), Severe Multiple Impairment (SXI), or Autism Spectrum Disorder (ASD).

DISABILITY-RELATED TAX CREDITS

Child and Disabled Dependent Care Credit - If you are among the millions of parents who must pay someone to care for your child or disabled dependent while you earn a living; you may use those same expenses to help reduce your personal income tax liability. This credit was made permanent by the American Taxpayer Relief Act of 2012.

Child and disabled dependent care expenses are handled as a tax credit, instead of a deduction, enabling you to reduce your tax liability by the amount of credit you have coming.

No credit is allowed unless you supply identifying information concerning the service provider on Form 2441. This credit must be claimed by using either Form 1040 or 1040A. If you cannot obtain this information, then attach a statement to the form describing your good faith efforts to do so. The IRS will probably allow the credit.

To be eligible for the credit, the taxpayer must maintain a household for one of the following individuals:

1. A dependent under age 13 for whom a dependent exemption may be claimed;

2. Any other dependent that is physically or mentally incapable of self-care. The taxpayer must be able to claim either (a) the person as a dependent, or (b) the person as a dependent except for the fact that the person had income exceeding the exemption amount; or

3. The taxpayer's spouse if he or she is physically or mentally incapable of self-care.

The Working Families Tax Relief Act of 2004 changed the relationship, support and residence requirements for a qualifying child and a dependent (see: Page 8). The residence and/or disabled individuals and spouses incapable of self-care rules, now only require that they have the same principal place of abode as the taxpayer for more than half of the taxable year.

Qualifying expenses include expenses paid for household services and for the care of a qualifying individual. Services outside the home qualify if concerning the care of a child under age 13 or a disabled spouse or dependent that regularly spends at least 8 hours a day in the taxpayer's home.

The credit is equal to 35% of *employment-related expenses* for taxpayers with adjusted gross income (AGI) of not more that $15,000 and is 20% for taxpayers with AGI of more than $43,000. For taxpayers between these two amounts, the credit is reduced one percentage point for each $2,000 or fraction thereof of adjusted gross income in excess of $15,000. The maximum amount of *employment-related expenses* to which the credit can be applied is $3,000 if one qualifying child or dependent is involved and $6,000 if more than one is involved.

A married taxpayer generally must file a joint return to claim the credit. For married taxpayers, expenses are limited to the earned income of the spouse earning the lesser amount. Income limitations affect the percentage and amount of credit allowed. Usually, if one spouse is not working, no credit is allowed. If the non-working spouse is physically or mentally incapable of self-care or is a full-time student for at least five months during the year, then the law will assume an earned income --- for each month of being disabled or going to school --- of $250 per month if there is one qualifying child or dependent or of $500 per month if there are two or more qualifying individuals. (§1301 – 2017 U.S. Master Tax Guide)

Work Opportunity Tax Credit – Originally a part of the Small Business and Work Opportunity Tax Act of 2007 (P.L. 110-28), this important law may be elected by employers who hire individuals from within certain targeted groups (for example, those with a disability). It is based on first-year wages paid to these eligible workers. The credit was expanded in 2007 to include hiring disabled veterans and individuals living in counties experiencing population losses.

NOTE: The "Protecting Americans from Tax Hikes Act of 2015" extended this credit through 2019. (see: Wolters Kluwer/CCHGroup "Tax Briefing" dated 12/18/15)

The deduction for such wages must be reduced by the amount of the credit, and is computed on Form 5884 ("Work Opportunity Credit"). No credit is allowed for wages paid to an individual for services rendered at the employer's plant or facility that is substantially similar to services performed by employees who are participants in a strike or who are affected by a lockout.

