

# Client Bulletin

Smart Tax, Business & Planning Ideas *from your Trusted Business Advisor*<sup>SM</sup>

## Be Sure About Rental Car Insurance

July 2014



This summer, whether you're driving for business or pleasure, you may want to rent a car. If so, you'll likely be driving an unfamiliar vehicle on unknown roads. What's more, you'll encounter other (perhaps many other) motorists in similar circumstances. You can't overlook the chance you'll be involved in an accident.

Obviously, your first priority is to avoid injuring yourself, your passengers, and any others. Still, you'll also want to minimize your financial exposure, so it will pay to have the right insurance in place.

### Protection begins at home

Your first line of defense lies in the coverage you already have. Check your auto insurance policy and your excess liability (umbrella) policy to see what—if anything—they say about rental cars.

Call your insurance agent to double check. If there is coverage, see if there are exclusions for rental cars. Does the coverage apply to long-term rentals or to rentals in a foreign country you may be visiting? If traveling for business, ask how that affects your coverage.

If you feel your coverage is inadequate, your agent might be able to offer you additional insurance for car rentals. Weigh the added cost versus the extra protection you'll get. Remember, your greatest exposure might be liability, if you injure someone while driving the rental car.

After discussing your plans, send an email to the agent, summarizing the conversation, and have the agent respond, so you'll have a record of what you were told.

### Credit check

Besides your existing policies, you also may have coverage from your credit card issuer.

**Example 1:** Howard Green rents a car and puts the charge on his Visa card. He skids off the road in a rain storm and causes extensive damage to the vehicle. Some or all of the repair costs may be covered by Visa. Indeed, if Howard has to pay a deductible amount under his personal auto insurance policy, his credit

*continued on page 2*

## What's Inside

- 1 Be Sure About Rental Car Insurance
- 2 Deductions for Dining Out
- 4 Tax-Free Income From Renting Your Home
- 4 Tax Calendar

## Stocks on the Up-And-Up

*The 32.4% gain posted in 2013 by large-company U.S. stocks was the steepest rise since a 33.4% rise in 1997, which was followed by two more excellent years and a three-year bear market.*

card coverage may reimburse him for the outlay. In some cases, credit card insurance can provide secondary coverage, paying claims beyond the limits of your primary auto insurance policy.

Again, it pays to read the fine print. To determine what a given credit card will pay, enter the full name of the card and “rental car insurance” into an Internet search engine, such as Google. Be sure to be precise in designating the type of card you have (gold, platinum, etc.) because different cards from the same company may have different levels of protection. With Visa or MasterCard, there can be variations in coverage from one issuing bank to another.

Credit card coverage can be valuable, especially if it’s included in the basic card member services at no extra charge, but it probably is not absolute. Often, this insurance applies to vehicle damage or theft, but not liability for injuries. In

such cases, be sure you have other protection for any liability incurred while driving a rental car.

Be wary of any exclusions in the coverage you receive from your credit card company. Coverage might not be available, for instance, for rentals of recreational vehicles, rentals of very expensive vehicles, rentals by students, or rentals much longer than 15 days.

The bottom line is that you almost certainly will use a credit card when you rent a car. You might as well see which of your cards has the best suite of free car-rental benefits, in sync with your auto insurance, and use that card when you rent a car.

### Counter moves

When you rent a car, the person behind the counter will ask you if you want the optional insurance offered by the company. The stated cost—often X dollars per day—may seem modest but in fact the annualized costs generally are much

greater than you’d pay for standard auto insurance.

Why would you pay for this expensive coverage? If you haven’t fully researched your insurance options, you might want to buy some coverage from the car rental company, for peace of mind. Alternatively, if you are informed about your present coverage, you might choose some of the optional choices to fill in any gaps.

**Example 2:** Mindy Carter lives in New York City without a car, so she has no auto insurance. When she goes away on weekends, she rents a car. Mindy knows that her credit card covers damage and theft but not liability for injury to others. Therefore, she buys liability insurance at the car rental counter.

Similarly, drivers with little or no collision damage coverage on their personal cars might buy this insurance from the rental company. ■

## Deductions for Dining Out

Champagne and caviar on the IRS? Typically, the answer is no. Nevertheless, there are times when you can go out to eat—perhaps to the best restaurant in town—and recoup some of your costs through tax savings.

