Remarks from Beanna

2020 - Happy New Year’s Day!

New Year’s Day is a national holiday celebrated on January 1st, the first day of the New Year, following both the Gregorian and the Julian calendar. This New Years’ holiday is often marked by fireworks, parades, and reflection upon the last year while looking ahead to the future’s possibilities. Many people celebrate New Year’s in the company of loved ones, involving traditions meant to bring luck and success in the upcoming year. Many Cultures celebrate this happy day in their own unique way. Typically the customs and traditions of happy New Years Day involve celebrating with champagne and a variety of different foods. New Years marks a date of newly found happiness and a clean slate. For many celebrating New Years, it is their opportunity to learn from the prior year and make positive changes in their life.

New Year’s is one of the oldest holidays still celebrated, but the exact date and nature of the festivities has changed over time. It originated thousands of years ago in ancient Babylon, celebrated as an eleven day festival on the first day of spring. During this time, many cultures used the sun and moon cycle to decide the “first” day of the year. It wasn’t until Julius Caesar implemented the Julian calendar that January 1st became the common day for the celebration. In the twentieth century, the holiday grew into its own celebration and mostly separated from the common association with religion. It has become a holiday associated with nationality, relationships, and introspection rather than a religious celebration, although many people do still follow older traditions.

New Year’s Day Resolutions and Traditions

While celebration varies all over the world, common traditions include:

- Making resolutions or goals to improve one’s life.

  - Common resolutions concern diet, exercise, bad habits, and other issues concerning personal wellness. A common view is to use the first day of the year as a clean slate to improve one’s life.
• A gathering of loved ones: Here you’ll typically find champagne, feasting, confetti, noise makers, and other methods of merriment. Fireworks, parades, concerts.

• Famous parades include London’s New Year’s Day Parade and the Rose Parade in Pasadena, California. Superstitions concerning food or visitors to bring luck.

This especially includes circle-shaped foods, which symbolize cycles. The reasoning behind superstitions is that the first day of the year sets precedent for the following days. A common superstition specific to New Year’s Day concerns a household’s first visitor of the year—tradition states that if a tall, dark-haired stranger is the first to walk through your door, called the First Footer or Lucky Bird, you’ll have good luck all year. Also, if you want to subscribe to superstition, don’t let anything leave the house on New Year’s, except for people. Tradition says: don’t take out the trash and leave anything you want to take out of the house on New Year’s outside the night before. If you must remove something, make sure to replace it by bringing an item into the house. These policies of balance apply in other areas as well—avoiding paying bills, breaking anything, or shedding tears.

• Toasting

Toasts typically concern gratefulness for the past year’s blessings, hope and luck or the future, and thanking guests for their New Year’s company. In coastal regions, running into a body of water or splashing water on one another, symbolizing the cleansing, “rebirth” theme associated with the holiday.

However, many nations and cultures within them have their own characteristic way of celebrating:

American Citizens often celebrate with a party featuring toasting, drinking and fireworks late into the night before the New Year, where the gathering counts down the final seconds to January 1st. Some might even get a kiss at midnight. Many English speaking countries play “Auld Lang Syne,” a song celebrating the year’s happy moments. Americans often make resolutions and watch the Time Square Ball drop in New York City. Although much of this celebration occurs the night before, the merrymaking typically continues to New Year’s Day. Football is a common fixture on New Year’s Day in America, usually the day of the Rose Bowl. Some foods considered “lucky” to eat during the festivities include:

Circular shaped foods
Black-eyed peas
Cabbage
Pork

For thousands of years, New Year’s has been a festival of rebirth and reflection, allowing people all over the world to celebrate another great year.

New Year’s Song

The song, “Auld Lang Syne,” is sung at the stroke of midnight in almost every English-speaking country in the world to bring in the new year. At least partially written by Robert Burns in the 1700’s, it was first published in 1796 after Burns’ death. Early variations of the song were sung prior to 1700 and inspired Burns to produce the modern rendition. An old Scottish tune, “Auld Lang Syne” literally means “old long ago,” or simply, “the good old days.” The lyrics can be found here.

Auld Lang Syne

Should old acquaintance be forgot
...And never brought to mind
Should all acquaintance be forgot
And auld lang syne

For auld lang syne, my dear
For auld lang syne

We’ll take a cup o’ kindness yet
For auld lang syne

To my friends and colleagues, A Very Happy New Year! May 2020 be filled with good health, friends and family to share good fortunes and peace within and in the world about us.

Stat well and finish well.

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2019 Estate And Gift Taxes
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Form 706 with Portability
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The "How to" of Form 1041
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2019 Ethics
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The New Offer In Compromise
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The Incredible LLC
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2-CE HOURS

Identity Theft
2 CE Hours

IRS Audits
1-CE HOUR

Taxation Of Ministers
1-CE HOUR

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February 1st, 2020
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Too Many Credit Cards? Protect Your Credit Scores While Closing Accounts

If you have more credit cards than you want, don’t close the extra accounts all at once because that could deal a blow to your credit scores.

By Liz Weston

Dear Liz: Over the years, my husband and I have accumulated a number of credit cards. All have had a zero balance for years. I want to start canceling these cards, but I’m concerned that will hurt our great credit scores. How should I go about this, or should I?

Answer: As you probably know, closing credit accounts won’t help your scores and may hurt them. That doesn’t mean you can never close a credit card, but you shouldn’t close a bunch of them at once or close any if you’ll be in the market for a major loan, such as a mortgage or auto loan.

If you’re not planning to borrow money in the near future, then you can start closing accounts one at a time. You’ll probably want to keep the cards with the highest credit limits, and perhaps your oldest card as well. Monitor your scores to see how long they take to recover from each closure. You may need to wait a few months before shutting the next account.

Be sure to use your remaining cards occasionally by charging small amounts and paying the balance in full. That will keep the cards active and help prevent the issuer from canceling them.

Editor’s Note: As tax professionals we continuously are asked questions seemingly unrelated to tax, however, if bankruptcy due to credit cards, cancellation of debt and other issues evolve, you can be assured of a tax consequence.

Tax Court Allows Long String Of Horse Losses

Peter J Reilly, Contributor

A long string of losses in a horse related business may well attract IRS attention. Don’t despair. If you take the right steps you have a good chance of winning in Tax Court. Reilly’s Eighteenth Law of Tax Planning - Honest objective trumps realistic expectation.

Lowell G. Den Besten was facing a tab of over $250,000 in tax and accuracy penalties from IRS denial of the losses from his cutting horse activity for the years 2006-2010. Tax Court Judge Paris ruled that the losses are allowed.

There are two notable things about the case. The first is that Mr. Den Besten managed this win representing himself in Tax Court. The second is the issue that he lost on, which ended up not costing him anything. Here is some background according to the decision.

Background

Mr. Den Besten owns and manages Dakota’s Best Seed, which apparently has been quite successful. He sold the business on the installment basis in 2002 to focus more on his cutting horse business, but found that it did not do so well without him and had to take back over in 2005. The seed business lost nearly $200,000 in 2005, but was consistently profitable in the subsequent years averaging around $140,000 per year in the years under audit.

The cutting horse business was, of course, losing money in those years or there would not be a decision to write about.

This is not Judge Paris’s first rodeo when it comes to cutting horses, so she refers to her opinion in the case of Finnis Welch to describe
"A “cutting horse”, although not a specific breed, is typically an American quarter horse that has been developed through superior breeding and careful training to isolate and remove a single animal from a larger herd. Cutting horses were originally prized on working ranches for their ability to cut, or separate, individual cows from the herd. A horse’s skills can be showcased through timed competitions that mimic ranch work.”

You make money in the business both through prize money and breeding. The latter is probably where the potential for the big payday is. Mr. Den Besten started the business in 1997 and through the date of the trial (May 2, 2016) had not had a profitable year.

Things had been looking really good around 2005 with a world champion horse with great breeding potential. But the horse died and Mr. Den Besten had to devote more time to the seed business. Everything I know about horse businesses I learned from reading Section 183 cases. My overall conclusion is that more than most businesses, being involved with horses is one GD thing after another.

The Factors

Judge Paris went through the nine factor drill called for in the regulations and confirmed my observation from studying hundreds of other cases. If you win on the first factor you win the case. The factors are:

(1) the manner in which the taxpayer carried on the activity; (2) the expertise of the taxpayer or his advisors; (3) the taxpayer’s time and effort expended in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the taxpayer’s success in carrying on other similar or dissimilar activities; (6) the taxpayer’s history of income or losses with respect to the activity; (7) the amount of occasional profits, if any, which are earned; (8) the financial status of the taxpayer; and (9) the presence of personal pleasure or recreation.

Reg § 1.183-2. Activity not engaged in for profit defined

One Factor To Rule Them All

If you want to win a hobby loss case, Judge Paris’s discussion of Mr. Den Besten’s businesslike approach (the first factor) is what you want to read.

Mr. Den Besten was able to show that he had a business plan through his actions.

"Petitioner’s business plan is evidenced by his actions. Petitioner’s plan was to build upon his established reputation in the cutting horse industry and increase recognition of his brand through his horses’ continued superior performances at cutting horse competitions. In order to carry out this plan he purchased and bred quarter horses to train into winning cutting horses. “

Make a note here if you can’t wring a written business plan out of your client to use this decision.

He also managed to get by on fairly simple business records, basically receipts and disbursements. Judge Paris laid off the common critique of business records that they were not used explicitly to control expenses.

Changing operating methods was also a win as the cutting business was ramped up in conjunction with the sale of the seed business and ramped down when he had to dive back into the seeds.

Finally, there was plenty of advertising.

Success on this factor is critical and the success speaks well of the credibility that Mr. Den Besten was able to project.

The Other Factors

As far as the other factors go, he wins easily on expertise, effort and the prospect of appreciating assets. The fifth factor success in other activities was neutral as the seed business is very different. Naturally he loses on factors six and seven. Other taxpayers with similar facts might have lost on financial status of the taxpayer and elements of recreation, but it is really the first factor that sets the tone.

The Losing Argument

There would have been no need to walk through the 183 factors at all, if the seed business and the cutting horse business were unified. Mr. Den Besten tried to make that argument, but Judge Paris was not having it.

It was actually pretty simple. That is not the way the returns were filed which makes for a really heavy burden in proving otherwise. Positions taken by a taxpayer in a tax return are treated as admissions and cannot be overcome without proof that they are erroneous.

T.C. Memo 2019-154

The Moral

My perspective is that of a tax adviser and what I have learned from studying Section 183 cases is this. If there is something that your client really wants to do, regardless, and they honestly tell you that they are going to try to make money at it, you should take the losses. You should also coach them on the factors, but particularly on the first factor which is being businesslike.

At the end of each loss year go over the results with them and ask them what they are going to do differently in the next year. Document the narrative. Who knows? Maybe with enough discipline they will start making money. Regardless, you will be ready when the audit comes.

Editor’s Note: Peter Reilly has graciously allowed the reprint of his article in the Taxing Times and he is welcomed as a member of the Fellowship.

TCJA Provision 11011 -- Section 199A, Qualified Business Income Deduction FAQs

Basic questions and answers on new 20-percent deduction for pass-through businesses

Below are answers to some basic questions about the new qualified business income (QBI) deduction, also known as the section 199A deduction, that may be available to individuals, including many owners of sole proprietorships, partnerships and S corporations. Some trusts and estates may also be able to take the deduction.

This deduction, created by the 2017 Tax Cuts and Jobs Act, allows non-corporate taxpayers to deduct up to 20 percent of their QBI, plus 20% of qualified real estate investment trust (REIT) dividends and
qualified publicly traded partnership (PTP) income.

Income earned through a C corporation or by providing services as an employee is not eligible for the deduction.

Q1. What is the Qualified Business Income Deduction?

A1. Section 199A of the Internal Revenue Code provides many owners of sole proprietorships, partnerships, S corporations and some trusts and estates, a deduction of income from a qualified trade or business. The deduction has two components.

1. QBI Component. This component of the deduction equals 20 percent of QBI from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust or estate. Depending on the taxpayer's taxable income, the QBI component is subject to multiple limitations including the type of trade or business, the amount of W-2 wages paid by the qualified trade or business and the unadjusted basis immediately after acquisition (UBIA) of qualified property held by the trade or business. It may also be reduced by the patron reduction if the taxpayer is a patron of an agricultural or horticultural cooperative. Income earned through a C corporation or by providing services as an employee is not eligible for the deduction.

2. REIT / PTP Component. This component of the deduction equals 20 percent of the combined qualified REIT dividends (including REIT dividends earned through a regulated investment company (RIC)) and qualified PTP income. This component is not limited by W-2 wages or the UBIA of qualified property. Depending on the taxpayer's income, the amount of PTP income that qualifies may be limited depending on the type of business engaged in by the PTP.

The deduction is limited to the lesser of the QBI component plus the REIT/PTP component or 20 percent of the taxpayer's taxable income minus the net capital gain. For details on figuring the deduction, see Q&A 6 and 7. The deduction is available for taxable years beginning after Dec. 31, 2017 and ending before December 31, 2025. Most eligible taxpayers will be able to claim it for the first time when they file their 2018 federal income tax return in 2019. The deduction is available, regardless of whether an individual itemizes their deductions on Schedule A or takes the standard deduction.

Q2. Who may take the QBI deduction?

A2. Individuals and some trusts and estates with QBI, qualified REIT dividends or qualified PTP income may qualify for the deduction. In some cases, patrons of horticultural or agricultural cooperatives are required to reduce their deduction under section 199A(b)(7) (patron reduction).

Q3. How do S corporations and partnerships handle the deduction?

A3. S corporations and partnerships are generally not taxable and cannot take the deduction themselves. However, all S corporations and partnerships report each shareholder's or partner's share of QBI items, W-2 wages, UBIA of qualified property, qualified REIT dividends and qualified PTP income items on a Schedule K-1, or on a statement attached to, so the shareholders or partners may determine their deduction.

Q4. What is qualified business income?

A4. QBI is the net amount of qualified items of income, gain, deduction and loss from any qualified trade or business. Only items included in taxable income are counted. In addition, the items must be effectively connected with a U.S. trade or business. Items such as capital gains and losses, certain dividends, and interest income are excluded. W-2 income, amounts received as reasonable compensation from an S corporation, amounts received as guaranteed payments from a partnership, and payments received by a partner for services under section 707(a) are also not QBI.

Q5. What is a qualified trade or business?

A5. A qualified trade or business is any section 162 trade or business, with three exceptions:

1. A trade or business conducted by a C corporation.

2. For taxpayers with taxable income that exceeds the threshold amount, specified service trades or businesses (SSTBs). An SSTB is a trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, investing and investment management, trading, dealing in certain assets or any trade or business where the principal asset is the reputation or skill of one or more of its employees or owners. The principal asset of a trade or business is the reputation or skill of its employees or owners if the trade or business consists of the receipt of income from endorsing products or services, the use of an individual's image, likeness, voice, or other symbols associated with the individual's identity, or appearances at events or on radio, television, or other media formats. The SSTB exception does not apply for taxpayers with taxable income below the threshold amount and is phased in for taxpayers with taxable income above the threshold amount. For 2018, the threshold amount is $315,000 for a married couple filing a joint return, or $157,500 for all other taxpayers. The threshold amounts will be adjusted for inflation in subsequent years.

3. The trade or business of performing services as an employee.

Q6. How is the deduction for qualified business income computed?

A6. The SSTB limitation discussed in Q&A 5 does not apply if a taxpayer's taxable income (before the QBI deduction) is at or below the threshold amount, discussed in Q&A 5; the deduction is the lesser of:

1. 20 percent of the taxpayer's QBI, plus 20 percent of the taxpayer's qualified REIT dividends and qualified PTP income' or

2. 20 percent of the taxpayer's taxable income minus net capital gain.

If the taxpayer's taxable income (before the QBI deduction) is above the threshold amount, the deduction may be limited based on whether the business is an SSTB, the W-2 wages paid by the business and the unadjusted basis immediately after acquisition of certain property used by the business. For 2018, these limitations are phased in for joint filers with taxable income above $315,000 but below $415,000, and all other taxpayers with taxable income above $157,500 but below $207,500. The threshold amounts and phase-in range are for tax year 2018 and will be adjusted for inflation in subsequent years.

Income earned through a C corporation or by providing services as an employee is not eligible for the deduction regardless of the taxpayer's taxable income. In some cases, patrons of horticultural or agricultural cooperatives are required to reduce their deduction under section 199A(b)(7) (patron reduction). See also Q&A 13 for more information on computation and available worksheets.
Q7. I have income from a specified service trade or business. How does that affect my deduction?