The credit is 40% of the first $6,000 ($3,000 for qualified summer youth employees) of wages paid to a "targeted group" member during the first year of employment and 25% in the case of wages attributable to individuals meeting only minimum employment levels.
Included among the "targeted groups:" ... a "vocational rehabilitation referral;" a "qualified food

stamp recipient;" or a "qualified SSI recipient." The minimum employment periods include individuals who began work for an employer after 9/30/1996 and before 1/1/2019 - the employee must have completed a minimum of 120 hours of work. The hour-of-service test is the only measurement for a minimum employment period for Work Opportunity Tax Credit purposes. If the 120-hour test is met, an employer is entitled to a credit of 25% if the employee performs less than 400 hours of service. For 400 or more hours of service, the percentage is 40% of the employee's wages. (§1365G – 2017 U.S. Master Tax Guide)

Disabled Access Credit - An eligible small business is entitled to this non-refundable tax credit for costs incurred to make a business accessible to disabled individuals. The credit amount is 50% of the amount of eligible access expenditures for a year that exceed $250 but that do not exceed $10,250. The credit is computed on Form 8826. (§1365M – 2017 U.S. Master Tax Guide)

Low-Income Housing Credit - A non-refundable income tax credit is available on a per-unit basis for low-income units in qualified low-income buildings of qualified low-income housing projects. Calculate the credit on Form 8586 and claim it as a part of the general business credit. An owner must utilize an enforceable 30-year low-income use agreement with the appropriate housing agency. Credits are allowed to both profit and non-profit ventures.
[IRC §42] (§1365K – 2017 U.S. Master Tax Guide).

Credit for Persons Who Are Elderly or Who Are Permanently Disabled - A 15% tax credit that applies to persons who are either 65 years of age or older, or who are under age 65, retired on disability, and were totally and permanently disabled when they retired. An individual is considered permanently and totally disabled for credit purposes if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or to last for a continuous period of not less than 12 months. The credit is computed on Schedule R. [IRC §22] (§1302 – 2017 U.S. Master Tax Guide)

DEPENDENCY AND SHELTERED WORKSHOP SCHOOL INCOME

Income derived at a sheltered workshop school by an individual who is permanently and totally disabled is to be disregarded in determining that individual's status as a dependent.

No dependency exemption is available for a student who has attained age 24 at the close of the calendar year unless the student's gross income for the year is less than the exemption amount ($4,050 in 2016). (§§137A and 143 – 2017 U.S. Master Tax Guide)

Your individual tax advisor can assist you if there are any questions regarding what is a qualifying "sheltered workshop school" or "student." Also, please note that SSI and Medicaid rules may differ from those of the IRS when earned income is involved.

DEDUCTION FOR "IMPAIRMENT RELATED WORK EXPENSES"

Expenses of an individual with a disability for attendant care services at his place of employment, other expenses in connection with his place of employment that are necessary for the individual to be able to work, and all ordinary and necessary expenses paid or incurred during the tax year in carrying on any business, are not subject to the two-percent (2%) floor that applies to miscellaneous itemized deductions. Persons with a disability include any individuals who have a physical or mental disability (including blindness or deafness) that limits employment or who have any physical or intellectual impairment (including sight or hearing impairments) which substantially limits one or more major life activities. [IRC §67(d); IRS Publication 502]

AMOUNTS EXPENDED BY STATE FOR TRAINING, EDUCATION, ROOM AND BOARD ARE NOT "SUPPORT" - DEPENDENT EXEMPTION AND DEDUCTION IS AVAILABLE

- **REV. RUL. 59-379**
- **REV. RUL. 60-190 (modified by Rev. Rul. 61-186)**
- **REV. RUL. 71-347**
- **§147 – 2017 U.S. Master Tax Guide**

While contemplating the following, please note that IRS rules differ from those of the SSI and Medicaid Program. The level of SSI benefits may determine one's status as a dependent. (See page 18 of this tax guide.)

For persons with an intellectual impairment residing in an institution where education and/or training is being provided to the individual, the amount furnished by the state for room and board and education is considered a "scholarship" and excluded from the computation of support for that individual. However, parents who may be paying for incidentals (clothing, toiletries, education, medical and dental care, gifts, transportation, church contributions and entertainment and recreation) may still claim their child as a dependent, allowing a deduction, if more than one-half of the year's total support for that dependent child was paid by the taxpayer.

