

Dear Client:

The recent tax reform added new tax code Section 67(g), which states, “No miscellaneous itemized deduction shall be allowed for any taxable year beginning after December 31, 2017, and before January 1, 2026.”

Holy moly!

John is a W-2 mortgage banker paid on a commission basis, and during 2018, he will incur \$27,000 of employee business expenses. His 2018 tax deduction for his employee business expenses will be zero. How do you think John will feel?

Before the recent tax reform, employees were already getting the short end of the stick when it came to business expenses. Why? The alternative minimum tax (AMT) did not allow tax deductions for employee business expenses, so those employees who had to pay the AMT were granted no business deduction tax benefits.

Of course, not all employees suffered the AMT. Those who did not suffered simply a 2 percent of adjusted gross income floor on deductions that fell into the miscellaneous itemized deduction category.

All of this was bad, but it was NOTHING compared to ZERO business deductions—period. Getting a zero deduction for your legitimate business deductions is absolutely unfair. Is it possible that you can get even?

Maybe.

Let me tell you the story of Dan Butts.

Dan Butts, an Allstate insurance agent, paid almost \$10,000 more in federal income taxes than his State Farm counterparts did because Allstate treated him as an employee. State Farm treated its agents as independent contractors.

In other words, with exactly the same income and the same tax deductions as a State Farm agent, Butts, the employee, paid \$10,000 more in federal income taxes than a State Farm independent contractor agent did, for only ONE reason—the AMT does not allow a penny in deductions for business expenses.

Butts, with the heart of a lion, decided that he was not going to take this AMT unfairness lying down. He took on the system. He amended his tax return and put his W-2 employee commission income on Schedule C. He then subtracted his business expenses from this Schedule C income just as the State Farm agents did, and presto, he saved almost \$10,000 in taxes.

The IRS immediately noticed that Butts had put his income and expenses on the wrong tax form. After discussions, the IRS sent Butts a notice of deficiency stating that it wanted the almost \$10,000 in taxes.

Butts said, “Forget it!” He took the IRS to court and won.

This was no ordinary case. Allstate had treated Butts as a W-2 employee from the time he started to work for them almost 20 years before. He was happy with this employee arrangement; happy, that is, until lawmakers enacted the Tax Reform Act of 1986 and applied the AMT to his employee business expenses, which hammered his business deductions right out of his tax return.

In this case, the court granted Butts independent contractor status even though Allstate Insurance

- paid him on a W-2,
- compensated him for vacation days,
- covered him with pension benefits,
- matched his 401(k) contributions,
- paid 75 percent of his health insurance,
- paid his insurance licensing fees,
- paid part of his group life insurance costs, and
- provided him with errors and omissions malpractice insurance coverage.

The court ruled for Butts because he had a “risk of loss” in his sales activities, and that made him just like other independent contractor agents.

It’s possible you can have facts that line up with those of Butts or another taxpayer who won status as an independent contractor despite being paid on a W-2.

If you think you could be one of these fortunate ones, let’s spend some time examining your facts to see if we might have a good case. My direct line at the office is [603-296-7547](tel:603-296-7547).

Sincerely,

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