A7. The SSTB limitation does not apply to any taxpayer whose taxable income (before the qualified business deduction) is at or below the threshold amounts discussed in Q&A #5. For taxpayers whose taxable income is within the phase-in range discussed in Q&A #6, the taxpayer’s share of QBI, W-2 wages and UBIA of qualified property related to the SSTB may be limited. If the taxpayer’s taxable income exceeds the phase-in range, no deduction is allowed with respect to any SSTB. The threshold amounts and phase-in range are for tax year 2018 and will be adjusted for inflation in subsequent years.

In some cases, patrons of horticultural or agricultural cooperatives are required to reduce their deduction under section 199A(b)(7) (patron reduction). See also Q&A 13 for more information on computation and available worksheets.

Q8. In 2018, I will report taxable income under $315,000 and file married filing jointly. Do I have to determine if I am in an SSTB in order to take the deduction? Is there any limitation on my deduction?

A8. No, if your 2018 taxable income (before the QBI deduction) is at or below the threshold amount ($315,000, if married filing jointly, or $157,500 for all other filing statuses), the SSTB limitations do not apply. You will be able to deduct the lesser of:

1. Twenty percent (20%) of your QBI, plus 20 percent of your qualified REIT dividends and qualified PTP income, or

2. Twenty percent (20%) of your taxable income minus your net capital gain.

Income earned through a C corporation or by providing services as an employee is not eligible for the deduction regardless of the taxpayer’s taxable income.

Q9. In 2018, I will report taxable income between $157,500 and $207,500 and file as single. I receive QBI. Does it matter if it is from an SSTB?

A9. Yes, because your taxable income is above the threshold amount, your QBI deduction with respect to any SSTB will be limited. However, because you are within the phase-in range (above $315,000 but below $415,000 for married filing joint, and all other taxpayers with taxable income above $157,500 but below $207,500), you may be allowed some QBI deduction with respect to an SSTB. In addition, for taxpayers above the threshold amount, the 20 percent QBI with respect to any trade or business, including an SSTB, may be limited by the amount of W-2 wages paid by the trade or business and the UBIA of qualified property held by the trade or business.

Q10. In 2018, I am single and will report taxable income over $207,500. My only income is from an SSTB. Am I entitled to the deduction with respect to the SSTB?

A10. No. The same is true for a married couple filing a joint return whose taxable income exceeds $415,000.

Q11. In 2018, I am single and will report taxable income over $207,500. I am NOT in an SSTB. Am I entitled to the deduction?

A11. Yes, if you have QBI, qualified REIT dividends or qualified PTP income. For eligible taxpayers with total taxable income in 2018 over $207,500 ($415,000 for married filing joint returns), the deduction for QBI may be limited by the amount of W-2 wages paid by the qualified trade or business and the UBIA of qualified property held by the trade or business. The regulations provide additional information on these limitations.

Q12. How do cooperatives qualify for the qualified business income deduction?

A12. Cooperatives do not qualify for the QBI deduction under section 199A(a) but may be eligible to take the section 199A(g) deduction. Section 199A(g) provides a deduction for Specified Agricultural or Horticultural Cooperatives (Specified Cooperatives) and their patrons similar to the deduction under former section 199, which was known as the domestic production activities deduction. The IRS issued additional guidance for cooperatives and their patrons on June 18, 2019.

Q13. Is there a form for reporting the qualified business income deduction? And if so, where can I find it?

A13. There is no form for reporting the QBI deduction in 2018. However, two worksheets have been developed to help taxpayers compute their deduction. The first worksheet is located in the instructions to Form 1040 and can be used by taxpayers with taxable income (before the QBI deduction) at or below the threshold amount ($315,000 for a married couple filing a joint return, or $157,500 for all other taxpayers) and that are not patrons in a horticultural cooperative.

The second worksheet will be located in Publication 535, Business Expenses. It should be used by taxpayers with taxable income exceeding the threshold amount. It should also be used by taxpayer's that are patrons of specified agricultural or horticultural cooperatives.

For tax year 2019, Form 8995, Qualified Business Income Deduction Simplified Computation, and Form 8995-A, Qualified Business Income Deduction, will be available and will replace the worksheets found in the Form 1040 instructions and Publication 535, respectively.

Q14. Does the deduction reduce earnings subject to self-employment tax?

A14. No. The QBI deduction does not reduce net earnings from self-employment, under section 1402. Similarly, the deduction does not reduce net investment income under section 1411 (Form 8960, Net Investment Income Tax).

Q15. If I report taxable income under the threshold are there any limits to my deduction?

A15. If your taxable income (before the QBI deduction) is at or below the threshold, then most of the limitations are not applicable. The specified service trade or business, W-2 wage, and UBIA limitations do not apply to taxpayers whose taxable income is at or below these thresholds.

The deduction is limited the lesser of 20% of QBI plus 20% of qualified REIT dividends and qualified PTP income or 20% of taxable income less net capital gain for all taxpayers, regardless of income. Also, if you are a patron in an agricultural or horticultural cooperative, the QBI component may be reduced by the patron reduction. Finally, income earned through a C corporation or by providing services as an employee is not eligible for the deduction regardless of the taxpayer’s taxable income.

Q16. Do any limitations apply to the REIT/PTP Component?
A16. Yes. The REIT/PTP Component generally includes qualified REIT dividends (including REIT dividends earned through a RIC) and PTP income as defined in section 199A and the regulations thereunder. For taxpayers above the threshold amount, discussed in Q&A #5 and #6, qualified PTP income may be limited if the PTP operates an SSTB. The limitation does not apply to any taxpayer whose taxable income (before the qualified business deduction) is at or below the threshold amounts discussed in Q&A #6. For taxpayers whose taxable income is within the phase-in range discussed in Q&A #6, the taxpayer's PTP income from the SSTB may be limited. If the taxpayer's taxable income exceeds the phase-in range, no deduction is allowed with respect to any SSTB operated by a PTP. The threshold amounts and phase-in range are for tax year 2018 and will be adjusted for inflation in subsequent years.

Q17. If someone is a real estate professional, will their rental real estate qualify for the deduction?

A17. The deduction is not based on whether the taxpayer qualifies as a real estate professional under section 469. Rental real estate may constitute a trade or business for purposes of the QBI deduction if the rental real estate:

- Rises to the level of a trade or business under section 162,
- Satisfies the requirements for the safe harbor provided by Rev. Proc. 2019-38, or
- Meets the self-rental exception (i.e., the rental or licensing of property to a commonly controlled trade or business conducted by an individual or RPE).

Whether rental real estate rises to the level of a trade or business under section 162 depends on all the facts and circumstances. To be engaged in a trade or business under section 162, the taxpayer must be actively involved in the activity with continuity and regularity and the primary purpose for engaging in the activity must be for income or profit.

Q18. If I have net income from one qualified business and a net loss from another qualified business, is the loss from the second business carried forward and applied against that same business in the future or is it netted against the income from the first business when calculating the deduction? What if the losses are greater than the income, does this mean I will not get a deduction?

A18. A taxpayer must net their QBI, including losses, from multiple trades or businesses (including aggregated trades or businesses). So, negative QBI from one business will offset positive QBI from other trades or businesses (including aggregated trades or businesses) in proportion to the net income of the trades or businesses with positive QBI.

If the total QBI from all trades or businesses is less than zero, the taxpayer's QBI Component will be zero and any negative amount is carried forward to the next taxable year. The carried forward negative QBI will be treated as negative QBI from a separate trade or business for purposes of determining the QBI Component in the next taxable year.

Q19. Does a net QBI Component loss reduce the REIT PTP Component?

A19. A net loss in the QBI Component does not impact the calculation of the deduction with respect to the REIT/PTP Component. However, if qualified PTP income is a loss, it is netted against qualified REIT dividends in a separate netting calculation from the loss netting of the QBI Component. These two netting requirements could result in two separate loss carryforwards, one for the QBI Component and one for the REIT/PTP Component.

Q20. Do I have to materially participate in a business to qualify for the deduction?

A20. No. Material participation under section 469 is not required for the QBI deduction. Eligible taxpayers with income from a trade or business may be entitled to the QBI deduction (if they otherwise satisfy the requirements of section 199A) regardless of their involvement in the trade or business.

Q21. I file a joint return, my income is under the threshold amount, the only income I have is from W-2 wages and a domestic Schedule C business. Does my QBI equal the amount on Schedule C, line 31, Net profit or (loss)?

A21. Not necessarily. As discussed in Q&A #4, QBI is the net amount of qualified items of income, gain, deduction and loss from any qualified trade or business. In addition to the profit or loss from Schedule C, QBI must be adjusted by any other items of gain or deduction related to the business, including but not limited to gains from Form 4797, the deductible part of self-employment tax, self-employed health insurance, self-employed SEP, SIMPLE, and qualified plan deductions. Amounts received as W-2 income, reasonable compensation from an S corporation, guaranteed payments from a partnership, and payments received by a partner for services under section 707(a) are not QBI and are not eligible for the deduction.

Q22. I am a statutory employee and report my income on Schedule C. Does it qualify for the qualified business income deduction?

A22. Payments made to statutory employees, as defined in section 3121(d)(3), are excluded from the definition of wages considered income from the trade or business of performing services as an employee under §1.199A-5(d)(1). Items of income, gain, deduction, and loss from performance of services as a statutory employee are considered QBI and are eligible for the QBI deduction to the extent the requirements of section 199A are satisfied.

Q23. Can you explain in more detail how losses that are limited by basis, at-risk, or passive activity rules affect the deduction?

A23. Items not included in taxable income are not qualified items of income, gain, deduction, or loss and are not current year QBI. If a taxpayer has a suspended loss that is allowed against current year taxable income, whether the loss reduces QBI depends on whether the loss was limited before or after January 1, 2018.

If the loss was disallowed before 2018, the loss is never taken into account for purposes of computing QBI. This means the taxpayer must keep track of pre-2018 disallowed losses, so that they can be excluded from QBI in the year the loss is allowed.

If the loss was generated after 2018, it is included in QBI if it is a qualified item of deduction or loss that would otherwise be included in QBI, but not until the year it is included/allowed in taxable income. Disallowed, limited, or suspended losses must be used in order from the oldest to the most recent on a first-in, first-out (FIFO) basis.

Q24. How do I satisfy the disclosure requirements if I choose to aggregate my trade or businesses?
A24. Pub 535, Business Expenses, has a Qualified Business Income Deduction Worksheet that can be used to compute the QBI deduction. Schedule B, Aggregation of Business Operations, or another schedule reflecting the taxpayer's aggregation should be attached to the return as a PDF to satisfy the disclose requirement. Q25. Do I need to disclose my aggregated trades or businesses when I use the simplified worksheet in the Instructions for Form 1040 to calculate the QBI deduction?

A25. Yes, taxpayers should disclose their aggregations regardless of which worksheet they use to compute the QBI deduction. A failure to aggregate will not be considered to be an aggregation for purposes of the consistency requirement. So, if the taxpayer is under the threshold in 2018 and there is not a need to aggregate, it would not prevent the taxpayer from aggregating in a subsequent year when the taxpayer's taxable income exceeds the threshold amount.

Q26. I received a REIT dividend either directly or through a regulated investment company (RIC), reported as a section 199A dividend in box 5 of Form 1099-DIV. Is this amount eligible for the QBI deduction?

A26. Box 5 of Form 1099-DIV is used by REITs and RICs to report amounts that may be eligible for the QBI deduction, but some amounts reported in box 5 may be ineligible for the deduction.

Ineligible dividends include those for which the taxpayer did not meet holding period requirements for REIT or RIC stock. The QBI deduction may not be taken for any dividend reported in box 5 for dividend received on a share of REIT or RIC stock that is held for 45 days or less during the 91-day period beginning on the date that is 45 days before the date on which such share became ex-dividend with respect to the dividend. When counting the number of days the stock is held, include the day the stock is disposed of but not the day the stock is acquired. Also, don't count days during which the risk of loss was diminished. Specifically, don't count any day during which any of the following conditions are met:

1. The taxpayer had an option to sell, was under a contractual obligation to sell, or entered into (and not closed) a short sale of substantially identical stock or securities.
2. The taxpayer was a grantor (writer) of an option to buy substantially identical stock or securities.
3. The taxpayer's risk of loss was diminished by holding one or more other positions in substantially similar or related property.

In addition, the deduction may not be taken for any dividend on shares of REIT or RIC stock reported in box 5 to the extent the taxpayer is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property.

Pass-through Entity

Q27. I am a partner in several partnerships, how do I know what qualifies for the deduction?

A27. The Schedule K-1s for 2018 have new codes for the QBI deduction items. The partnership needs to provide each partner with their share of QBI items, W-2 wages, UBIA of qualified property, and other information necessary for partners to compute their deduction. The same rules apply for S corporations.

If a partnership or S corporation fails to provide this information, the final regulations provide that each unreported income of positive QBI, W-2 wages, or UBIA of qualified property attributable to the entity's trades or businesses will be presumed to be zero. This means that a partner or shareholder may be unable to claim a QBI deduction on the entity's income if the entity fails to report the information. It is recommended that taxpayer follow-up with a pass-through entity if they do not provide the necessary information.

Q28. If a pass-through entity has one business, is it only required to provide one dollar amount for the QBI?

A28. The pass-through entity is required to provide the owners QBI information necessary for the owner to compute the deduction. If the entity only has ordinary income from a single trade or business, it may be appropriate to reflect one QBI amount. Items from a pass-through entity are required to be separately stated due to the potential of unique treatment on one or more owners' returns. Items not included in current year taxable income are not included in QBI. Therefore, additional details will also need to be provided for the owners. If for example, in addition to ordinary income the owner is allocated a section 179 deduction, since the 179 deduction may be limited, the detail would be required in order for the owner to properly determine the current year QBI.

Also note that the rules to separately state items from each activity for the application of the at-risk rules and passive activity loss limitation rules still apply even when a pass-through entity chooses to aggregate a trade or business for the purposes of section 199A.

Q29. My income is under the threshold amount and I only have income from W-2 wages and a partnership interest. Does my QBI equal the amount of partnership income reported on Schedule K-1?

A29. Maybe. As discussed in Q&A 4, QBI is the net amount of qualified items of income, gain, deduction and loss from any qualified trade or business. To determine the total amount of QBI, the taxpayer must consider deductions not reported on Schedule K-1 that are related to the trade or business. This could include unreimbursed partnership expenses, business interest expense, the deductible part of self-employment tax, the self-employment health insurance deduction, and self-employed SEP, SIMPLE, and qualified plan deductions in addition to other adjustments. Amounts received as guaranteed payments and payments received by a partner for services under section 707(a) are not QBI and are not eligible for the deduction.

Q30. What about fiscal-year pass-through entities? I have a partnership whose fiscal year ended on March 31, 2018. Do I get a qualified business income deduction for the income I earned?

A30. The QBI deduction itself is available only to taxpayers whose tax years begin after December 31, 2017.

However, any QBI reported to a taxpayer from a related passthrough entity with a taxable year beginning in 2017 and ending in 2018 is treated as having been incurred in the owner's taxable year in which the passthrough entity's taxable year ends.

For example, a calendar year partner in a partnership with a fiscal year end of March 31, 2018, will be able to include the partnership's QBI for the entire fiscal year in determining the partner's 2018 QBI deduction. The partner may also use the partnership's W-2 wages and UBIA of qualified property in computing the deduction, if applicable. Note that the pass-through entity's 2017 Schedule K-1 does not have the detail relating to the new QBI deduction. The entity should still
Q31. In 2018, I receive a Schedule K-1 allocating a PTP loss. The loss is not currently allowable due to the passive activity rules. Is it used in computing the REIT/PTP component?

A31. No. Since the loss is not included in taxable income for 2018, it is not used in computing the QBI deduction in 2018. In a later taxable year, when the loss is allowable, the loss generated in 2018 will be used in computing the REIT/PTP component.

Q32. I was told that I can rely on the rules in the proposed regulations under § 1.199A-1 through 1.199A-6 to calculate qualified business income (QBI) for my 2018 tax return. Does this mean I do not have to include adjustments for items such as the deductible portion of self-employment tax, self-employed health insurance deduction, or the self-employed retirement deduction when calculating my QBI in 2018?

A32. Section 199A(c)(1) defines qualified business income as the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer. Proposed regulation § 1.199A-1(b)(4) followed this definition, providing that QBI is the net amount of qualified items of income, gain, deduction, and loss with respect to any trade or business as determined under the rules of 1.199A-3(b). Section 1.199A-1(b)(5) of the final regulations retains this rule, also providing that QBI means the net amount of qualified items of income, gain, deduction, and loss with respect to any trade or business (or aggregated trade or business) as determined under the rules of 1.199A-3(b).