### Business as usual

Perhaps the most obvious way to deduct dining costs is to buy a meal for someone with whom you do business or would like to do business. The good news is that everything counts: food, drinks, tax, and tip. The bad news? Meal costs typically are considered entertainment expenses, which generally have a 50% cap on deductions.

**Example 1:** Nora Peters has dinner with a potential client for her landscaping business. They both have

full-course meals with wine, and the tab comes to \$100 with tax and tip. If Nora pays the bill, she can take a \$50 tax deduction.

The IRS explicitly frowns on so-called “taking turns” deductions. Thus, if the potential client is Nora’s neighbor and they dine together every month, alternating as to who pays the bill, the IRS won’t allow either party to take tax deductions.

However, that may not always be the case.

**Example 2:** Nora and her neighbor dine together throughout



the year, discussing possible ideas for the latter’s garden, and Nora picks up the tab every other time, paying a total of \$600. Eventually, the neighbor hires Nora to landscape her garden; Nora ultimately earns \$2,000 from that job, reported as taxable

income. Can Nora take a \$300 (50% of \$600) tax deduction, despite the alternate bill paying? Our office can help you determine the answer to such difficult questions.

### Beyond reasonable doubt

The IRS also asserts that meal outlays that are “lavish or extravagant” won’t qualify for a tax deduction. Unfortunately, the agency doesn’t provide a dollar limit or any tangible guideline, only that the cost must be “reasonable,” considering the “facts and circumstances.” Merely dining at a deluxe restaurant or a pricey resort won’t automatically rule out a 50% deduction.

One way to approach this issue is to put things into perspective. In a major city with a steep cost of living, spending \$100 on a dinner for two may not be considered lavish, if there’s a valid business purpose for the excursion. Conversely, spending hundreds of dollars on a meal with someone who has only a peripheral connection to your company and little chance of providing meaningful revenues in the future, might not pass muster.

One U.S. Commerce Department website provides an example of spending \$200 for a business-related meal. If \$110 of that amount is not allowable because it is lavish and extravagant, the remaining \$90 is subject to the 50% limit. Thus, the tax deduction could be \$45 (50% of \$90).

### Going solo

You should be aware that the 50% limit also applies to business meals away from home, not just to meals where you’re entertaining someone.

**Example 3:** Ron Sawyer travels from his Dallas home to Tucson on a sales trip. He does no entertaining but spends \$140 eating his meals in restaurants. Ron’s meal deduction is \$70 (50% of \$140).

### Filling out a foursome

Generally, you can’t claim a 50% deduction for buying your spouse a meal. There are exceptions, though, if including your spouse at the table serves a business purpose, rather than one that’s personal or social.

**Example 4:** Tim Walker invites a customer to dinner. The customer is visiting from out of town, so the customer’s spouse is also invited because it is impractical to entertain the customer without the spouse. Tim can deduct 50% of the cost of the meal for the customer’s spouse. What’s more, if Tim’s wife joins the group because the customer’s spouse is present, the cost of the meal for Tim’s wife is also deductible.

### Taking the deduction

For self-employed individuals and business owners, taking 50% deductions for business meals may be straightforward. For employees, though, those deductions might be harder to obtain. Unreimbursed expenses are included in miscellaneous itemized deductions, which are deductible only to the extent they exceed 2% of adjusted gross income (AGI).

**Example 5:** Lynn Knox, who is an employee, spends \$500 on business meals in 2014 and is not reimbursed. When she prepares her tax return for the year, she includes \$250 as a miscellaneous itemized deduction. Her AGI is \$100,000, so her 2% threshold is \$2,000. If Lynn’s miscellaneous deductions add up to \$2,400, she is entitled to deduct the \$400 excess. Without her business meals, Lynn’s miscellaneous deductions would have been only \$2,150, generating a \$150 deduction, so Lynn effectively gets a \$250 deduction for her \$500 of business meal expenses. If Lynn’s miscellaneous deductions were under \$2,000, she would have no tax benefit from her business meals. ■

## Trusted Advice

### Meal Plans

- In order to support a deduction for buying someone a meal, you must be present.
- The purpose of the meal must be the active conduct of business, you must engage in business during the meal, and you must have more than a general expectation of getting income or some specific business benefit in the future; or the meal must be associated with the active conduct of business and come directly before or after a substantial business discussion.
- You should keep a record of all these meal expenses. Note the “who, where, when, and how much” details along with an explanation of the business purpose of your mealtime conversation.