The current ruling on exemptions for dependents who are persons with an intellectual impairment extends an earlier ruling that held that the cost of room and board for dependents who reside in an institution for persons with an intellectual impairment may be considered a scholarship grant that will not be taken into account in determining whether the parents have provided more than one-half of his/her support. The extension no longer limits such care to state institutions, and includes all who are persons with an intellectual impairment regardless of age.

The actual ruling reads as follows: "Revenue Ruling 64-221, DB 1964-2, 46 amplifies the earlier ruling (61-186-CB 1961-2, 30) which refers to the status as 'students' under section 151(e)(4) of the Internal Revenue Code of 1954, of handicapped children who are placed for purposes of education and training in a state institution which specializes in the care, treatment, education and training free of charge, of minor children who are severely handicapped both physically and mentally. However, the principles therefore are not necessarily restricted to state institutions."

"Therefore, where any institution for persons with mental retardation or division thereof, which qualified as an educational institution under section 151(e)(4) of the Code, accepts any individuals for purposes of education and training and certifies that it is making an effort to educate or train him/her to use his/her faculties to the extent that he/she is physically or mentally able to do so, the individual will qualify as a student under section 151(e)(4) of the Code - regardless of age, the education or training received or the extent of his disability. If such certification is made, the amounts expended by the institution for room and board and tuition of the individual will be taken into account in determining whether such an individual received more than one-half of his support from his parents or step-parents for the purpose of determining exemption for dependents for Federal income tax purposes."

NOTE: *Consult with your tax advisor to determine whether specific institutions in your state qualify for the dependency exemption explained above. Keep in mind that there may also be negative implications relative to Supplemental Security Income (SSI) and/or Medicaid eligibility should this exemption be used.*

WORKING SSI/SSDI RECIPIENTS: TO FILE OR NOT TO FILE?

As more persons receiving SSI/SSDI benefits begin to work, families should determine whether a federal income tax return must (or may) be filed. Refer to the exemption amount and standard deductions portions of the Tax Change Highlights to help determine if the federal return **MUST** be filed. If a federal filing were not required, it would be desirable only if the worker would be due a refund of any federal tax withheld from 2016 wages, or a child tax credit refund.

Even if federal filing is not done, families should consider filing State of Michigan tax returns if there is the likelihood of a refund due because of a **Homestead Property Tax Credit** or **Home Heating Credit** (each is potentially available to renters as well). Consult your tax advisor to assure that your family and any member who is a (working) recipient of SSI or Social Security benefits are receiving all the credits to which you may be entitled.

FOSTER CARE PROVIDERS

Foster parents can exclude from income qualified reimbursements of their expenses for caring for foster children under the age of 19 who are placed in their home by a government agency, a tax-exempt child placement agency, or a placement agency that is licensed or certified by a state to make foster care payments. They can also exclude "difficulty-of-care" payments paid to care for children with disabilities, up to a maximum amount of payments for ten children. Foster parents do not have to keep records of all expenses for each child.

An exclusion from income for foster care payments (including difficulty-of-care payments) includes payments for foster care individuals age 18 and over. These individuals must have been placed in the foster care provider's home by a government agency. The exclusion applies only to payments (including difficulty-of-care payments) for up to five individuals age 18 or older.

A key provision of the "Job Creation and Worker Assistance Act of 2002" (P.L. 107-147) expanded the exclusion beyond only a state agency or a tax-exempt child placement agency making such payments to also include payments made by a placement agency that is licensed or certified by a state to make foster care payments.

In summary, most foster care providers, for children and/or adults, can exclude from their income the foster care payments that they receive (including difficulty-of-care payments) with the above-stated limitations and with no record-keeping of expenses. This DOES NOT apply to corporation-operated group homes.

(LTR-RUL 200039006 of June 8, 2000) [IRC §131] (§883 – 2017 U.S. Master Tax Guide)

PROPERTY TAX CREDIT - MICHIGAN

Persons living in rental situations, including residents of Adult Foster Care Homes, are eligible to file for Michigan's refundable Property Tax Credit based on the portion of property taxes they pay in their rental (or AFC) payment. Instructions for filing are in Michigan's **2016 Income Tax Return and the Homestead Property Tax Credit Claim** booklets, which is available on-line at *www.michigan.gov/taxes*. It contains specific reference to Adult Foster Care residents.