Section 1.199A-3(b)(2) defines the term "qualified items of income, gain, deduction, and loss" as items of gross income, gain, deduction, and loss to the extent such items are effectively connected with the conduct of a trade or business within the United States (with certain modifications) and included or allowed in determining taxable income for the taxable year. The final regulations add additional clarity in § 1.199A-3(b)(1)(vi), which provides that generally deductions attributable to a trade or business are taken into account for purposes of computing QBI to the extent that the requirements of section 199A and § 1.199A-3 are satisfied. For purposes of section 199A only, deductions such as the deductible portion of the tax on self-employment income under section 164(f), the self-employed health insurance deduction under section 162(l), and the deduction for contributions to qualified retirement plans under section 404 are considered attributable to a trade or business to the extent that the individual's gross income from the trade or business is taken into account in calculating the allowable deduction, on a proportionate basis to the gross income received from the trade or business.

The above the line adjustments for self-employment tax, self-employed health insurance deduction, and the self-employed retirement deduction are examples of deductions attributable to a trade or business for purposes of section 199A. There is no inconsistency between the proposed and final regulations on this issue. QBI must be adjusted for these items in 2018.

Q33. Health insurance premiums paid by an S-Corporation for greater than 2% shareholders reduce qualified business income (QBI) at the entity level by reducing the ordinary income used to compute allocable QBI. If I take the self-employed health insurance deduction for these premiums on my individual tax return, do I have to also include this deduction when calculating my QBI from the S-Corporation?

A33. Generally, the self-employed health insurance deduction under section 162(l) is considered attributable to a trade or business for purposes of section 199A and will be a deduction in determining QBI. This may result in QBI being reduced at both the entity and the shareholder level.

Patrons and Cooperatives

Q34. What is the purpose of the proposed regulations in §§1.199A-7 through 1.199A-12?

A34. The purpose of these proposed regulations is (1) to provide guidance to patrons of cooperatives regarding the application of the QBI deduction. (See Q&A1) including the reduction of the QBI deduction that is required for patrons of Specific Agricultural and Horticultural Cooperatives (patron reduction) and (2) to provide guidance to Specific Agricultural and Horticultural Cooperatives (Specified Cooperatives) and their patrons on the computation and allowance of the deduction for income attributable to domestic production activities of Specific Cooperatives (Section 199A(g) deduction). These proposed rules apply to taxable years ending after final regulations are published in the Federal Register. Taxpayers, however, may rely on these proposed regulations until that date, but only if the taxpayers apply the rules in their entirety and in a consistent manner.

Q35. I am a farmer who is a patron of a Specified Cooperative. Could I be entitled to two deductions under section 199A?

A35. Yes. A farmer can have a qualified trade or business that generates a QBI deduction and could be passed through a Section 199A(g) deduction from the Specified Cooperative of which the farmer is a patron. Regardless of whether the section 199A(g) deduction was passed through, the farmer would have to determine whether their QBI deduction is subject to the patron reduction under section 199A(b)(7). The farmer may take any Section 199A(g) deduction passed through to the extent of their taxable income determined after their QBI deduction.

Q36. What are Specified Cooperatives?

A36. They are agricultural or horticultural cooperatives to which Part I of subchapter T of the Internal Revenue Code applies that are engaged (i) in the manufacturing, production, growth, or extraction (MPGE) in whole or significant part of any agricultural or horticultural product, or (ii) in the marketing of any agricultural or horticultural product that their patrons have MPGE in whole or significant part. Specified Cooperatives include cooperatives that are considered nonexempt or exempt. Exempt cooperatives are those farmers' cooperatives that are qualified under section 521 of the code. An organization will not be considered exempt, even though it operates within the provisions of sections 521 and 1381 through 1388, unless it files IRS Form 1028, Application for Recognition of Exemption Under Section 521 of the Internal Revenue Code or has previously received a ruling recognizing its exemption under section 521 of the Internal Revenue Code of 1986 or corresponding provisions of prior law.

Q37. How do cooperatives and their patrons handle the QBI deduction?

A37. Cooperatives are C corporations for federal income tax purposes, and therefore are not eligible for the QBI deduction. However, patrons that are individuals and certain trusts and estates may qualify for the deduction. See also Q&A 2.
Patrons of cooperatives that are individuals, trusts or estates and that have QBI, qualified REIT dividends or qualified PTP income may qualify for the QBI deduction. The rules in §§1.199A-1 through 1.199A-6 apply to all taxpayers, including patrons, eligible to take the QBI deduction. See preceding Q&A’s for additional information on computing the QBI deduction. To the extent a patron receives patronage dividends or similar payments from a cooperative, the patron must follow the additional special rules and clarification in proposed §1.199A-7 to calculate its QBI deduction. Patronage dividends or similar payments from cooperatives may be included in the patron’s QBI to the extent that (i) these payments are related to the patron’s trade or business, (ii) are qualified income at the cooperative’s trade or business level, (iii) are not income from a specified service trade or business (SSTB) at the cooperative’s trade or business level (unless the patron has taxable income below the threshold amount; see Q&A5), and (iv) provided the patron receives information from the cooperative regarding whether the payments are qualified items of income. Patrons that receive qualified payments from a Specified Cooperative are required to reduce their QBI deduction as provided in section 199A(b)(7) (patron reduction). See Chapter 12 of Publication 535 and Instructions for Form 8995-A.

Q38. How is the patron reduction computed and what are qualified payments?

A38. Patrons that receive qualified payments must reduce their QBI deduction by the lesser of 9% of the QBI properly allocable to the qualified payments, or 50% of the W-2 wages paid with respect to the QBI allocable to the qualified payments. This reduction is required whether the Specified Cooperative passes through all, some, or none of the Specified Cooperative’s Section 199A(g) deduction to the patrons in that taxable year.

Section 199A(g)(1)(E) and proposed §1.199A-8(d)(2)(ii) define qualified payments as any amount of a patronage dividend or per-unit retain allocation, as described in section 1385(a)(1) or (3) received by a patron from a Specified Cooperative that is attributable to the portion of the Specified Cooperative’s qualified production activities income (QPAI), for which the cooperative is allowed a section 199A(g) deduction. For this purpose, patronage dividends include any advances on patronage and per-unit retain allocations that are derived from any lease, rental, license, sale, exchange, or other disposition of any agricultural or horticultural product which was MPGE by the taxpayer. Such term shall not include gross receipts which are derived from the disposition of land or services.

Q39. What information are Cooperatives required to determine and provide to patrons for computation of the QBI deduction?

A39. Cooperatives must provide patrons with certain information for the patron to determine its QBI deduction. The cooperative must determine whether its distributions of patronage dividends and similar payments from each trade or business that is not a SSTB contain qualified items of income, gain, deduction, and loss. The cooperative must also determine the amount of SSTB income, gain, deduction, and loss included in its distributions that is qualified with respect to any SSTB directly conducted by the cooperative. A Specified Cooperative must also report the amount of distributions that are qualified payments made to the eligible taxpayer. All of this information is reported to the patron on an attachment to or on the Form 1099-PATR, Taxable Distributions Received From Cooperatives, or any successor form, unless otherwise provided by the instructions to the Form.

The patron then determines if any of the distributions may be included in the patron’s QBI depending on the patron’s taxable income and the statutory phase-in and threshold amounts ($315,000 in the case of joint returns and $157,500 for all other taxpayers for any taxable year beginning before 2019) and whether the patron reduction applies. Cooperatives should not allocate W-2 wages or unadjusted basis immediately after acquisition (UBIA) of qualified property to their patrons. For the patrons’ QBI deduction, the patrons consider the W-2 wages and UBIA of qualified property from the patrons’ trade or business from which the payments arise.

Q40. What is the Section 199A(g) deduction?

A40. Section 199A(g) provides a deduction for Specified Cooperatives and their patrons similar to the deduction under former section 199, which was known as the domestic production activities deduction. Section 199A(g) allows a deduction for income attributable to domestic production activities of Specified Cooperatives. The deduction allowed is equal to 9 percent of the lesser of (i) the qualified production activities income (QPAI) or (ii) the taxable income of the Specified Cooperative for the taxable year. The deduction is further limited to 50 percent of the W-2 wages of the Specified Cooperative for the taxable year that are properly allocable. Calculating the deduction is further explained in Q&As below.

Q41. How do Specified Cooperatives and their patrons handle the Section 199A(g) deduction?

A41. Only a Specified Cooperative may calculate the Section 199A(g) deduction. A Specified Cooperative may pass all, some, or none of the Section 199A(g) deduction to patrons that are eligible to take the deduction (this does not include a patron that is C corporation, unless that patron is a Specified Cooperative). The Specified Cooperative will reduce its deduction under section 1382 by the amount of the Section 199A(g) deduction that was passed through.

If a Specified Cooperative passes any of the Section 199A(g) deduction to a patron that is eligible, that patron is allowed to deduct the amount so long as the deduction does not exceed the patron’s taxable income (after taking into account any QBI deduction allowed to the patron).

Q42. How do nonexempt Specified Cooperatives compute the Section 199A(g) deduction?

A42. Proposed §1.199A-8 sets forth four steps to determine the amount of a nonexempt Specified Cooperative’s Section 199A(g) deduction;

1. Patronage/Nonpatronage Split – Identify and separate the gross receipts and related deductions that are from patronage sources and from nonpatronage sources. Nonexempt Specified Cooperatives may use only patronage gross receipts and related deductions to calculate domestic production gross receipts (DPGR), QPAI, taxable income, and the W-2 wage limitation.

2. Identify Patronage DPGR – Nonexempt Specified Cooperatives only consider gross receipts from patronage sources when identifying DPGR from the disposition of agricultural or horticultural products. DPGR are gross receipts of the taxpayer that are derived from any lease, rental, license, sale, exchange, or other disposition of any agricultural or horticultural product which was MPGE by the taxpayer. Such term shall not include gross receipts which are derived from the disposition of land or services. Proposed §1.199A-9 contains additional information on DPGR.

3. Calculating Patronage QPAI – Nonexempt Specified Cooperatives must compute the QPAI using the weighted average of DPGR from patronage transactions and QPAI from nonpatronage transactions. The cooperative must use the same method of accounting it uses to calculate its taxable income.

4. Compute QBI deduction – Compute QBI deduction using Section 199A(g) formula.
Cooperatives must determine cost of goods sold (COGS) and other expenses, losses, or deductions that are allocable to patronage DPGR. Proposed §1.199A-10 contains additional information on making this determination.

4. Calculating Patronage Section 199A(g) Deduction – A nonexempt Specified Cooperative's Section 199A(g) deduction is equal to 9% of the lesser of QPAI or taxable income from patronage sources, and is subject to a 50% W-2 wage limitation. A patronage Section 199A(g) deduction may only be used to reduce patronage taxable income. Proposed §1.199A-11 contains additional information on the W-2 wage limitation.

Q43. How do exempt Specified Cooperatives compute the Section 199A(g) deduction?

A43. Exempt Specified Cooperatives calculate two separate Section 199A(g) deductions, one based on gross receipts and related deductions from patronage sources, and one based on gross receipts and related deductions from nonpatronage sources. Proposed §1.199A-8 requires exempt Specified Cooperatives to perform steps two through four twice, first using only its patronage gross receipts and related deductions and second using only its nonpatronage gross receipts and related deductions. An exempt Specified Cooperative cannot combine, merge, or net patronage and nonpatronage items at any step in determining its patronage Section 199A(g) deduction and its nonpatronage Section 199A(g) deduction. Exempt Specified Cooperatives may only use the patronage Section 199A(g) deduction to reduce patronage taxable income.

Q44. How does a Specified Cooperative pass through a Section 199A(g) deduction to its patrons?

A44. Specified Cooperatives may pass through all, some, or none of their allowable Section 199A(g) deduction to patrons who are eligible taxpayers as defined in section 199A(g)(2)(D), that is, (i) a patron, that is not a C corporation, or (ii) a patron that is a Specified Cooperative. A Specified Cooperative must notify each of its patrons of the amount of Section 199A(g) deduction being passed to them in a written notice mailed to the patron during the payment period described in section 1382(d) and also include any amount passed through in such written notice on the Form 1099-PATR issued to its patrons. The amount of the Section 199A(g) deduction that a Specified Cooperative can pass through to an eligible taxpayer is limited to the portion of the Section 199A(g) deduction that is allowed with respect to the QPAI to which the qualified payments made to the patron are attributable. The Specified Cooperative will reduce its deduction under section 1382 by the amount of the Section 199A(g) deduction that was passed through.

Individual patrons that receive a written notice from a Specified Cooperative allocating a Section 199A(g) deduction may take the deduction to the extent of their taxable income determined after the QPAI deduction. A Section 199A(g) deduction that can't be used in the year it is received is lost. A Specified Cooperative that receives a Section 199A(g) deduction as an eligible taxpayer can take the deduction only against patronage gross income and related deductions, or can pass on the deduction to its patrons that are eligible taxpayers.

Q45. Can an exempt Specified Cooperative pass through its nonpatronage Section 199A(g) deduction?

A45. No. Exempt Specified Cooperatives are not allowed to pass through any of the section 199A(g) deduction attributable to nonpatronage activities because no QPAI is attributable to any qualified payments.

Q46. What if a Specified Cooperative is a partner in a partnership?

A46. The proposed rules provide that the partnership must separately identify and report on the Schedule K-1 to the Form 1065, U.S. Return of Partnership Income, issued to a Specified Cooperative partner the Specified Cooperative's allocable share of gross receipts and related deductions. This allows the Specified Cooperative partner to include the partnership items when applying the four steps in proposed §1.199A-8 required to calculate its Section 199A(g) deduction (as described in Q&A42). For example, when applying the four steps, a Specified Cooperative determines the amount of gross receipts from the partnership that are patronage and that qualify as DPGR from the disposition of agricultural or horticultural products.

Q47. What is the definition of patronage and nonpatronage?

A47. Proposed §1.1388-1(f) sets forth a definition of patronage and nonpatronage that is consistent with the current state of the law. Whether an item of income or deduction is patronage or nonpatronage sourced is determined by applying the directly related use test. The directly related use test provides that if the income or deduction is produced by a transaction that actually facilitates the accomplishment of the cooperative’s marketing, purchasing, or services activities, the income or deduction is from patronage sources. However, if the transaction producing the income or deduction does not actually facilitate the accomplishment of these activities but merely enhances the overall profitability of the cooperative, being merely incident to the association's cooperative operation, the income or deduction is from nonpatronage sources.

Rental FAQs

Q48. When is rental real estate treated as a trade or business for purposes of determining the QBI deduction?

A48. Rental real estate is treated as a trade or business for purposes of the QBI deduction under section 199A if it meets any of the following three tests:

1. The rental real estate rises to the level of a section 162 trade or business.
2. The rental real estate is a rental real estate enterprise meeting the requirements of the safe harbor provided in Revenue Procedure 2019-38. See Q49.
3. The rental or licensing of property is to a commonly controlled trade or business operated by an individual or a passthrough entity as described in Treas. Reg. § 1.199A-1(b)(14). This is often referred to as a self-rental.

Q49. When is a rental real estate enterprise eligible to rely upon the safe harbor provided in Revenue Procedure 2019-38?

A49. Revenue Procedure 2019-38 provides a safe harbor under which a rental real estate enterprise that meets certain requirements will be treated as a trade or business for purposes of section 199A. In order to rely upon the safe harbor, the enterprise must meet all requirements of the Revenue Procedure.
A rental real estate enterprise is defined as an interest in real property held for the production of rents and may consist of an interest in a single property or interests in multiple properties. The interest must be held directly or through a disregarded entity by the individual or relevant passthrough entity (RPE) relying on the safe harbor. Multiple properties of the same category (residential or commercial) can be treated as a single enterprise if the individual or RPE also includes all other properties of the same category in the enterprise. Residential and commercial property cannot be combined into a single property except for mixed-use property as discussed in Q 51. To qualify under the safe harbor, the rental real estate enterprise must satisfy all of the following requirements:

1. Separate books and records are maintained to reflect income and expenses for each rental real estate enterprise. If a rental real estate enterprise contains more than one property, this requirement may be satisfied if income and expense information statements for each property are maintained and then consolidated;

2. For rental real estate enterprises that have been in existence less than four years, 250 or more hours of rental services are performed (as described in Revenue Procedure 2019-38) per year with respect to the rental real estate enterprise. For rental real estate enterprises that have been in existence for at least four years, in any three of the five consecutive taxable years that end with the taxable year, 250 or more hours of rental services are performed (as described in Revenue Procedure 2019-38) per year with respect to the rental real estate enterprise; and

3. The taxpayer maintains contemporaneous records, including time reports, logs, or similar documents, regarding the following: (i) hours of all services performed; (ii) description of all services performed; (iii) dates on which such services were performed; and (iv) who performed the services. If services with respect to the rental real estate enterprise are performed by employees or independent contractors, the taxpayer may provide a description of the rental services performed by such employee or independent contractor generally spends performing such services for the enterprise, and time, wage, or payment records for such employee or independent contractor. Such records are to be made available for inspection at the request of the IRS.