## Did You Know?

**T**he average cost for nursing-home care in the U.S. has climbed by 20% in the past five years, to \$95,706 per year from \$79,935. Of the five markets with average fees over \$150,000 a year, four are in New York and Connecticut, led by Bridgeport-Stamford-Norwalk, Conn., at \$159,359. The other is Anchorage, Alaska, in second place with annual costs of nearly \$157,000.

Source: New York Life

# Tax-Free Income From Renting Your Home

From Canton, Ohio, where the Pro Football Hall of Fame Weekend takes place in August, to Los Angeles, which has Haunted Hayrides to celebrate Halloween throughout October, cities small and large host special events throughout the year. Moreover, oceanfront communities attract millions of tourists in the summer while mountain regions offer winter sports each winter.

What is the common denominator? If you live in an area popular with tourists, for a season or a month or even a day, you can rent your home for a sizable amount. According to some reports, homes in the Augusta, Georgia area rent for as much as \$20,000 for the week of the Masters Golf Tournament in April.

Moreover, income from such rental activity is legitimately tax-free: you don't have to report it on your tax return. You can't deduct any expenses incurred for the rental, but you still can take applicable mortgage interest and property tax deductions for your home with no reduction for the profitable rental period.

## Fortune's fortnight

As you might expect, you have to clear some hurdles to qualify for

this tax-free income. Perhaps most important, you must rent the home for no more than 14 days during the year. If you go over by even one day, tax-free taxation will vanish. In that case, you will have to report your rental income, and you may take appropriate deductions, but the process can become very complicated.

In addition to the 14-day limit, the IRS says that you must use the "dwelling unit as a home." This means that you must use the property for personal purposes more than (a) 14 days or (b) 10% of the days it is rented to others at a fair price, whichever is greater.

**Example 1:** Jan Harrison lives in Charlotte, North Carolina, throughout the year but rents her home for a week when the Bank of America 500 race is in town. She moves in with her sister and then goes home after the weeklong rental ends. Jan lives in her home well over 300 days in the year, so claiming the tax-free rental income won't be a problem.

You also can claim this tax break for a vacation home as long as there are at least 15 days of personal use and you keep rentals under 15 days a year. With either a primary residence

or a second home, keep careful records to show that you observed the 14-day rental limit.

## Proceed prudently

Tax-free income is certainly welcome, but it shouldn't be your only concern. Keep in mind that you are letting other people occupy your home, perhaps during a time when parties may occur. Make sure you have a formal rental agreement in place and that you collect the rent upfront, along with a deposit for possible property damage. Check with your homeowners insurance agent to see if you need special coverage, and check with local officials to find out if you need a permit for a short-term rental.

If you decide to use a service to handle the rental and save you some aggravation, ask what fees you'll owe. In addition, ask if the rental income will be reported to the IRS. Such reports may complicate what can be a straightforward tax benefit; our office can explain the possible problems and solutions. ■

## TAX CALENDAR

### JULY 2014

#### July 15

**Employers.** For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in June if the monthly rule applies.

#### July 31

**Employers.** For Social Security, Medicare, and withheld income tax, file Form 941 for the second quarter of 2014. Deposit any undeposited tax. If your tax liability is less than \$2,500, you can pay it in full with a timely filed return. If you deposited the tax for the quarter in full and on time, you have until August 11 to file the return.

For federal unemployment tax, deposit the tax owed through June if more than \$500.

If you maintain an employee benefit plan with a calendar year-end, file Form 5500 or 5500-EZ for calendar year 2013.

### AUGUST 2014

#### August 11

**Employers.** For Social Security, Medicare, and withheld income tax, file Form 941 for the second quarter of 2014. This due date applies only if you deposited the tax for the quarter in full and on time.

#### August 15

**Employers.** For Social Security, Medicare, withheld income tax, and nonpayroll withholding, deposit the tax for payments in July if the monthly rule applies.