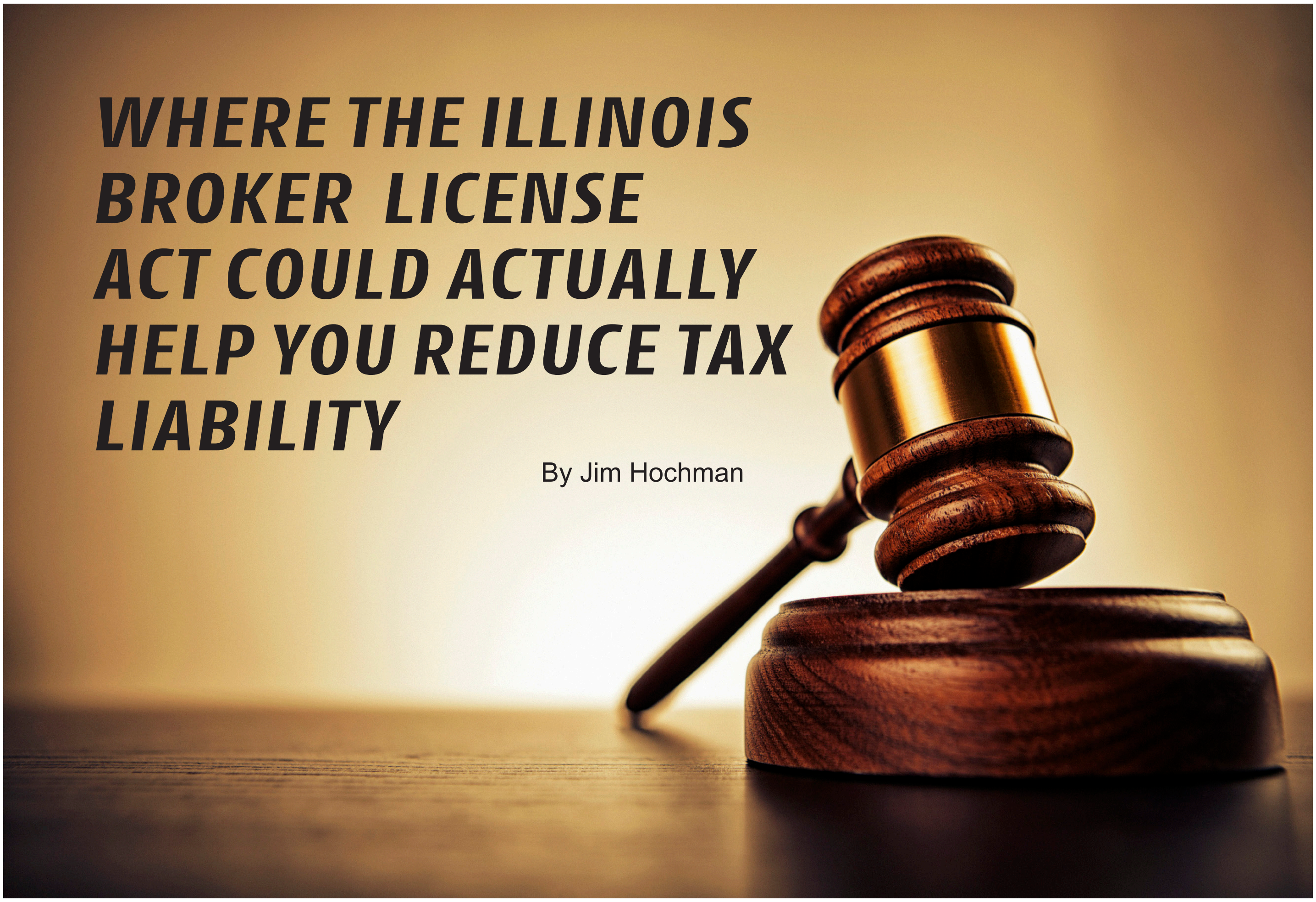

WHERE THE ILLINOIS BROKER LICENSE ACT COULD ACTUALLY HELP YOU REDUCE TAX LIABILITY

By Jim Hochman

The Illinois Real Estate License Act of 2000, 225 ILCS 454/1 et. seq. contains a provision by which an Illinois licensee can assert some control over his or her licensed services and other income, and may allow for reduction of the licensee's income tax liability. At Section 10-20(e), the Acts reads:

"Notwithstanding the fact that a sponsoring broker has an employment [or independent contractor] agreement with a licensee, a sponsoring broker may pay compensation directly to a corporation solely owned by that licensee that has been formed for the purpose of receiving compensation earned by the licensee…"

An Illinois licensee, then may form a corporation (or limited liability company) where the licensee is the sole shareholder or member, and income derived from licensed services or other services may be paid by the sponsoring broker to that entity. The Administrative Rules at 68 Part 1450, Section 1450.745 elaborates, requiring notice of the entity to IDFPR, but allow all income earned by the sole shareholder (whether from licensed services or elsewhere) to be paid to that entity. A few saavy licensees have formed such entities, and here is why.

Certain business expenses (as explained below) can then be paid by the corporation "above the line" such as business related expenses for automobiles, cell phones, licensed or unlicensed assistants, professional organization dues and subscriptions, marketing expenses, computer and supplies, professional education, and license fees.

Where these expenses might otherwise be taken on the licensee's individual tax return, either in Schedule A (Itemized Deductions) or Form 2106 (Employee Business Expenses), there are limitations imposed on the taxpayer which limit the benefit of those deductions. These limitations would not apply if taken by the corporation which the licensee formed to receive his or her income. If all of the business expenses were applied against the gross income received by the licensee, thereby reducing the net or taxable income (for federal and state income tax reporting), the licensee could actually reduce his or her tax liability.

Illinois CPA Bonnie Ansburg Marshall of Ansburg & Co. in Naperville, Ill. advises:

"As a commercial real estate broker, you are usually considered an independent contractor and therefore self-employed. As such you are qualified to take a myriad of expenses including but perhaps not limited to office rent, office supplies, advertising and promotions, travel and entertainment, license and professional education expenses, business automobile expenses, telephone, and dues. By forming this corporation (or limited liability company) so long as you are the sole owner (i.e. shareholder or member), you are allowed to deduct 100 percent of these expenses to reduce your taxable income. This is a considerable advantage compared to those expenses you could deduct as an employee."

Further, employees are required to report expenses on Form 2106, which is subsequently included on Schedule A. However, your Form 2106 unreimbursed employee business expenses are only deducted to the extent that these expenses exceed 2 percent of your adjusted gross income. Amounts used as a deduction on Form 2106 may be further limited by the Alternative Minimum Tax provision.

Conversely, corporate expenses are 100 percent deductible from your income without these limits being imposed. For further information about what type of expenses are allowable, you can reference http://www.irs.gov/Business and click on the Small Business & Self-Employed Center.

Working within the applicable guidelines, tax reduction can be substantial.

The costs of formation and annual fees of the corporation or LLC are also deductible; but remember that the licensee must be the sole shareholder or sole member of the LLC. The licensee still performs services in his or her own name (i.e. this section is no substitute for the firm doing business as a corporation or LLC, and is no substitute for errors and omissions insurance). However, where those business expenses are taken “above the line” by the corporation, tax liability can be reduced.

I have not surveyed other states’ real estate license acts for similar provisions, so presently this particular plan may benefit only IL real estate licensees. There is no reason, however, not to seek a change in other states’ license acts.

Reminder: this article is intended to offer new possibilities, but shall not be deemed personal income tax advice. The reader is always advised to consult his or her own tax advisors to determine whether such a corporation or LLC works best for the individual taxpayer. ■