4. The taxpayer or RPE attaches a statement to a timely filed original return, including extensions, (or an amended return for the 2018 taxable year only) for each taxable year in which the taxpayer or RPE relies on the safe harbor. An individual or RPE with more than one rental real estate enterprise relying on this safe harbor may submit a single statement but the statement must list the required information separately for each rental real estate enterprise. The statement must include the following information:

   - A description (including the address and rental category) of all rental real estate properties that are included in each rental real estate enterprise;

   - A description (including the address and rental category) of rental real estate properties acquired and disposed of during the taxable year; and

   - A representation that the requirements of this revenue procedure have been satisfied.

Certain rental real estate arrangements are excluded from the safe harbor and may not be included in a rental real estate enterprise. These include real estate used by the taxpayer as a residence under section 280A; real estate rented under a triple net lease; real estate rented to a trade or business conducted by a taxpayer on an RPE which is commonly controlled under section 1.199A-4(b)(1)(i) and rental real estate where any portion of the property is treated as a specified service trade or business (SSTB).

Q50. How can I meet the records requirement of the safe harbor contained in Revenue Procedure 2019-38 and what happens if I don't meet it?

A50: Reliance upon the safe harbor requires the maintenance of contemporaneous records, including time reports, logs or similar documents, regarding the hours of all services performed, a description of services performed, dates on which such services were performed and who performed the services.

If an employee or independent contractor performed the services with respect to the rental real estate enterprise, the taxpayer may provide a description of the rental services performed, the amount of time the employee or independent contractor generally spent performing the services for the enterprise, and time, wage or payment records for the employee or independent contractor.

The safe harbor is not available to taxpayers that fail to meet the contemporaneous records requirement. However, the rental real estate may still be treated as a trade or business for purposes of the QBI deduction if the rental real estate otherwise rises to the level of a section 162 trade or business or meets the self-rental rule. Whether rental real estate rises to the level of a trade or business under section 162 depends on all facts and circumstances.

The contemporaneous records requirement will not apply to taxable years beginning prior to January 1, 2020. However, taxpayers bear the burden of showing the right to any claimed deductions in all taxable years. INDOPCO, Inc. v. Comm’r, 503 U.S. 79, 84; 112 S.Ct. 1039, 1043) (1992); Interstate Transit Lines v. Comm’r, 319 U.S. 590, 593, 63 S.Ct. 1279, 1281 (1943). See also I.R.C. § 6001; Treas. Reg. § 1.6001-1(a)(a) and (e).

Q51. How does the safe harbor provided for in Revenue Procedure 2019-38 apply to mixed-use properties?

A51. Mixed-use property, as defined in Revenue Procedure 2019-38, is a single building that combines residential and commercial units. An interest in mixed-use property may be treated as a single rental real estate enterprise or may be split into separate residential and commercial properties. If treated as a single rental real estate enterprise, it may not be treated as part of the same enterprise as other residential, commercial or mixed-use property.

For example, a taxpayer has three mixed-use buildings and each includes a storefront and an apartment. For purposes of the safe harbor, the buildings can be included in a rental real estate enterprise in any of the following ways:

1. Each mixed-use building is treated as two separate interests in rental real estate, one commercial and one residential. The taxpayer treats these as six separate rental real estate enterprises, three commercial and three residential.

2. Each mixed-use building is treated as two separate interests in rental real estate, one commercial and one residential. The taxpayer treats the three commercial interests as a single rental real estate enterprise and also treats the three residential interests
as a separate single rental real estate enterprise. The taxpayer has two rental real estate enterprises, one commercial and one residential.

3. Each mixed-use building is treated as two separate interests in rental real estate, one commercial and one residential. The taxpayer treats the three commercial interests as a single rental real estate enterprise but treats the residential interests as three separate single rental real estate enterprises. The taxpayer has four rental real estate enterprises, one commercial and three residential.

4. Each mixed-use building is treated as two separate interests in rental real estate, one commercial and one residential. The taxpayer treats the three residential interests as a single rental real estate enterprise but treats the commercial interests as three separate single rental real estate enterprises. The taxpayer has four rental real estate enterprises, three commercial and one residential.

5. Each mixed-use property is treated as a stand-alone enterprise containing both residential and commercial properties. The taxpayer has three rental real estate enterprises, three mixed-use.

If other non-mixed-use properties are also owned or subsequently acquired, the similar properties rule under Revenue Procedure 2019-38 still applies. In other words, if the mixed-use properties are split into residential and commercial properties, the requirement to either treat all similar properties as their own enterprises or as a single enterprise will include these properties, as well. For example, if the taxpayer described in example b above acquires an additional commercial property, that new property must also be added to the existing commercial real estate enterprise. The taxpayer may not treat the newly acquired commercial property as its own enterprise.

Once an enterprise determination is made, the rules of the safe harbor are applied to each enterprise in the manner outlined in Revenue Procedure 2019-38.

Q52. If rental real estate is treated as a trade or business for purposes of the QBI deduction (discussed in Q 48), do I report the rental real estate on Schedule C of my Form 1040, and is it subject to self-employment tax?

A52. In general, the answer to both questions is no. How rental real estate is reported on Form 1040 has NOT changed due to the QBI deduction. Rental real estate is usually reported on Schedule E, Part I, and is not subject to self-employment tax.

Even if rental real estate rises to the level of a section 162 trade or business, it is generally reported on Schedule E, Part I, because rental real estate is generally excluded from self-employment taxable income under section 1402(a)(1).

However, some rental real estate is subject to self-employment tax (e.g., boarding house, hotel or motel, and bed and breakfast, where substantial services are rendered for the convenience of the occupants). Rental real estate subject to self-employment tax is reported on Schedule C.

Q53. Can rental real estate that is a trade or business for purposes of section 199A be aggregated using the rules in Treas. Reg. § 1.199A-4?

A53. Rental real estate that is a trade or business can be aggregated with other trades or businesses, including other rental real estate trades or businesses, if the rules of section 1.199A-4 of the Regulations are met. This includes rental real estate that rises to the level of a section 162 trade or business, rental real estate enterprises that meet the safe harbor requirements of Revenue Procedure 2019-38 and self-rentals as described in section 1.199A-1(b)(14).

Q54. Do I have to materially participate in rental real estate for it to qualify for the QBI deduction?

A54. No. Section 199A does not have a material participation requirement. Eligible taxpayers with income from a qualified trade or business may be entitled to the QBI deduction regardless of their level of involvement in the trade or business.

Q55. If my rental real estate generates a net loss that is limited by section 469, passive activity loss limitations, what do I do with those losses for QBI purposes?

A55. Any losses from a trade or business that are suspended and not available for use in computing taxable income in the year incurred are not included in QBI for that year. The suspended loss will be treated as qualified business net loss carryover from a separate trade or business in the year the loss is allowed for purposes of determining taxable income.

For example, Taxpayer A owns rental property that rises to the level of a section 162 trade or business. The rental property generates a $20,000 net loss in Tax Year 2018. The loss would be includable in QBI in Tax Year 2018 if it were not fully limited by section 469, passive activity loss limitations. The $20,000 loss is not included in the calculation of taxable income in Tax Year 2018, so it is not included in A's QBI for Tax Year 2018. However, if the loss is allowed for use in computing A's Tax Year 2019 taxable income, the loss will be treated as qualified business net loss carryover from a separate trade or business and will be used to calculate A's Tax Year 2019 QBI deduction.

See Q23 for more information on suspended losses.

Q56. Do I need to file information returns, such as Form 1099-MISC, if I take a QBI deduction from income generated by my rental property?

A56. As provided in section 6041, persons engaged in a trade or business and making payment in the course of such trade or business to another person of $600 or more in any taxable year may be required to file an information return reflecting the details of such transactions. Application of section 199A and its rules do not change any existing requirement for information reporting as provided under section 6041.

Q57. Triple net leases do not qualify for the safe harbor of Revenue Procedure 2019-38. Does this mean that income, gains, deductions and losses from a triple net lease can never be included in QBI?

A57. No. As explained in Q 48, rental real estate is treated as a trade or business for purposes of the QBI deduction if it rises to the level of a section 162 trade or business, is a self-rental as described in Treas. Reg. § 1.199A-1(b)(14) or is a rental real estate enterprise described in Revenue Procedure 2019-38. Revenue Procedure 2019-38 only excludes triple net leases from being included in a rental real estate enterprise (and are therefore not eligible for the safe harbor).
Here’s how people can know if it is really the IRS calling. The IRS does not:

- Call to demand immediate payment using a specific payment method such as a prepaid debit card, gift card or wire transfer.
- Generally, the IRS will first mail a bill to any taxpayer who owes taxes.
- Demand that taxpayers pay taxes without the opportunity to question or appeal the amount they owe. All taxpayers should be aware of their rights.
- Threaten to bring in local police, immigration officers or other law-enforcement to have the taxpayer arrested for not paying.
- Revoke the taxpayer’s driver’s license, business licenses, or immigration status.

People who believe they’ve been targeted by a scammer should:

- Contact the Treasury Inspector General for Tax Administration to report a phone scam. Use their IRS Impersonation Scam Reporting web page. They can also call 800-366-4484.
- Report phone scams to the Federal Trade Commission. Use the FTC Complaint Assistant on FTC.gov. They should add “IRS Telephone Scam” in the notes.
- Report an unsolicited email claiming to be from the IRS, or an IRS-related component like the Electronic Federal Tax Payment System, to the IRS at phishing@irs.gov. The sender can add “IRS Phone Scam” to the subject line.

**Tax Tips For Freelancers: How To Get Ahead Of Tax Season Now**

By Ann Schmid FOX Business

*If you are a freelance or gig worker, do not wait until January to start working on your taxes.*

“You should see your accountant now, before the end of the year,” Paul Miller, the owner of New York City-based accounting firm Miller & Company, LLP, told FOX Business.

“A lot of people would tell you, you start preparing when you’re in tax season,” Miller added. “My answer to all of my clients is, ‘I can’t help you for 2019 in 2020. I can help you now.’ People should be preparing for their taxes in November and December … The new year is too late.”
Miller said that one of the most common mistakes freelancers make is forgetting to report some of their income.

"Just because you didn't get a 1099 doesn't relieve you from the responsibility of reporting the income," Miller said.

He said that even if you didn't receive a 1099 from a client doesn't mean the client didn't send one to the government.

"A common cause of anxiety for people is [when] they get the fabulous letter from the IRS telling them they have an adjustment to their return," he said. "I see that often. It's very, very, very unsettling."

"You've got to realize if the federal government makes a change to your return, New York state is going to make a change to your return," he added. "So it's a cascading problem. But that, I find, to be a very big problem for freelancers."

One of the biggest things freelancers should consider is what entity they're operating in, Miller said.

"A freelancer should consider, are they a Schedule C, should they incorporate? What state should I be doing business in?" Miller said.

"If you don't ask the question, you don't know," he added. "I think the way you start your entity, you say, what entity should I choose? Is this the right entity for me? I need a tax consultation. I need to sit down and make sure that the way I'm operating, I'm maximizing my tax dollars and I'm in an entity that affords me the same deductions as I can get as if I'm a freelancer versus being in an S corporation or a C corporation. You know, there's a lot of considerations that you have to think about. It's not just a five-second question."

Editor's Note: Let us hope all our clients got the message to start early on their taxes.

Opinion: Here's The Formula For Paying No Federal Income Taxes On $100,000 A Year

The question of how much can we earn without paying federal income taxes is relatively easy to answer for most people.

The standard deduction for a married couple is $24,400 in 2019 (if both are under 65 years old), and the top of the 0% capital-gains tax bracket is $78,750. So we can make a total of $103,150 a year, provided that our ordinary income stays below the standard deduction and the rest comes from long-term capital gains and/or qualified dividends.

Those who aren't married should halve these dollar amounts. Note
that the IRS is increasing these numbers slightly for 2020.

With our daughter, we also qualify for the child tax credit ($2,000), so we could actually generate another $13,333 per year in dividends or capital gains, taxed at 15%. The tax liability of $2,000 exactly offsets the tax credit, for a federal tax bill of zero.

Once people file for Social Security benefits, though, things become a bit more complicated. That’s due to the convoluted formula used to determine how much of your Social Security is taxable income. So calculating and plotting the tax-free income limits is more complex.

First, a disclaimer: This exercise is for federal taxes only. That’s good enough for us personally because we live in Washington state, one of the few places without an additional state income tax. If you do have state income taxes, you will probably start owing state income taxes at much lower income levels. Also, all the other disclaimers apply here as well, including contacting a tax expert before you apply any of this.

I will also frequently mention capital gains and dividends as tax-advantaged income because long-term capital gains and qualified dividends are taxed at a lower rate. I may sometimes drop the terms “long term” and “qualified” because it doesn’t always fit into the chart axis labels. But keep in mind that short-term capital gains and nonqualified dividends will fall into the ordinary-income bucket, taxed at a higher rate.

Tax-free income limits without Social Security

Just to warm up, here are the income limits for a married couple (both under 65 years old) who file a joint federal tax return. They can claim a $24,400 standard deduction in 2019 as well as up to $78,750 of long-term capital gains taxed at 0%. So to stay tax-free, we need to stay under the blue line in the chart below.

\[
\text{Tax} = F2 (\text{Taxable Social Security + Ordinary Income }, \text{Capital Gains})
\]

(Side note: There’s a fourth category, municipal-bond interest income, because that enters the Social Security worksheet formula as well but stays tax-free otherwise.)

So it’s no longer feasible to display the tax-free income limits in a simple one-size-fits-all chart because our tax liability depends on three distinct variables, and I can’t easily plot that zero-tax boundary in three dimensions. So, here’s how I did it.

- Start with Social Security on the x-axis. I used a range of $0 to $90,000, which is probably close to the absolute maximum two spouses can haul home in combined benefits.
- On the y-axis, plot the maximum of the “other income” to guarantee zero federal taxes. This is the combination of all ordinary income and dividends and capital gains (i.e., Line 3 in the Social Security worksheet).
- How much “other income” is sustainable at zero taxes clearly depends on the composition: ordinary income vs. tax-advantaged income (long-term capital gains and dividends). So I plotted a line for three different cases: 100%/0%, 50%/50%, and 0%/100% in the two income buckets.
- I also assume that this is for a couple where both spouses are 65 years or older to increase the standard deduction to $27,000 ($24,400 base plus $1,300 extra per spouse above age 65).

Let’s look at the results:

- The lowest tax-free income allowance prevails if all of the other income is ordinary income. Say you get $50,000 in combined Social Security, then you can make around another $20,000 in other ordinary income. The sustainable amount of income gradually declines because more Social Security income will become taxable and limit the amount of other income you can make before hitting the $27,000 standard deduction. But you can still haul in a lot of income: $50,000 in Social Security and another $20,000 in ordinary income. Or $90,000 in Social Security plus another close to $11,000 in other ordinary income for a total of more than $100,000.
- Not surprisingly, that boundary shifts up if part of the “other income” is long-term capital gains. That’s because less of the
2019 Year End Tax Advice For Farmers And Ranchers

By: Russell Nemetz - Montana AG Network

From lower commodity and livestock markets to weather challenges, 2019 has been a very challenging year for a lot of Montana farmers and ranchers.

“We're encouraging people to get in, get their records up to date, figure out where they're at and come talk to their CPA about what moves might be good to even out the income,” said Barnekoff.

“Maybe even minimize the loss and pull some income back into 2019 if they can.”

He also offers this tax advice for those producers who need or want to make equipment or facility updates.

“Fast depreciation is available for pretty much any asset that's bought and put into service on a farm or ranch,” said Barnekoff. “Those options are great. They're available with great flexibility.”

“Also, there's a lot of flexibility in deciding when you pay expenses or when you collect your income. If you want to put it in this year or next year, there's huge flexibility that way. So, we’re working with people that way, as we always do,” he added.

He says the new tax bill that was passed in 2017 really has helped farmers and ranchers, especially during these challenging times here of late.

“You know, we have a few new deductions, some lower tax rates and different structures,” said Barnekoff. “I’d say what happened in 2017 with the tax bill, it’s been good for farmers and ranchers. And we’re really pleased to have more tools in our toolbox to help everybody.”

He also offers this tax advice for those producers who need or want to make equipment or facility updates.

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“Also, there's a lot of flexibility in deciding when you pay expenses or when you collect your income. If you want to put it in this year or next year, there's huge flexibility that way. So, we’re working with people that way, as we always do,” he added.

Advisers Expect More Roth Conversions Under The Secure Act

Clients likely will want to reduce tax burden on inheritors given law's limits on 'stretch IRAs'

By Mark Schoeff Jr.

Investment advisers expect a pickup in the conversion of traditional individual retirement accounts to Roth IRAs as a result of the SECURE Act, which reached another milestone.
The Senate approved, 71-23, part of a $1.4 trillion budget package that includes the Setting Every Community for Retirement Enhancement Act. The funding measure will finance the government through September and avert a shutdown.

