



T. Dennis Connally Financial Consultants, Inc.



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IRS Recognizes Obesity as a Disease; Medical Expenses for Weight-Loss Programs Now Deductible



With the addition of obesity to the types of diseases recognized by the IRS, taxpayers can jump-start their health while receiving tax breaks at the same time. The IRS will allow taxpayers to take medical deductions for the costs of certain weight-loss programs. However, the traditional prohibitions on deducting weight-loss costs must be rooted in a diagnosis of obesity or related to another recognized disease.

- The costs of weight-loss programs now join the list of medical expenses that are deductible, such as certain costs to help individuals stop smoking as well as costs for lodging and meals at the lo-

cation where an individual receives medical treatment (this includes alcoholism or drug addiction treatment, where often an individual must travel away from his or her home in order to obtain treatment).

- The costs of weight-loss programs, like other qualifying medical expenses, are deductible only if they are out-of-pocket, uncompensated expenses and the amount of such costs that can be deducted is in excess of 7.5 percent of a taxpayer's adjusted gross income.

Past Policy

The new ruling is a significant departure from past practice. Despite lobbying by many advocacy and health organizations, the IRS did not recognize obesity as a disease.. Taxpayers could only deduct the costs of weight-loss programs if the programs were in conjunction with treatment for another disease. If the weight-loss program was merely to improve an individual's general health or appearance, its cost was not deductible. Under the new policy, the costs of a weight loss program for the purpose of treating

obesity in and of itself are deductible. The IRS will treat obesity as a disease.

Examples

The IRS explained the mechanics of the new policy by examples. In the first example, the taxpayer has been diagnosed by a physician as obese. In the second example, the taxpayer, who is overweight but not obese, has been diagnosed by a physician as having hypertension and has been directed by the physician to lose weight.

Both taxpayers can deduct their weight-loss programs' related costs under Internal Revenue Section 213, but only to the extent they are not compensated or reimbursed by insurance or otherwise. However, the cost of purchasing reduced-calorie diet foods is not deductible since they are substitutes for those normally consumed satisfying their nutritional requirements.

- The above examples can be distinguished from the facts in a previous IRS ruling—Revenue Ruling 79-151—

where the taxpayer participated in a weight-loss program only to improve general health and appearance, and was not suffering from any specific ailment or disease. In that case, the costs of the weight-loss program were not deductible as a medical expense under Internal Revenue Code Section 213.

Applicability

The new policy is applicable to 2001 returns being filed this year and to any years for which amended returns can be filed by taxpayers (generally three years back, to the 1998 tax year).

The time for filing an amended return for 1998 has run out. The deadline was April 15, 2002, for most taxpayers. Determining what qualifies as an otherwise deductible medical expense also determines what may be paid out of a pre-tax flexible spending account. Of course, if pre-tax dollars are used to pay for treatment, the cost cannot also be taken as an itemized deduction. Obtaining a diagnosis from a physician of either obesity (defined by some experts as being more than 20 percent of ideal weight) or hypertension paired with being overweight - prior to undertaking a weight loss program — was included in the ruling's fact situation and probably should be done as a precaution. For amended returns, of course, taxpayers will need to go back to their physicians who would then consult their past medical records.



Educators Advised to Save Receipts for Purchase of Books and Classroom Supplies to Substantiate New Tax Deduction

The IRS has advised teachers to save their receipts for purchases of books and classroom supplies because those out-of-pocket expenses may serve to lower their taxes, due to the addition of Code Section 62(d) by the Job Creation and Worker Assistance Act of 2002. Noting that many teachers use their own funds to pay for needed classroom supplies, IRS Commissioner Charles O. Rossotti stated, "A new law gives them a tax break this year and next, and we want them to have the records they'll need to claim it on their returns." The new deduction may be claimed by eligible educators in both public and private elementary and secondary schools who work at least 900 hours during a school year as a teacher, instructor, counselor, principal, or aide. Up to \$250 of qualified expenses may be subtracted when calculating adjusted gross income (AGI), and it will not be necessary for educators to itemize deductions in order to obtain this benefit. Prior to the law change,

these expenses could be claimed only as miscellaneous itemized deductions subject to the 2%-of-AGI floor.

Educators who excluded education savings bond interest or payments from qualified tuition programs, or who made tax-free withdrawals from an education savings account, will be eligible for the new deduction only to the extent that their qualified expenses exceed the tax-free amounts.

In order to prevent a missed deduction at tax time, the IRS has suggested that educators maintain their records of qualifying expenses in a folder or envelope labeled "Educator Expenses Deduction," noting the date, amount and purpose of each purchase. Details on this deduction and other new law changes are set forth in IRS Publication 3991, "Highlights of the Job Creation and Worker Assistance Act of 2002."



Our office will be closed on Thursday, July 4th and Friday, July 5th, 2002

"It isn't the mountains ahead that wear you out— It's the grain of sand in your shoe."- Anonymous

T. Dennis Connally, Financial Consultant Inc.
8484 Campbellton Street
Douglasville, GA 30134

Phone: 770-920-2890
Fax: 770-942-7180
Email: tdconnally@tdconnally.com

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You'll want to consider the strength of your normal backup activities such as making regular backups of your data and maintaining a good paper trail of the important documentation from your systems. You'll also want to consider the frequency of your backups (how often the backups are done) and the storage of backups and paperwork both on-site and off-site just to be safe. This might be a good time to make arrangements to use another organization's work site in case you temporarily experience power outages or hardware and equipment failures. Or you might find other vendors who offer the products and supplies you need if your regular vendors or suppliers are not able to ship products to you.

In short, treating Year 2000 issues as natural disasters and evaluating your disaster recovery plan for your computer systems and other systems may be your best course of action.

A Final Note

No one knows for sure what will happen during the Year 2000 rollover, but it's always best to be prepared. We hope our suggestions are useful to you as you make your own plans. After all, the success of your company and your continued business with us is as im-

portant to us as it is to you. This article is not meant to be an extensive road-map on the direction you can take to prepare for the Year 2000. However, we hope it has provided you with some guidelines that can be used as a starting point. It is up to you to assess your company's needs and to choose the best options that will benefit your business in the next century.

*"All of us here at
T. Dennis Connally,
Financial Consultant Inc.
extend to each of you and
your family
every good wish for the
holiday season"*

HERMAN

By Jim Unger



"Let's see. That's 18 volumes of 'Income Tax Made Easy.'"

NOTICE

Credit Policy Change

Effective September 1, 1999, any account that is more than 90 days past due will be automatically turned over to our collection service, and the credit bureau will be notified of the delinquent account.

TAX TIP

For the past three years, making investment decisions based upon their income tax consequences has been especially difficult since Congress made surprise changes to the capital gains rules in mid-1997 and mid-1998. There seems to be the potential for more changes in late-1999 in light of the "Taxpayer Refund and Relief Bill of 1999," which was recently passed by Congress. Provisions in this bill would lower the maximum capital gains rate to 18%, effective starting in 1999, and would index the rate for inflation beginning in 2000. Although President Clinton is expected to veto the bill in its present form, passage of the bill does send a signal to taxpayers that a lower capital gains rate is on Congress's agenda, and that rates could very well decrease in the near future. Although we can't predict which proposals become law, it is always a good idea to keep up with potential changes and to understand early in the planning process how they would impact your investment decisions.

Happy Holidays!