ADOPTION SUBSIDY & EXPENSES CREDIT

The State of Michigan has an "adoption subsidy" program that pays for many "non-recurring" adoption expenses in connection with adopting a child with special needs. Also, the state provides a non-taxable monthly financial stipend to adoptive families, along with limited medical coverage for qualifying children.

Michigan in the past offered a refundable "Qualified Adoption Expenses Credit," spanning tax years 2001 through 2011, for excess adoption expenses. This credit is no longer available to Michigan taxpayers.

On 2016 federal returns, qualified adoption expenses and fees (including those of an attorney) may be claimed as a non-refundable "tax credit" (not a "tax deduction"). The maximum credit is $13,460 ($13,570 for 2017), and the phase-out range begins for taxpayers with a Modified Adjusted Gross Income of $201,920 ($203,540 for 2017), with no credit allowed for taxpayers with a modified adjusted gross income (AGI) over $241,920 ($243,540 for 2017). If the child is one with special needs, the full amount of the tax credit is allowed regardless of actual expenses paid or incurred in the year the adoption became final.

Employers are allowed to offer a fringe benefit for payment of qualified adoption expenses. The American Taxpayer Relief Act of 2012 extended permanently the Bush-era enhancements to the adoption credit and the income exclusion for employer-paid or reimbursed adoption expenses up to $13,460 ($13,570 for 2017) --- identical to the maximum credit listed above; and is indexed for inflation --- both for non-special needs adoptions and special needs adoptions. However, any expenses incurred in excess of the amount provided under an employer's adoption assistance program may be used to claim the adoption credit.

An eligible child is an individual not yet 18 years of age as of the time of the adoption or who is physically or mentally incapable of providing self-care. To qualify as a child with special needs, the child must be a citizen or resident of the United States.

(Rev. Proc. 2009-50; 2015-53; and 2016-55) (§1307 – 2017 U.S. Master Tax Guide)

ACHIEVING a BETTER LIFE EXPERIENCE ACT ("ABLE ACT")

The ABLE Act arose from the federal "Tax Increase Prevention Act of 2014." It creates tax-favored savings accounts for individuals with disabilities for tax years beginning after December 31, 2014. The ABLE Act authorizes states to create an ABLE Act program (similar to the Internal Revenue Code §529 college savings programs). (see: IRC §529A)

Qualified distributions include amounts used to cover medical expenses as well as costs of education, transportation, housing, employment support, health and wellness, training, assistive technology, personal support, and much more. Another key component of the ABLE Act provisions is that the placing of funds into such an account would not disqualify the individual with a disability from most state or federal aid, for example, Medicaid or SSI. Distributions used for non-qualified expenses would be subject to income tax on the portion of the distributions attributable to earnings from the account, plus a 10% penalty.

Individuals with disabilities are limited to only one ABLE Act account; and the total annual contributions by all individuals to any one ABLE Act account could be made up to the gift tax exclusion amount. For 2016 and 2017, the gift tax exclusion amount is $14,000. Further, such an account is capped at $100,000 according to the federal guidelines.

NEW: The **Michigan ABLE Act** was signed into law on October 28, 2015, made effective January 26, 2016, and went fully operational on November 1, 2016. It created this new savings program under the authority of Internal Revenue Code Section 529A, which is aimed at encouraging and assisting individuals and families to save private funds to support individuals with disabilities. A deduction may be taken on the Michigan income tax return for contributions made to an ABLE account to the extent included in Adjusted Gross Income (AGI). The maximum deduction is $5,000 for a single filer ($10,000 for a jointly filed return). The amount deducted includes total contributions made to the plan less qualified withdrawals made during the tax year. Distributions from the account must be used to pay for qualified disability expenses of the eligible designated beneficiary of the account. The program is administered by the Michigan Department of Treasury and will be similar to that office's administration of higher education savings accounts ("529 Plans"). For more detailed information, go to: **www.MIABLE.org**.