The House of Representative approved the piece of the budget legislation containing the Secure Act. The legislation, now headed to President Donald J. Trump to be signed into law.

Beginning Jan. 1 for many of its provisions, the Secure Act would implement substantial policy changes designed to increase retirement savings. They include providing legal protections for employers that offer annuities in retirement plans, making it easier for small businesses to band together to sponsor retirement plans, and increasing the age for required minimum distributions to 72 from 70½.

To pay for those reforms, the bill would require most non-spouse beneficiaries of IRAs to take distributions over 10 years instead of over their lifetimes. That limitation on so-called "stretch IRAs" could cause a stampede toward Roth IRAs.

Converting from a traditional IRA, which allows tax-free contributions and then taxes withdrawals, to a Roth IRA, which applies the tax on contributions rather than withdrawals, would ease what could be a substantial tax bill for IRA inheritors after a decade.

People who have saved $1 million or more in an IRA and plan to pass it on to someone other than their spouses should consider doing Roth conversions, said Ed Slott, president of Ed Slott & Co., which specializes in IRA education and training.

For instance, if their children inherit the IRAs, they would likely receive them and face the tax consequences during their prime earning years.

"It's a big tax hit," Mr. Slott said. "Beneficiaries can let the money accumulate tax-free in a Roth."

Investment advisers are going to put a premium on Roth conversions.

"It is going to be critical to execute Roth conversions on the highest scale possible," said Justin Brownlee, owner of Brownlee Wealth Management. "Prior to the Secure Act, the difference between doing Roth conversions from ages 60 to 70 and not doing them could be millions of dollars over a few decades. Now it's even more extreme. A Roth conversion is going to be more powerful than taking Social Security at an early age."

Rob Greenman, a partner at Vista Capital Partners, said advisers already have been having Roth conversations with their clients. The passage of the Secure Act adds urgency to those discussions.

"Now that the rules of the game have changed, it could change the math in terms of how much to convert and in what time frame," Mr. Greenman said.

With the adjustment in the RMD age, the Secure Act provides a bigger window for Roth conversions at a time when the 2017 tax reform law has reduced marginal rates.

"They can spread the conversions over more tax years and enjoy the low tax rates," said Vid Ponnapalli, president of Unique Financial Advisors. "This is a great opportunity to do as much conversion as possible."

Doing Roth conversions would make passing IRAs between generations smoother, said Travis Gatzemeier, founder of Kinetix Financial Planning.

"They don't have to worry about deploying any tax strategies to mitigate their tax liability," he said. "It's a cleaner transfer of wealth." Roth conversions also would benefit the government, which would get tax revenue more quickly than it would under IRA distributions. But the change in stretch IRA policy under the Secure Act will upset many estate plans that were written based on children being able to hold onto IRAs for their lifetimes.

"I call this section of the Secure Act the broken promise," Mr. Slott said. "It's like they changed the rules in the ninth inning."

**Four Common Tax Errors That Can Be Costly For Small Businesses**

A small business owner often wears many different hats. They might have to wear their boss hat one day, and the employee hat the next. When tax season comes around, it might be their tax hat.

They may think of doing their taxes as just another item to quickly cross off their to-do list. However, this approach could leave taxpayers open to mistakes when filing and paying taxes.

Accidentally failing to comply with tax laws, violating tax codes, or filling out forms incorrectly can leave taxpayers and their businesses open to possible penalties. The IRS encourages small businesses to explore using a reputable tax preparer – including certified public accountants, Enrolled Agents or other knowledgeable tax professionals – to help with their tax situation. Filing electronically can also help avoid common errors.

Being aware of common mistakes can also help tame the stress of tax time. Here are a few mistakes small business owners should avoid:

**Underpaying estimated taxes**

Business owners should generally make estimated tax payments if they expect to owe tax of $1,000 or more when their return is filed. If they don't pay enough tax through withholding and estimated tax payments, they may be charged a penalty.

**Depositing employment taxes**

Business owners with employees are expected to deposit taxes they withhold, plus the employer's share of those taxes, through electronic fund transfers. If those taxes are not deposited correctly and on time, the business owner may be charged a penalty.
Filing late

Just like individual returns, business tax returns must be filed in a timely manner. To avoid late filing penalties, taxpayers should be aware of all tax requirements for their type of business the filing deadlines.

Not separating business and personal expenses

It can be tempting to use one credit card for all expenses especially if the business is a sole proprietorship. Doing so can make it very hard to tell legitimate business expenses from personal ones. This could cause errors when claiming deductions and become a problem if the taxpayer or their business is ever audited.

Social Security Offices Will Return To Full Public Service Hours

Wednesdays to Return to Full Public Service Hours; Agency to Hire 1,100 Direct Service Employees.

Starting on January 8, 2020, Social Security offices nationwide will be open to the public on Wednesday afternoons, Andrew Saul, Commissioner of Social Security, announced. This change restores Wednesday public service hours that were last in place in late 2012.

“I don’t want someone to come to our office at 2:30 on a Wednesday only to find our doors closed,” Commissioner Saul said.

For more information, please visit https://www.ssa.gov/news/press

When Can I Expect My 2020 Income Tax Refund?"

IRS Accepts Between These Dates === > Direct Deposit Sent (Or Check Mailed)

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* = IRS may delay tax filing season by one week or more due to changes in tax law.

** = Returns with EITC or CTC may have refunds delayed until late February to verify credits.

*** = Filing during peak season can result in slightly longer waits.

Important: If you file electronically (using an online tax program or preparer), the IRS will notify you of the actual date they "accepted" your return. This is often 1-3 days from the time you actually hit the "file" button, and it is this date that you need to use for the above chart.

Taxpayers who mail a paper version their income tax return can expect at least a 3-4 week delay at the front-end of the process, as the return has to be digitized before it can be processed.

Editor's Note: These dates are approximations and should not be relied upon for accuracy.

Tax Practice Management

Using Strong Password Is A Strong Defense Against Identity Thieves

Two things taxpayers can do to prevent themselves from identity theft is to use strong passwords and keep those passwords secure. While many people use fingerprint or facial recognition technology to protect their devices, sometimes it's still necessary to use a password. In recent years, cybersecurity experts' recommendations on what constitutes a strong password has changed. With that in mind, here are four tips for building a better password:

- Use word phrases that are easy to remember rather than random letters, characters and numbers that cannot be easily recalled.

- Use a minimum of eight characters; longer is better.

- Use a combination of letters, numbers and symbols, i.e., XYZ, 567, !@#.

- Avoid personal information or common passwords.

Writing strong passwords isn't the only way to keep data secure. Here are a few more tips for folks to remember. People should:

- Change default and temporary passwords that come with accounts or devices.

- Not reuse passwords. Rather use a completely different password for every account and device.

- Give a password a total makeover when changing it. For example, simply changing Bgood!17 to Bgood!18 is not good enough.

- Not use email addresses as usernames, if that's an option.

- Store any password list in a secure location, such as a safe or locked file cabinet.
• Not disclose passwords to anyone for any reason.
• Use a password manager program to track passwords if you have numerous accounts.

Whenever it is an option for a password-protected account, users also should opt for a multi-factor authentication process. Many email providers, financial institutions and social media sites now offer customers two-factor authentication protections.

Two-factor authentication helps by adding an extra layer of protection. Often two-factor authentication means the returning user must first enter credentials like a username and password. Then they must do another step, such as entering a security code texted to a mobile phone.

What to Do if Someone Files a Fraudulent Tax Return in Your Name
By Maryalene LaPonsie and Teresa Mears

However, that's a reality for thousands of people each year. In 2018, the Federal Trade Commission received 38,967 reports of identity theft for tax fraud, a 38% decrease from the year before.

Fraudulent tax returns can be a headache, but they typically don't result in a taxpayer losing their refund. "It's probably going to be fine," says Bill Smith, a managing director for the accounting firm CBIZ MMH's National Tax Office, based in Bethesda, Maryland. However, that doesn't mean you'll be getting your refund quickly. Smith estimates that it takes the IRS about six months to investigate and issue a refund to the appropriate person in many of these cases. Fortunately, you can avoid a delay in your refund by taking steps to prevent tax identity theft in the first place. Read on to learn how to keep your data safe, how to know when someone has filed a fraudulent tax return in your name and what steps to take if you become a victim.

How to Prevent Tax Identity Theft

There is nothing unique about how fraudsters steal personal information for tax fraud. "Usually it originates with a traditional identity theft scheme," says David Britton, vice president of industry solutions, global identity and fraud at global technology company Experian.

That means many of the best practices you should already be employing to keep your data safe will protect you against tax identity theft. These include the following six strategies:
• Use strong passwords.
• Watch out for scams.
• Don't carry your Social Security card or number.
• Send sensitive information over secure channels.
• File as early as possible.
• Only work with reputable tax preparers.

Use strong passwords. Strong passwords that combine letters, numbers and characters are now required on many websites. Even if they aren't mandatory, you should use them. "It's so important for people to protect themselves," says Ana del Cerro-Fals, principal in the tax and accounting department for the Miami office of accounting firm MBAF. Use a different strong password for every one of your financial accounts and opt in to two-factor authentication if offered. This option will require you to verify your login through a secondary method, such as entering a code sent via text.

Watch out for scams. Scam emails, texts and calls are often how fraudsters collect sensitive data. "A lot of identity theft starts with things like old-fashioned phishing attacks," Britton says. In these attacks, criminals may impersonate your bank or a trusted website and send fraud alerts or other notifications. When you respond to them, you may be asked to provide your Social Security number or password. These sorts of requests should be red flags. "If it doesn't feel right, it's probably not right," Britton says.

Sometimes criminals will pretend to be IRS agents, and an unsolicited call from the agency should be another tipoff that a scam is afoot. "The IRS doesn't contact you out of the blue," Smith says. "If you get an email from the IRS, it's not from the IRS." The agency uses postal mail for most communications and will never call or email to request financial information.

Don't carry your Social Security card or number. There is no reason to have your Social Security card or number with you at all times. If your wallet is stolen and it contains both your driver's license and Social Security number, a thief will have everything he or she needs to file a fraudulent tax return in your name.

Send sensitive information over secure channels. There are instances when you might need to give someone your Social Security number. For example, a tax preparer will need it to complete your return. However, sending it via an unsecured email or over the phone in a public location can be a mistake. "Be very careful when sending your Social Security number electronically," del Cerro-Fals says. She notes her firm has a portal where clients can log in to share sensitive data. This ensures it isn't sent in emails that could be intercepted by criminals.

File as early as possible. Scammers usually file returns as soon as tax filing opens, hoping to receive refunds before the real taxpayers report their fraud. However, if you get your return in first, the fraudulent filing can't be processed. "One of the best remedies is to file early," Britton says.

Only work with reputable tax preparers. Tax preparers have been both victims and perpetrators of scams. If you hire someone else to do your taxes, hire someone with good references and experience. You can check whether preparers hold credentials recognized by the IRS. While vetting preparers, ask what security measures they use to protect your data.

How to Know if Someone Filed a Return in Your Name

If the IRS flags problems with your return, you'll get a letter before any refund is issued. That gives you the opportunity to tag the initial return as fraudulent and then file normally.

"They have systems to try to identify suspicious returns," explains Jeffrey Craig, principal and senior wealth advisor with the financial planning firm The Colony Group in Boston. If the IRS algorithms don't detect any anomalies and process the fraudulent return, you won't find out about it until you try to file your own return and have it rejected.
Of the two options, the second is most common. "By and large, for most people, it's the e-file rejection notice (that notifies taxpayers of a problem)," Smith says.

That notification won't provide specific information though. "They are not very detailed in their reasons," del Cerro-Fals says. Instead, the notification will indicate there was a problem with the Social Security number. Assuming you haven't transposed any numbers, it's likely that tax identity theft is the reason for the rejection.

What to Do if You're a Victim of Tax Identity Theft

If you do discover someone has filed a fraudulent tax return in your name, here are eight steps to take:

- Complete a paper return.
- File Form 14039.
- File a police report.
- File a report with the Federal Trade Commission.
- Request a copy of the fraudulent return.
- Check your credit reports and account statements.
- Put a credit freeze on your accounts.
- Get a PIN for tax filing.

Complete a paper return. "The fact that your e-filed return was rejected doesn't mean you don't have to file," Craig says. Be sure you submit a paper return, along with any required payment, by the filing deadline to avoid tax penalties or late fees.

File Form 14039. Fill out and attach Form 14039, Identity Theft Affidavit, with your paper return. If you receive a letter from the IRS or otherwise suspect you’re the victim of ID theft, you can also complete and mail this form. Your case then goes to the Identity Theft Victim Assistance organization, which will request documentation proving your identity. That documentation can vary by case but may include copies of your driver's license, Social Security card or utility bills, del Cerro-Fals says.

File a police report. Next, file a police report with your local law enforcement agency. "The police probably aren't going to go out and find the culprit," Craig says. However, having a report might be useful to stop collection efforts if your identity is used to rack up debt as well.

Your fraud may also be part of a larger local fraud scheme. The more information the police have, the better chance they have of cracking the criminal enterprise. Depending on the size of your local police department, there may even be a division that deals with financial crimes or ID theft.

File a report with the Federal Trade Commission. While the FTC doesn't investigate identity theft cases, it does compile statistical information on the crimes and offer helpful information on its website for taxpayers who face this situation. Visit IdentityTheft.gov to file a report and receive a recovery plan.

Editor's Note: Needing a Tax Practice Policy Manual or CyberSecurity Plan for your tax practice, go to Resources on www.ncpeFellowship.com and scroll down to "T" - Tax Practice Policy Manual. Both are there for your use.

Number Crunching: Guide On How To Start a Tax Practice Business

The IRS processes 238 million tax returns every year. While some people will do it alone, many more turn to a trusted tax professional to assist them with filing.

The person they turn to could be you. If you already do bookkeeping, have strong math skills, and love details, then starting a tax preparation business could be a wise choice for you.

There's just one problem. How do you go about setting up your own tax preparation business? We put together this comprehensive guide to help.

Start With the Training

Before you start a tax preparation business, you'll need to get the right training.

There are a few different types of tax preparers. All have some basic training in preparing taxes.

The basic course will ask you to put in around 60 hours of training time. The fee usually isn't too high, and you can find these courses offered by major tax franchises.

Becoming a Certified Professional Accountant, or CPA is the most intensive route. CPAs are the most qualified type of tax preparer.

If you're doing tax returns for individuals, you may not feel the need to complete CPA training. If you want to serve small businesses or prepare corporate taxes, more training is a good idea.

You can always start with basic training and then gain more qualifications later on.

Gain Some Experience Preparing Taxes

Next, you should gain some experience preparing taxes. It's a good idea to have at least a few tax returns under your belt before you open your doors as a tax preparer.

First, experience helps you hone the skills you develop in your educational training. Practice makes perfect, after all. Next, you'll also be challenged more with real-life tax returns.

Finally, getting some experience can help you develop expertise in a certain area. Maybe you're great at preparing taxes for small businesses. Maybe corporate taxes are your forte.

By getting some experience doing each, you can discover where your true talent lies. It may also tell you which kinds of clients you like working with most. Do you like helping individuals, or do you love the challenge that small businesses present?

Decide on Your Clientele

Discovering your talents and passions is important when having a tax prep business. You need to decide who you're going to serve.

Many tax preparers work with a wide range of clients. If you excel at preparing individual tax returns, focusing on those clients makes sense. It can also help you streamline your business.

Picking a focus is important for businesses that are just starting out. First, it helps you craft a brand message. If you don't serve individual taxpayers, then your messaging needs to reflect that.
It can also help you decide on other aspects of your business. You may not need the same tools for preparing individual taxes as you do for handling small business returns.

If you know who your target client is, you can focus on serving them and their needs. Knowing this can save you from buying tools you don’t need or spending on marketing that doesn’t work.

Put Together a Budget

As you prepare to start a tax prep business, you’ll want to take a look at the costs. To that end, you should prepare a budget.

The budget will guide your business spending as you get off the ground. You’ll want to examine start-up costs around tax prep businesses.

What licenses will you need to pay for? Are there any fees you’ll need to pay upfront before you begin accepting clients?

You’ll also want to become familiar with the operating expenses of the business. These are ongoing costs, which you’ll pay year after year. They’re the cost of doing business.

Common expenditures associated with tax prep businesses include:

- The cost of tools like software and computer equipment
- Rental space or a mortgage
- Business insurance
- Marketing expenses
- Utilities, like telephone lines and electricity costs

If you hire anyone to work for you, you may also have salary and payroll costs. You may even need to think about worker’s compensation insurance or benefits. Banking fees, compliance costs, and more will also need to be factored in.

If you want to apply for any kind of credit to fund the business, you’ll need to include a budget in your business plan. Loans can help you get your business off the ground, but you’ll need to show lenders a solid plan for creating a successful business.

Register the Business

Now we come to the finer details of how to start a tax business. You’ve done the training, thought about your clientele, and laid out how you’ll pay for it all.

It’s time to register your business. This act creates the business as a legal entity. In short, it makes your tax prep business a reality. The first step in registration is usually filing with your state. Most states will have a form that allows you to register a “Doing Business As” name for the business.

You can also choose to operate as a limited liability corporation or LLC. If you choose this option, you don’t need to file the “Doing Business As” name. This step is already included.

Setting up an LLC is usually more involved, so you may not feel the need to take this step immediately. It can provide your business with more protection.

Once you’ve registered the business, it’s time to get set up with the IRS.

Getting Your PTIN

You’ll need a preparer tax identification number or PTIN. Without this number, you can’t charge anyone for tax preparation.

Getting a PTIN is a simple online process. You’ll need to renew the number each year. If you hire anyone else to work for you, they must also have their own valid PTIN.

Getting Your EFIN

If you plan to file 11 or more tax returns, the IRS requires you to file electronically. As a business owner, you probably hope to file more than ten returns. Even if you don’t file this many tax returns in your first year of business, it’s a good idea to get your EFIN.

EFIN stands for electronic filing identification number. Once you have this number, you’ll be an Authorized e-File Provider.

To get an EFIN, you’ll need to submit an application. There are no fees for applying, but you may need to complete suitability checks. Suitability checks include:

- A tax compliance check
- A credit check
- A criminal background check
- A check for prior non-compliance with the IRS e-File system

Your state may also need separate e-File registration.

If you employ people for your business, you may also need an employer identification number.

Choose a Location for Your Tax Preparation Business

Now you can think about where to locate your new tax prep business. Many tax preparers work out of a home office. This is especially true for those who deal primarily with individual tax filings.

This is because many people start their tax businesses as side gigs. The work can be very seasonal, so you may yourself quite busy from February through April.

If you plan to offer other services or you work with businesses, then you may have a steadier stream of work. Businesses need to remit payroll taxes all year round. Some people need to pay the IRS on a quarterly or monthly basis.

Location can be quite important to the success of your business. A small office near the business district may be the best choice if you work with industry or business clients.

Always think about making your office easy to locate and get to. How visible is it from the street? Will people driving by know there’s a tax preparation service in this plaza or building?

Convenience also plays a role. A business that’s close to your office may choose to do business with you because you’re close by. An individual may find it convenient to manage all their finances if your office is next door to their bank.

Invest in the Right Tax Prep Tools

Preparing taxes can be quite time-intensive. You need to be familiar with the ever-changing tax code, and you also have to have a great
eye for detail. It’s not just about crunching numbers, although good math skills are essential.

There are plenty of tools out there designed to help tax preparation professionals. They help you save time and streamline your work, so you can prepare tax filings faster.

They can also help you double-check your work so that you don’t make costly mistakes on client filings. Some professional tax software can even help you stay up to date with the tax code.

Don’t forget about the hardware either. You’ll need a computer to run your software, as well as printers and scanners. Smartphones can help you stay on top of all your communication tasks, from email to scheduling meetings.

Spread the Word About Your Business

Now we get to the fun stuff. You’re starting a tax preparation business, but who knows about the services you offer?

You’ve probably told a few people. If you’ve prepared taxes for some people before, they may be excited to hear you’re opening your own business.

If you want to be successful and grow your business, though, you’re going to need a much wider reach. That’s where marketing comes in. You’ll want to make sure you’re present on the web and social media. A professional-looking website makes it easy for people to discover your business and reach out to you. Good SEO helps people searching “tax preparation near me” find you.

You may also want to engage in some PR for your business. Contact local media around tax season and see if they’d be interested in setting up an interview. You can share tax tips or other expert advice to help people get through tax season.

You may also want to try paid advertising. A sign outside your business can advertise a deal for new clients. A flyer about your services can help you spread the word to other people who might be looking for a tax preparer.

Get Your Finances in Order

Starting a tax business means you need to have some way to collect payments. It’s easy to accept cash and checks, but some of your clients may want to pay other ways.

You can get set up with merchant accounts so you can process debit and credit card transactions. Depending on your clientele and how much you charge, having these options available is key.

Another consideration is business financing. We mentioned before that you’ll need a budget if you plan to apply for credit. A business credit card or another type of loan can help you manage your business expenses.

Finally, you’ll want to set up a business account with your bank. You’ll likely have more money coming in and out of your account. The business account will manage your banking costs more effectively.

Patience Is a Virtue

Our final tip for starting your own tax prep business is to be patient. Rome wasn’t built in a day, and neither is any great business.

You may start off small. With the right market and financial know-how, you’ll be able to grow your customer base and expand your business.

You may want to consider expanding the services you offer. As you grow, you’ll also need to consider the tools you use and the people you have on your team.

In business, it’s better to wait until you need a tool or a second set of hands than hiring someone immediately. Be patient, and you’ll lay a solid foundation to grow a successful business firm.

Question of the Month

Can A Trust Make A Loan To A Beneficiary?

The Trustee's Power to Loan

Trust agreements often give trustees the power to make loans. When and how to exercise the power should be given significant thought. Upholding the fiduciary duty owed to all beneficiaries is always a key concern. Consideration of tax implications, due diligence and documentation are essential.

Loans To Beneficiaries

A loan taken from a trust can be good for the beneficiary or the beneficiary's business and can be an alternative to making an outright distribution to the beneficiary. In determining whether to make a loan to a beneficiary, the trustee should consider the following:

- The trustee should first determine whether the trust agreement (and not merely a trust certification) permits the trustee to loan money. If prohibited, the trustee may not make the loan.
- If permitted, proper internal procedures, similar to those for making an outright distribution to a beneficiary, should be followed and documented.
- Once it has been determined that the trustee has the authority to make a loan to a beneficiary, and subsequent to the trustee’s proper exercise of its discretion to make such loan, the collateral security requirements of the loan must be considered by the trustee. A beneficiary may benefit from relaxed collateral security requirements for the loan, as standard commercial lending criteria may be modified to suit the needs of the beneficiary. Nonetheless, the trustee should ensure that there is sufficient collateral for the loan, as the loan will be a trust asset and may be scrutinized for proper portfolio management by the beneficiaries or a court having jurisdiction over the trust.
- The ability of the beneficiary to repay the loan must also be considered. If the trustee knows that the beneficiary will be unable to repay the loan, the loan could be challenged by the IRS and may be re-characterized as a disguised distribution to the beneficiary, which could cause an adverse income tax result for the beneficiary.
- Although Congress has eliminated the tax advantages of interest-free loans, a trust loan with a below-market interest rate can be an attractive and viable financing option for a beneficiary. Provided the trustee complies with certain rules prescribed by
the IRS pertaining to adequately stated interest, the trustee could
decide to make a loan to a trust beneficiary in order to suit the
needs of the beneficiary. For example, Rev.Rul. 2015-03 contains
the minimum required interest rates for loans made in April 2015
and provides for (i) a short term rate for demand loans and loans
with terms of up to 3 years equal to 0.48%; (ii) a mid-term rate
for loans from 3 to 9 years equal to 1.70%; and (iii) a long-term
rate for loans over 9 years equal to 2.47%. These rates are
significantly lower than rates that would be commercially available
to the beneficiary and, in general, may be used to the benefit of
the beneficiary without an adverse income tax result.

• Finally, all loans made to a trust beneficiary should be
supported by appropriate documentation, such as a promissory
note, and, if necessary, a collateral security agreement.

Repayment of a loan from a trust can be made from money the
beneficiary might otherwise have been entitled to receive from the
trust, or trustees can make loan payments on behalf of the beneficiary.
The specific language of the trust and the powers expressly conferred
upon the trustees determine these issues. Because of the significant
fiduciary obligations associated with making a loan to a beneficiary,
and because the IRS may carefully examine the loan transaction
to determine the appropriate tax treatment to the trust and the
beneficiary, the trust loan transaction should be carefully considered
and documented by the trustee and its counsel. McNees attorneys
have the fiduciary, tax and lending experience to help corporate
fiduciaries navigate and document the complexities of trust loan.

Editor's Note: Rev. Rul. 2019-16 is the Revenue Ruling regarding
interest rates, applicability of short-term and long-term, to loans.

Military News

Here’s When Your Military 2019 Tax Statement Will Be Ready

Tax statements for all members of the active duty and Reserve
components will be available online no later than Jan. 22, according
to the Defense Finance and Accounting Service.

Dates vary by the different components:

• Jan. 7: Reserve Army, Navy, Air Force W-2 statements
• Jan. 11: Active and Reserve Marine W-2 statements
• Jan. 22: Active Army, Navy, Air Force W-2 statements
• Dec. 19: Retiree 1099R statements

For those who receive their tax statements by mail, your statement
will be mailed no later than Jan. 31.

If you’re looking to jump on filing that tax return if you think you’ll get
a refund, you can’t do that immediately. The Internal Revenue Service
doesn’t start accepting tax returns generally until late January. That
start date hasn’t yet been announced, but it should be announced in
early January.

Author Karen Jowers

Karen has covered military families, quality of life and consumer
issues for Military Times for more than 30 years, and is co-author of
a chapter on media coverage of military families in the book "A Battle
Plan for Supporting Military Families." She previously worked for
newspapers in Guam, Norfolk, Jacksonville, Fla., and Athens, Ga.

Gold Star Families, Hit By Surprise Tax Bills, Get Relief
In Budget Deal

Gold Star families hit by unexpected, large tax bills earlier this year
will see that debt erased under language included in the massive
federal budget deal passed by Congress this week.

Advocates have said the so-called military “kiddie tax” cost some
families as much as $10,000 last spring, and could have meant
even bigger bills next spring for thousands of families. Now, under
the fix included in the $1.4 trillion budget deal headed to the White
House, that burden will be erased and families will be able to apply
for refunds for last year’s taxes.

“Our service members protect our nation, but they also protect their
families,” said Kelly Hruska, government relations director at the
ensures the service and sacrifice of their parents is recognized and
honored.”

By: Leo Shane III

The problem stemmed from the tax code overhaul passed in 2017,
which mandated that certain minors with unearned income be taxed
at a rate as high as 37 percent. The idea behind that change was to
prevent families from using underage children to shield income for
tax purposes.

But the move was particularly traumatic to military families who lost a
loved one on duty and saw their Defense Department death benefits
suddenly taxed at a much higher rate. While those benefits typically
go to a spouse, in some cases families have transferred them to
children to counter a separate offset problem known as the military
“widow’s tax.”

Lawmakers corrected that offset in the annual defense authorization
bill passed by Congress earlier this week. But that move didn’t
provide any relief for families hit by the “kiddie tax.”
In a statement, Rep. Elaine Luria, D-Va. and the sponsor of the tax fix language, called the measure an urgent priority to help “America’s most heroic families” recover from a congressional mistake.

The fix itself had been non-controversial, with members from both parties expressing support for the idea over the last few months. But the legislation was stalled amid other budget fights until the final days of this year’s session.

**Estate and Trust News (And Gifting)**

**Gift Tax in 2020: How Much Can I Give Tax-Free?**

Gift-giving season is upon us, and for many people, coming up with the cash to afford presents for loved ones is a huge challenge. For wealthier gift givers making larger gifts, there’s another issue to keep in mind: whether you'll owe any gift tax to the federal government.

Gift taxes are complicated. Tax rates on taxable gifts are high, but there are several provisions you can use to escape the tax entirely. Based on current law, it’s rare for anyone to owe any gift tax. Below, we’ll walk you through what you need to know.

**How the gift tax works**

The key to understanding how the U.S. taxes gifts is that the tax system seeks to combine gifts you make during your lifetime with bequests from your estate at your death. What that means is that dead or alive, any money that you transfer to someone else is potentially subject to gift and estate tax.

In order to avoid taxing everyone on the tiny gifts they make throughout the course of the year, though, lawmakers recognized the value of letting people make some gifts tax-free. The annual exclusion amount gives everyone the right to make gifts up to a certain amount each year to someone without having to worry about anything related to gift taxes. For 2020, that amount is once again $15,000, the same as it's been for several years.

The annual exclusion amount applies to each recipient of a gift from a donor. So you can give up to $15,000 to one person while making another $15,000 gift to someone else -- all without triggering any gift tax.

**Why big gifts still might not trigger gift tax**

If all your gifts are under $15,000 for the year, then you're all set. But even if you make bigger gifts, you still might not owe any gift tax.

There are two reasons why. First, there are some gifts that you're allowed to make tax-free in larger or even unlimited amounts, including:

- Gifts to spouses who are U.S. citizens
- Gifts to charity
- Gifts for tuition and qualified educational expenses that you make directly to the educational institution
- Gifts to cover medical expenses for someone else that you make directly to the provider of the medical services

Note that for gifts related to educational or medical purposes, it's critical for you to make the gift directly to the institution in question. If you give it to the student or patient first, then it doesn't qualify for the exclusion and can get treated as a taxable gift.

In addition, even if your gifts don't qualify for any of those exemptions, you're also entitled to a lifetime exemption from gift and estate tax. In 2020, that exemption amount jumps to $11.58 million.

**How it all adds up**

To understand this better, consider an example. Say you make $15,000 gifts to three different people and give a fourth person $75,000. The three $15,000 gifts all qualify for the annual exclusion and therefore have no gift tax consequences. The fourth exceeds $15,000, making $60,000 of the gift potentially taxable.

If the fourth person is your spouse, then you'd qualify for the unlimited marital deduction, and you still wouldn't have any gift tax consequences even on the $60,000. If the recipient of that gift isn't your spouse, then the $60,000 would be taxable. However, you'd still get to use your $11.58 million lifetime exemption amount, and you'd have $11.52 million left to use for the rest of your life and in your estate.

**Make gifts worry-free**

Many people are scared of the gift tax when they're doing their tax planning, but it really affects very few people. With a $15,000 annual exclusion continuing for 2020, gifts won't be a tax problem for the vast majority of Americans in the coming year.

**Beneficiaries Of Estate Are Liable For Estate Taxes**

Normally the estate tax is paid by the estate. Sometimes beneficiaries receive so many of the assets directly, there isn't enough left in the estate to pay the tax. This case involves late filing as well as nonpayment of the tax. Each beneficiary ended up being liable a pro-rata portion of the tax based on that beneficiary received, even if received directly.

In this case Harold Arshem, the decedent, had listed some beneficiaries directly on some assets. Upon the decedent’s death in December 1999, these assets went directly to the named beneficiaries and were not controllable by Mr. Arshem’s will.

He had made a few large gifts shortly before his death including gifting a remainder interest in the family farm to a grandson. He bequeathed the remainder of his estate into three equal parts for his three daughters, one of which was Donna Ringling.

The three daughters were appointed the executors of his will. An inheritance tax report was filed in South Dakota. This report incorrectly showed the county assessed values of the real estate instead of their appraised values.

In June 2003, a court appointed Stan Whiting as special administrator to take over the estate proceedings. In August 2003 the court ordered
Mr. Whiting to amend the inheritance tax report with South Dakota and filed a Form 706, Estate Tax Return, with IRS. On April 14, 2008, one of the daughters signed the Form 706 which reported a gross estate of about $834,000 and a net tax due of just under $29,000 but nothing was paid with the return. In July 2008 IRS sent a bill for the tax, plus assessments for late filing penalty, late paying penalty, and interest with the total coming to about $65,000. Another notice was sent by IRS in November 2008. The special administrator had amended the South Dakota report, filed the Form 706, and advised the beneficiaries of the amount each owed for the tax. Since his court assigned duties were completed, he applied for release of his duties in December 2008. Nothing in the case summary explains why the filings took so long to be completed, but they were obviously late.

In January 2010, Ms. Ringling requested IRS abate the interest and penalties. IRS denied the request. Over the next several years IRS sent notices of the amounts due as well as a various other forms and notices over the years.

IRS has pursued each of the beneficiaries for a portion of the unpaid assessment against the estate equal to their pro-rata share of assets received.

The District Court sided with IRS stating each beneficiary was required to pay a pro-rata portion of the estate tax based on the value the beneficiary received. It would appear this requirement would also apply to any taxes the decedent owed prior to death.

_Donna Ringling, District Court, South Dakota District, 2/21/19._
_This text has been graciously shared courtesy of David & Mary Mellem, ncpe Instructors._

**Never a Better Time to Gift**

The lifetime estate and gift tax exemption for 2019 deaths is $11.4M, $22.3M for couples if portability is elected after the death of a spouse.

The exemption increases to $11.58M for 2020 deaths and $22.16M if portability is elected. Portability is only available if a Form 706 is filed for the first to die on married couples.

The exemption will not always remain at these high levels. It will become only $5M, adjusted for inflation, after 2025, unless Congress extends the higher amount. Tax-free gifts you make now will not unfairly trigger tax in 2025, as many wealthy individuals had projected.