(Sources: ♦ Wolters Kluwer CCH, Inc. "Tax Briefing" Special Report dated 12/16/14; and ♦ blog by financial planner, Michael Kitces, at https://www.kitces.com dated 12/17/14); and ♦ Autism Society of the U.S. e-mail notice dated 12/17/14). ♦ Michigan Treasury "New Developments for Tax Year 2016 [http://www.michigan.gov/treasury]. (§§131 and 870 – 2017 U.S. Master Tax Guide)

APPEAL RIGHTS

From time-to-time some taxpayers are selected for auditing. During an audit, the IRS examiner may propose certain changes to the return(s) as filed. If you don't agree with the proposed changes of the examining officer and the examination was made in an Internal Revenue Service office, you may request an immediate conference with a supervisor and explain your position.

Except in an unusual circumstance, such a conference will be granted. If an agreement is reached at this conference, your case will be closed. If agreement is not reached at this conference, or if the unagreed examination was made outside of an Internal Revenue office, you will receive: (1) copy of the examination report explaining proposed adjustments, and (2) a transmittal letter detailing the further appeals available to you and giving you 30 days to respond.

The "Technical and Miscellaneous Revenue Act of 1988", the "1996 Taxpayer Bill of Rights 2" (P.L. 104-168), and the IRS Restructuring and Reform Act of 1998 (P.L. 105-206) provide many safeguards against I.R.S. abuses of tax collection procedures. See your tax advisor for details.

APPEAL WITHIN THE SERVICE

The Internal Revenue Service now has a single appeal level. Your appeal from the findings of the examiner is to the Appeals Office in the region. Conferences are conducted as informally as possible.

If you want an appeal conference, address your request to your district director in accordance with the transmittal letter sent to you by the Internal Revenue Service in the transmittal letter concerning your tax case.

You may represent yourself at an appeals conference. You may also engage an attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service to represent your interests.

LETTER RULINGS

If your particular tax situation is unique or a "close call," it may be advantageous to secure the opinion of the Internal Revenue Services (IRS). This may be done by mail. Your tax professional will have detailed procedures, but the <u>regular U.S. mail</u> address for obtaining such "Letter Rulings" is as follows:

Internal Revenue Service
Ruling Request Submission
ATTN: CC:PA:LPD:DRU
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

If you use a <u>private delivery service</u> (e.g., FEDEX or UPS), the address is as follows:

Internal Revenue Service
Ruling Request Submission
ATTN: CC:PA:LPD:DRU, Room #5336
1111 Constitution Ave., NW
Washington, D.C. 20224

There is a “user” fee that must be paid to IRS when submitting a Letter Ruling Request. A taxpayer may submit a user fee request for a standard fee of $9,800 made before 2/1/17 ($10,000 after 2/1/17).

This fee is reduced to $2,200 if submitted before 2/1/17 ($2,400 after 2/1/17) for individuals, trusts and estates that report less than $250,000 of income on a federal tax return (as amended) for the last tax year ending before the date the Letter Ruling request is filed.

For those taxpayers reporting more than $250,000 but less than $1,000,000 of income, the fee is $6,500 if submitted prior to 2/1/17 ($7,600 after 2/1/17)

[Please refer to: IRB/Rev. Proc. 2017-1, at Appendix (A)(3)(c), and (A)(4)(a) and (b)]

ADDITIONAL TAXPAYER PROTECTIONS

As a result of the Internal Revenue Service Restructuring and Reform Act of 1998 (P.L. 105-206), taxpayers have additional protections and rights. Examples include: (1) a re-organization of the IRS into units serving groups of taxpayers with similar needs rather than by geographic region; (2) appointment of a “National Taxpayer Advocate” who reports directly to the Commissioner of the IRS, and who directs independent Local Advocates; (3) possible civil damages up to $100,000 if an IRS employee negligently disregards the Tax Code or regulations; (4) notice and right-to-hearing requirements when the IRS files property liens; and (5) the statute of limitations on refund claims may be tolled during any period in which financially disabled taxpayers with determinable medical or physical impairments are unable to manage their financial affairs due to such impairments.

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2017 Income Tax Guide prepared for persons supporting children and/or adults with intellectual impairment and/or related developmental disabilities.