Estates can use the higher lifetime exemption for gifts made prior to 2026 to calculate after 2025 estate taxes, the Internal Revenue Service has reported. Anyone who made or plans on making very large gifts from 2018 through 2025 will not lose out on the benefit of the larger exemption amount if it drops back down in 2026.

There are 12 states and the District of Columbia that levy their own estate tax on some decedents. They include:

- Connecticut
- Hawaii
- Illinois
- Maine
- Maryland
- Massachusetts
- Minneapolis
- New York
- Oregon
- Rhode Island
- Vermont
- Washington

The estate tax exemption amounts in these locations vary widely. No state has increased its exemption amount to match the current federal level.

There are 6 states with inheritance taxes. They include:

- Iowa
- Kentucky
- Maryland
- Nebraska
- New Jersey
- Pennsylvania

**News from Capitol Hill**

**Flurry of Last Minute Legislation**

The Secure Act is changing retirement — here are the most important things to know

The new law takes effect Jan. 1 and changes some rules about retirement savings

President Donald Trump signed the federal spending bill, ushering in new retirement legislation to enhance retirement security across the country.

_By Alessandra Malito_

President Trump signed the Secure Act as part of the government’s spending bill and it will inevitably affect most retirement savers, for better or worse.

The Secure legislation — which stands for “Setting Every Community Up for Retirement Enhancement” — puts into place numerous provisions intended to strengthen retirement security across the country.

Part of the bill addresses the grim outlook for many workers who don’t have access to workplace retirement accounts.

It offers small businesses tax incentives to set up automatic enrollment in retirement plans for its workers, or allows them to join multiple employer plans, where they can band together with other companies to offer retirement accounts to their employees in the first place. The bill also eliminates the maximum age cap for contributions to traditional individual retirement accounts.

Not all retirement experts are certain the bill will have much of an impact.
The Secure Act is a nice thing — anything we can do on a bipartisan basis in this day and age is something of value — but my sense is the changes in the act are really quite modest,” said Alicia Munnell, director of the Center for Retirement Research at Boston College, and a columnist for MarketWatch.

Some financial advisers worry a few of the changes can hurt savers — such as incorporating annuities in 401(k) plans and eliminating the rule that lets account beneficiaries stretch distributions across their lifetimes.

Here’s what the bill includes, and what that means for current savers and future retirees:

Annuities in 401(k) plans

The Secure Act opens the gates for more employers to offer annuities as investment options within 401(k) plans. Currently, employers hold the fiduciary responsibility to ensure these products are appropriate for employees’ portfolios, but under the new rules, the onus falls on insurance companies, which sell annuities, to offer proper investment choices.

The upside: Annuities provide a guaranteed income over the course of a retiree’s lifetime which is especially beneficial considering so many Americans are living longer, fuller lives in retirement. Proponents say annuities can offer a steady stream of money to retirees in the long-term, and also encourages savers to think about the far-off future. “They can be structured in a way to meet long-term retirement income objectives,” said Clint Cary, head of U.S. delegated investment solutions at Willis Towers Watson.

The downside: Annuities are complex investment products, and the wrong choice can be detrimental to a person’s portfolio. Employees should review their options and consult a financial adviser before moving forward with a plan. Annuitization could result in heftier fees and penalties if used incorrectly. Critics argued the bill was a major win for the insurance industry, which lobbied for the bill.

Increasing the required minimum distribution age — and contribution age

Previously, qualified account holders such as those with a 401(k) or IRA had to withdraw required minimum distributions (RMD) in the year they turned age 70.5. The Secure Act increases that age to 72, which may have tax implications, depending on where the account holders fall in their tax bracket in the year they withdraw. The 70.5 age was based on life expectancies in the early 1960s, the House said, and had not been updated since.

The bill also eliminates the maximum age for traditional IRA contributions, which was previously capped at 70.5 years old. “As Americans live longer, an increasing number continue employment beyond traditional retirement age,” the House Committee on Ways and Means said in a summary of the bill.

But be warned: Americans who turned 70.5 years old in 2019 will still need to withdraw their required minimum distributions this year, and failure to do so results in a 50% penalty of their RMD, said Jamie Hopkins, the director of retirement research at wealth management firm Carson Group. People who are expected to turn 70.5 years old in 2020 will not be required to withdraw RMDs until they are 72. The first withdrawal doesn’t need to be made until the following April 1, which means people who turned 70.5 in 2019 can wait to withdraw their RMD until April 1, 2020. They’ll then have to take another RMD by the following Dec. 31, and every Dec. 31 thereafter.

No more stretch IRAs

Required minimum distributions have also changed for non-spousal account inheritors. Under the current law, beneficiaries who did not inherit their accounts from a husband and wife are in some cases allowed to withdraw required minimum distributions for the span of their lives, which could be a few years, or a few decades. The amount of the distribution is calculated based on a few factors, including life expectancy and beneficiary age.

The Secure Act requires beneficiaries withdraw all assets of an inherited account within 10 years. There are no required minimum distributions within those 10 years, but the entire balance must be distributed after the 10th year. This change can be problematic for some beneficiaries, especially if they are in their 40s and 50s and at the peak of their earning years. Limiting the time frame in which someone can distribute money from an inherited account means potentially boosting the tax burden those distributions will cause.

The bill also widens access to multiple employer plans for small businesses. Previously, companies may have avoided participating in that type of program because of the so-called one bad apple rule that stated if one employer did not meet the plan requirements, the plan would fail for all others involved.

Under the Secure Act, employers no longer have to share “a common characteristic,” such as being in the same industry. “As employers pool together, they will enjoy the economy of scale, which is access to more features at affordable prices,” Cary said. “It does enable employers to help their employees in a big way.”

Employer-sponsored retirement plans would also be available to long-term part-time workers, with a lower minimum number of hours worked. Previously, employers did not have to invite workers who clock less than 1,000 hours every year to participate in a retirement plan, but the Secure Act drops the threshold for eligibility down to either one full year with 1,000 hours worked or three consecutive years of at least 500 hours.

Encouraging auto-enrollment

Another aspect of the Secure Act is the tax credit for employers that automatically enroll workers into their retirement plans. Auto-enrollment is a simple but effective measure to get people saving more for their futures, as studies show participants are more likely to stay in a plan than actively enroll in one themselves. Nobel Prize winner Richard Thaler, along with colleagues, may have helped Americans save nearly $29.6 billion in their retirement accounts with his work on auto-enrollment.

Under the Secure Act, small employers will get a tax credit to offset the costs of starting a 401(k) plan or Simple IRA plan with auto-enrollment, on top of the start-up credit they already receive.

Auto-enrollment is something the U.S. needs more of, Munnell said. The Secure Act provisions will only have a slightly positive impact on workers, but Americans need coverage and to be automatically enrolled in those plans. States have already stepped in, creating their own automatic-IRA programs, where companies without a retirement plan can — or in some cases, must — provide one for their employees. “That’s the only way to do it,” she said. “That is probably the biggest thing that could improve the retirement outlook for people.”
People in the Tax News

Congratulations to Lynn Jacobs, ncpeFellowship Member

Lynn Jacobs has been elected to the National Association of Enrolled Agents Board of Directors for 2020-2021. NAEA and its members are fortunate to find an individual of Lynn’s ability and dedication to serve. Congratulations to NAEA and to Lynn.

‘Jersey Shore’ Star Sorrentino Charged With Tax Evasion

Former reality TV celebrity Michael “The Situation” Sorrentino has been indicted for tax evasion, after federal prosecutors accused him and his brother of hiding millions of dollars he made while a cast member of the MTV series “Jersey Shore.”

In an indictment obtained and made public by the U.S. Department of Justice on Friday, Sorrentino and his brother Marc each faces nine criminal counts, some of which overlap, and including their alleged conspiracy to defraud the United States.

The new charges expand a case first brought against them in September 2014.

An arraignment is scheduled for April 17.

“Michael Sorrentino will enter a not guilty plea on April 17, 2017, and will vigorously contest the allegations,” his lawyer Kristen Santillo said in an email.

A lawyer for Marc Sorrentino did not immediately respond to requests for comment.

“Jersey Shore” ran from 2009 to 2012, featuring 20-something Italian-Americans partying, tanning and complaining about their jobs at a beachfront T-shirt stand.

Now 34, Michael Sorrentino popularized the phrase “gym, tan, laundry” to describe the pre-party routine of cast members.

The Sorrentino brothers were originally charged with trying to avoid taxes on $8.9 million of Michael Sorrentino’s income from 2010 to 2012. Prosecutors said they under-reported income, and claimed millions of dollars of expenses on clothes, expensive vehicles and other personal items as business expenses.

The new indictment accused Michael Sorrentino of evading taxes in 2011 by hiding income, not filing a personal return, and filing a false return for his company Situation Nation Inc.

It also accused him of having on several days in 2011 and 2012 made multiple cash deposits of less than $10,000 in different bank accounts to avoid federal reporting requirements.

Marc Sorrentino was accused of altering books and records of Situation Nation and MPS Entertainment LLC, in which the brothers owned stakes, after receiving grand jury subpoenas.

The brothers’ accountant, Gregg Mark, pleaded guilty in December 2015 to filing fraudulent tax returns on their behalf. His sentencing is scheduled for June 15.

Michael Sorrentino faces a maximum 10 years in prison on each of two counts over the bank deposits, and five years for the alleged tax evasion.

His brother faces up to 20 years in prison if convicted for obstructing a grand jury probe.


Reporting by Jonathan Stempel in New York

TurboTax Parent Investigated Over Treatment Of Low-income Taxpayers

Brittany De Lea
Fox Business

TurboTax parent Intuit is under fire once again, this time as multiple state attorneys general open an investigation into whether it deliberately steered low-income taxpayers away from free-file options they may have been eligible to use.

The investigation includes at least five state attorneys general, according to ProPublica, including from North Carolina. The exact number, however, is not clear.

A spokesperson for Intuit did not comment on the investigation specifically but said the company is cooperating with regulators.

“We are cooperating with regulatory inquiries and confident that we have been honest with consumers, over 13 million of whom filed their taxes with TurboTax last year for absolutely free,” the spokesperson said.

As noted by ProPublica, Intuit said in a filing earlier this year it believes the allegations in legal proceedings are “without merit,” adding that it would “vigorously defend” itself.

Individuals with incomes of $66,000 or less are eligible to file for free through the IRS’ Free File program – a partnership with third-party preparers. While 70 percent of Americans are eligible to use it, only 2.5 percent did so in fiscal 2018 (fewer than 3 million people of 104 eligible) – which some have attributed to the companies’ (Intuit and H&R Block) deliberate efforts to hide the products.

A group of senators asked the IRS to bring in an outside contractor (MITRE) to review the Free File program in May amid criticisms that industry partners were engaging in deceptive practices and not acting in the best interest of taxpayers.

The claims appear to be true. The report showed five of the 12 members of the program used a coding device to keep their Free File landing pages out of organic searches. However, engagement still increased at four of five of those partners.
Other explanations for low engagement were that half of the eligible taxpayers used a paid preparer, while others received refund-anticipation checks, filed paper returns or visited volunteer tax assistance sites.

Overall, about 30 million do-it-yourself filers were eligible to use the program, and about 9 percent of them did.

Intuit has been sued in a consumer class-action lawsuit over the allegations. It has also been sued by the city of Los Angeles and Santa Clara County.

A growing number of lawmakers, including New York Rep. Alexandria Ocasio-Cortez and Massachusetts Democrat Sen. Elizabeth Warren, have voiced support for a system where the IRS is able to play a larger role in the tax preparation process.

**HSBC Swiss To Pay $192M Over U.S. Tax Evasion Deal**

U.S. accused bank of helping rich Americans hide assets

The Swiss private banking unit of HSBC Holdings PLC will pay $192.4 million to resolve a U.S. probe of its role in helping wealthy Americans evade taxes by using undeclared Swiss bank accounts, the U.S. Department of Justice said.

The DoJ's deal with HSBC Private Bank (Suisse) SA is the latest in which numerous Swiss-based banks, including UBS and Credit Suisse Group, have paid billions of dollars in settlements and penalties for conspiring to help rich Americans dodge taxes.

The hard line taken by U.S. authorities over the last decade has helped pressure Switzerland to end banking secrecy that long allowed offshore clients to stash money in accounts in the republic. The Swiss government has deals with many countries to exchange information about accounts held by foreigners.

In this latest case, the DoJ filed a charge of conspiracy to defraud the United States against HSBC Private Bank (Suisse) but agreed to drop it in three years if the bank abides by the deal's terms, court documents show.

The charge relates to HSBC Private Bank (Suisse)'s conduct between 2000 and 2010, when the DoJ said the Geneva-based bank assisted U.S. clients in hiding offshore assets and income. Its bankers traveled to cities, including Miami, to scout for clients, the department said.

Even as the DoJ began investigating Swiss banks, including UBS, around 2008 for tax-dodging schemes, prosecutors said some HSBC Private Bank bankers continued the cross-border with U.S. residents.

"Some HSBC Switzerland bankers assisted clients in closing their accounts in a manner that continued to conceal their offshore assets," U.S. prosecutors said in a statement. UBS agreed to pay $780 million in fines, penalties, interest and restitution in 2009 for helping Americans hide their assets from U.S. tax authorities. In 2014, Credit Suisse paid $2.6 billion.

Many other Swiss banks have followed suit, including HSBC Private Bank, which said it cooperated with U.S. authorities, swapped out bankers and changed how it does business.

"Today the Swiss subsidiary operates under new management," Chief Executive Alex Classen said in a statement. "We have strengthened our compliance function, enhanced our control framework and put in place a comprehensive client tax transparency policy."

In 2017, HSBC paid 300 million euros ($330.6 million) to settle a separate investigation on tax evasion by French citizens via its Swiss private bank after an ex-employee leaked client data that spawned investigations in several countries.

**Owner of a Shreveport Medical Laboratory Service Admits Filing False Tax Returns**

Robert C. Poimboeuf, a Shreveport business owner, pleaded guilty today in federal court, to filing false tax returns, announced David C. Joseph, the United States Attorney for the Western District of Louisiana, and Principal Deputy Assistant Attorney General Richard E. Zuckerman of the Justice Department’s Tax Division.

According to documents and information provided to the court, Robert C. Poimboeuf, 57, along with his wife, owned and operated D&G Holdings, LLC, (D&G) a local medical business operating as Doctors Lab, that provided laboratory and phlebotomy services. From 2011 through 2015, Poimboeuf filed false tax returns that underreported gross receipts earned from D&G. In particular, Poimboeuf provided false and misleading information to his tax return preparers – hiding income, failing to disclose bank accounts and falsely characterizing business receipts as non-taxable loans.

D&G maintained an operating account and two accounts that received revenue – one for electronic payments and the other for physical deposits of checks. For 2011 through 2014, Poimboeuf concealed the nature of deposits into D&G’s operating bank account by falsely reporting to his accountant that the deposits were transfers from a billing service. Although D&G used a billing service, these deposits were not transfers from the billing service, but from D&G’s revenue accounts that Poimboeuf did not disclose to his accountant.

The Poimboeufs hired a different accountant to prepare their 2015 tax return and provided information for the electronic deposit account in addition to the operating account, but continued to withhold information about the physical deposits account. When the accountant asked for additional information concerning a loan, Poimboeuf provided a document to support the deposit for the loan, when in fact it was actually a transfer from the undiscovered physical deposits account. In addition, Poimboeuf did not provide numerous Forms 1099 reflecting earnings for D&G.

Poimboeuf underreported earnings for D&G in order to understatement taxes due for 2011 through 2015. As a result of Poimboeuf’s conduct, the filing of false federal income tax returns for the years 2011 through 2015 caused a tax loss of more than $1.9 million to the Internal Revenue Service (IRS).

"Mr. Poimboeuf cheated on his taxes in order to lower his tax bill. In doing so, he committed a crime and failed in a duty we all owe as American citizens," said U.S. Attorney Joseph. "He now awaits sentencing for this crime."

Sentencing is set for April 21, 2020, at 2:00 p.m., before Chief U.S. District Judge S. Maurice Hicks Jr. in Shreveport, Louisiana. Mr. Poimboeuf faces a statutory maximum sentence of six years in prison, as well as a period of supervised release and monetary penalties. Mr. Poimboeuf has agreed to pay restitution to the IRS in the amount of $1,904,477.

Special agents with the IRS-Criminal Investigation Division conducted the investigation. First Assistant U.S. Attorney Alexander C. Van...
IRS Selects Longtime Tax Professional, Sharyn Fisk, To Lead The Office Of Professional Responsibility

The Internal Revenue Service today announced the selection of Sharyn M. Fisk to lead the agency’s Office of Professional Responsibility (OPR).

Fisk has most recently been a professor of tax at the College of Business Administration at Cal Poly Pomona and active in the nation’s tax community in a variety of roles. She will assume leadership of OPR in early 2020.

“This is a critical position for the nation’s tax community. Sharyn Fisk is extremely well respected both internally at the IRS and throughout the tax professional communities. She has a strong set of skills and experience in many different settings that will serve the IRS well in this role,” said IRS Commissioner Chuck Rettig. “Taxpayers, the IRS and the tax community rely on this office to help uphold strong professional standards among tax professionals. We look forward to Ms. Fisk providing meaningful, fair and equitable guidance while also strengthening the oversight of tax professionals.”

OPR oversees all tax practitioners, tax preparers and other third parties in the tax system who practice before the IRS to ensure they adhere to professional standards and follow the law. The office works to increase education, awareness and understanding of Circular 230 and investigates and enforces cases related to Circular 230.

Circular 230 refers to Treasury Department Circular No. 230. The publication establishes the rules governing those who practice before the IRS including attorneys, Certified Public Accountants (CPAs) and Enrolled Agents (EAs).

Fisk’s extensive background in the tax community includes having represented thousands of individuals, businesses and corporate taxpayers before the IRS, the Department of Justice Tax Division, federal and state courts and state taxing authorities. These matters involved civil examinations and appeals, criminal investigations and tax collection issues. Fisk, a certified tax law specialist with the California State Bar, has also served as an adjunct professor teaching graduate and undergraduate level tax at several colleges and universities and recently concluded a term as a member of the IRS Advisory Council (IRSAC).

Fisk previously served as an attorney-advisor for the Honorable Maurice Foley, United States Tax Court in Washington, D.C., and has volunteered to assist unrepresented taxpayers for the pro se tax court calendar. In addition, she has served as director of Cal Poly Pomona’s VITA program and participated in the American Bar Association’s Adopt-A-Base program, where she provided training to military VITA volunteers at a naval base in San Diego.

Fisk is a past chair of the taxation section of the Los Angeles County Bar Association and previously chaired a task force on behalf of the Standards of Tax Practice Committee for the ABA Taxation Section. She has served as a former chair of the Tax Policy, Practice and Legislation Committee, articles editor of the California Tax Lawyer, and as a member of Executive Committee for the Taxation Section of the State Bar of California. Fisk has lectured before national, state and local tax professional organizations. She holds a B.A. in Journalism from San Diego State University, a J.D. from Rutgers University and an LL.M in taxation from the New York University School of Law. Fisk has three children and is married to Nelson Fisk, a retired Marine Lieutenant Colonel.

2020 Filing Season and IP PINS.

When the IRS begins the 2020 tax filing season, taxpayers in selected locations will be eligible to opt into the online Identity Protection PIN program.

Taxpayers will be eligible for this voluntary program if they filed a federal tax return last year from Arizona, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Illinois, Maryland, Michigan, Nevada, New Jersey, New Mexico, New York, North Carolina, Pennsylvania, Rhode Island, Texas and Washington.

The IP PIN is a 6-digit number that adds another layer of protection for taxpayers’ Social Security numbers and helps protect against tax-related identity theft.

The IRS has issued IP PINs to confirmed identity theft victims since 2011. In recent years, the IRS has been expanding the program to taxpayers who are not confirmed identity theft victims but who may want this additional protection.

Taxpayers opting into the IP PIN program must use the online Get an IP PIN tool at IRS.gov/IPPIN.

The IRS has created a new publication — Publication 5367, Identity Protection PIN Opt-In Program for Taxpayers — to help taxpayers understand the required steps. Please share with clients who are interested in this program. The publication is in English and Spanish. It can be printed and distributed, or the link may be shared.

Here are a few factors taxpayers should consider:  
- The identity verification process is, by design, rigorous. Not everyone will be able to authenticate their identities and obtain an IP PIN.
- Taxpayers cannot call the IRS to obtain an IP PIN. The IRS is working on alternatives to the online process, but one is not yet in place.
- A new IP PIN must be obtained each year from the online tool.
- Taxpayers should never share their IP PIN with anyone but their tax preparer to file their tax return. The IRS will not call or email to request an IP PIN. People should be on guard against identity thieves seeking their IP PINs.

Before making this program available nationwide, the IRS is expanding it in phases to ensure there is no adverse impact on existing systems. After the 2020 filing season, the IRS will decide whether to add additional states or expand nationwide.

Until then, the IRS is seeking assistance from tax professionals and others to help inform taxpayers in the 20 locations of their eligibility. Your help in spreading the word is greatly appreciated. Again, the Get an IP PIN tool will be available at the start of the 2020 filing season.
New Downloadable Assistant Helps Small Businesses Withhold The Right Amount Of Income Tax

The Internal Revenue Service has launched a new online assistant designed to help employers, especially small businesses, easily determine the right amount of federal income tax to withhold from their workers’ pay.

Known as the Income Tax Withholding Assistant for Employers, this new spreadsheet-based tool is designed to help employers easily transition to the redesigned withholding system (no longer based on withholding allowances), which goes into effect on Jan. 1. It does this by helping them easily implement new income-tax withholding requests from employees who fill out the completely redesigned 2020 Form W-4, Employee’s Withholding Certificate.

At the same time, the tool can also help employers continue to properly withhold from employees who still have a withholding request on file using a past version of the W-4, which was based on withholding allowances.

“We’ve been working closely with the payroll community and other partners to make improvements in the withholding process,” said IRS Commissioner Chuck Rettig. “As part of this effort and based on feedback from partners, the IRS has created a new spreadsheet-based tool that’s designed to help small businesses navigate a variety of situations involving their employees to help ensure the right amount of withholding.”

Now available for download, without charge, on IRS.gov, the Income Tax Withholding Assistant for Employers is designed to help any employer who would otherwise figure withholding, manually, using a worksheet and either the percentage method or wage bracket tables found in Publication 15-T, Federal Income Tax Withholding Methods.

Employers who already use an automated payroll system won’t need this new assistant because their system already does the math.

The Income Tax Withholding Assistant for Employers is available in Microsoft Excel. The employer can use the tool to create a profile for each employee that then automatically calculates their correct federal income tax withholding.

To use the Income Tax Withholding Assistant for Employers, the employer starts by indicating their pay period frequency (for example, weekly, bi-weekly, monthly, etc.), and then enters key information from an employee’s Form W-4. For the tool to work properly, the employer must indicate whether the employee submitted a 2020 Form W-4, which does not base withholding on the number of withholding allowances claimed, or a prior version of the W-4, which does.

The employer can then save a separate customized copy of the file for each employee containing that employee’s Form W-4 information. Then, each pay period, the employer simply opens the employee’s file and enters their gross wage or salary amount for that pay period. The tool will then automatically display the correct amount of federal income tax to withhold from that employee’s pay.

Interim Guidance Provided On Withholding From Retirement And Annuity Distributions

Notice 2020-3, 2020-3 IRB

In a Notice, the IRS has provided guidance for the 2020 calendar year regarding withholding from periodic payments for pensions, annuities, and certain other deferred income under Code Sec. 3405(a), including the rules for withholding from periodic payments under Code Sec. 3405(a) when no withholding certificate has been furnished (default rate of withholding). The IRS is considering whether the 2020 default rate of withholding under Code Sec. 3405(a) will continue to be appropriate for calendar years after 2020.

Prior to the 2020 calendar year, information requested on Form W-4P regarding withholding from periodic payments generally paralleled the information requested on Form W-4, Employee’s Withholding Allowance Certificate, for withholding from wages. The Form W-4 for the 2020 calendar year (which has been renamed the Form W-4), Employee’s Withholding Certificate has been redesigned to increase transparency and accuracy of the withholding system. Beginning in calendar year 2020, employers are required to use the redesigned form for all new employees and for employees hired before 2020 who wish to adjust their withholding. (Instructions for Form W-4) As a result, information requested on the 2020 Form W-4 no longer parallels information requested on Form W-4P for withholding from periodic payments. Among other changes, the redesigned Form W-4 requests the employee’s filing status, rather than marital status, and no longer requests the number of withholding allowances the employee is claiming. The 2020 Form W-4 also includes a new method by which an employee may request withholding using higher withholding rate tables. (Notice 2020-3, Sec. II)

The IRS has designed the withholding tables and computational procedures in the 2020 Publication 15-T, Federal Income Tax Withholding Methods, to work with both a 2019 or earlier Form W-4 and the redesigned 2020 Form W-4. Therefore, for purposes of withholding from periodic payments under Code Sec. 3405(a), the IRS plans to provide in the 2020 Publication 15-A, Employer’s Supplemental Tax Guide, that the 2020 Form W-4P will work with certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4. (Notice 2020-3, Sec. II)

Code Sec. 3405(a)(4) was amended by section 11041(c)(2)(G) of the Tax Cuts and Jobs Act (TCJA, PL 115-97) to provide that the withholding rate for periodic payments when no withholding certificate has been furnished "shall be determined under rules prescribed by the Secretary." Under the law in effect before 2018, Code Sec. 3405(a)(4) provided that, in the case of a payee entitled to periodic payments with respect to which a withholding certificate had not been furnished, the amount to be withheld from each such payment “shall be determined by treating the payee as a married individual claiming 3 withholding exemptions.” Temporary regs issued under Code Sec. 3405 (as in effect before 2018) continue to provide that, if no withholding certificate has been furnished with respect to periodic payments under Code Sec. 3405(a), then the payor must base withholding on the rates for a married person claiming three withholding allowances. (Reg. § 35.3405-1T, Q&As A-10, B-3, and B-4)

Following enactment of TCJA, the IRS issued guidance to address changes made by the TCJA to withholding rules under Code Sec. 3401, Code Sec. 3402, and Code Sec. 3405. (Notice 2018-14, 2018-7 IRB 353 and Notice 2018-92, 2018-51 IRB 1038) With respect to Code Sec. 3405(a), Notice 2018-14, Sec. V, provided that, for 2018, the default rate of withholding would parallel the rules for prior years and would be based on treating the payee as a married individual claiming three withholding allowances. Similarly, Notice 2018-92, Sec. 10, provided that, for 2019, the default rate of withholding under Code Sec. 3405(a)(4) would parallel the rules for prior years,
For the 2020 calendar year, the rules for withholding from periodic payments under Code Sec. 3405(a) when no withholding certificate has been furnished will continue to parallel the rules for prior years. Therefore, for 2020, the default rate of withholding from periodic payments under Code Sec. 3405(a) will be based on treating the payee as a married individual claiming three withholding allowances and applying that to the applicable withholding tables and related computational procedures in the 2020 Publication 15-T. The IRS plans to provide in the 2020 Publication 15-A that this default rate of withholding will work with certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4. (Notice 2020-3, Sec. IV)

The IRS will provide the rules and procedures that apply for calendar years after 2020 for withholding from periodic payments under Code Sec. 3405(a) in applicable forms, instructions, publications, and other guidance. In addition, the IRS is considering whether the default rate of withholding from periodic payments under Code Sec. 3405(a) described above will continue to be appropriate for calendar years after 2020. (Notice 2020-3, Sec. V)

**IRS and Treasury Finalize Opportunity Zone Guidance**

The Internal Revenue Service today issued final regulations providing details about investment in qualified opportunity zones (QOZ).

The final regulations modified and finalized the proposed regulations that were issued on October 28, 2018 and May 1, 2019.

The final regulations provide additional guidance for taxpayers eligible to make an election to temporarily defer the inclusion in gross income of certain eligible gain. The final regulations also address, the ability of such taxpayers’ eligibility to increase the basis in their qualifying investment equal to the fair market value of the investment on the date that it is sold, after holding the equity interest for at least 10 years.

The statute permits the deferral of all or part of a gain that would otherwise be included in income, if corresponding amounts are invested into a qualified opportunity fund (QOF). The gain is deferred until an inclusion event or Dec. 31, 2026, whichever is earlier. The final regulations provide a list of inclusion events. Further, the final regulations provide guidance to determine the amount of income that must be included at the time of the inclusion event or December 31, 2026.

The final regulations also address the various requirements that must be met to qualify as a QOF, as well as the requirements an entity must meet to qualify as a QOZ business. In order to provide clarity, the final regulations have modified the proposed regulations for QOFs and QOZ businesses. Specifically, the final regulations provide additional guidance on how an entity becomes a QOF or QOZ business, and the requirement that a QOF or QOZ business engage in a trade or business. The final regulations retain the general approach of the proposed regulations but provide additional guidance and clarity to the rules regarding QOZ business property.

Related forms, instructions and other information taxpayers need to take advantage of this update will be made available in January 2020.

**LB&I Announces New Self-employment Tax Compliance Campaign**

The IRS’s Large Business and International (LB&I) division has announced a new compliance campaign targeting self-employed individuals in the U.S. territories who fail to pay or who underpay their self-employment taxes.

The self-employment tax is equal to the social security and Medicare taxes on net earnings from self-employment. (Code Sec. 1401) The self-employment tax rate is 15.3%—12.4% for social security and 2.9% for Medicare. An individual must pay self-employment tax if his or her net earnings from self-employment are at least $400. (Code Sec. 1402(b)(2))

U.S. citizens and resident aliens who reside in any of the U.S. territories (Puerto Rico, Guam, American Samoa, the U.S. Virgin Islands (USVI) or the Commonwealth of the Northern Mariana Islands (CNMI)) must pay self-employment tax on net earnings from self-employment of $400 or more. These individuals must pay self-employment tax whether or not they must pay U.S. income tax or are otherwise required to file a U.S. income tax return. (Code Sec. 1402(a)(9))

Residents of the U.S. territories with net self-employment income of $400 or more file Form 1040SS, U.S. Self-Employment Tax Return (including the Additional Child Tax Credit for Bona Fide Residents of Puerto Rico) or Form 1040PR, Self-Employment Tax Return–Puerto Rico, to report net earnings from self-employment to the IRS and, if necessary, pay self-employment tax on that income.

The new LB&I campaign addresses residents of U.S. territories (Puerto Rico, USVI, Guam, American Samoa and the CNMI) who either failed to pay, or who underpaid, self-employment tax to the IRS.

Territorial residents who understate their self-employment tax should file an amended Form 1040SS or Form 1040PR (as applicable) to properly report and pay their self-employment tax.

The IRS will address continued noncompliance through a variety of treatment streams, including examination.

**IRS Updates Employee Meal And Incidental Expense Rules To Reflect TCJA**


In a Revenue Procedure and accompanying News Release, IRS has updated a portion of its annual Revenue Procedure on travel per diem rates to reflect the fact that the Tax Cuts and Jobs Act (P.L. 115-97, TCJA) doesn’t allow most employees to deduct meal and incidental travel expenses (M&IE).

**Background—before TCJA.** Code Sec. 162(a) of the Code allows a deduction for ordinary and necessary expenses paid or incurred...
To deduct expenses for travel away from home, a taxpayer must substantiate the expenses under Code Sec. 274(d), which also authorizes IRS to prescribe that some or all of the substantiation requirements do not apply to an expense that does not exceed a particular amount.

Reg. §1.274-5(g) authorizes IRS to prescribe rules under which reimbursement arrangements or per diem allowances are regarded (1) as equivalent to substantiation, by adequate records or other sufficient evidence, of the amount of travel expenses for purposes of Reg. §1.274-5(c), and (2) as satisfying the requirements of an adequate accounting to the employer of the amount of travel expenses for purposes of Reg. §1.274-5(f).

For purposes of determining adjusted gross income, Code Sec. 62(a)(2)(A) allows an employee to deduct business expenses the employee pays or incurs in performing services under a reimbursement or other expense allowance arrangement with a payor. In addition, Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E) allow qualified performing artists, fee-basis state or local government officials, eligible educators, and Armed Forces reservists to deduct specified business expenses paid or incurred in performing services. The expenses paid or incurred by employees that are deductible under Code Sec. 62(a)(2) in computing adjusted gross income are above-the-line deductions determined without regard to Code Sec. 67.

Before the effective date of TCJA, Code Sec. 67(a) provided generally that, in the case of an individual, the miscellaneous itemized deductions for any tax year are allowed only to the extent that the aggregate of such deductions exceeds 2% of adjusted gross income. Except as otherwise provided in Code Sec. 62(a)(2)(A), employee business expenses are miscellaneous itemized deductions. (Code Sec. 67(b))

Code Sec. 62(c) provides that an arrangement is not treated as a reimbursement or other expense allowance arrangement for purposes of Code Sec. 62(a)(2)(A) if it (1) does not require the employee to substantiate the expenses covered by the arrangement to the payor, or (2) allows the employee to retain any amount in excess of the substantiated expenses covered under the arrangement. Code Sec. 62(c) further provides, however, that substantiation is not required for the expense to the extent provided in regs under Code Sec. 274(d).

Rev Proc 2011-47, 2011-42 IRB 520 provides: a) guidance that allows an amount of ordinary and necessary business expenses of employee for reimbursed traveling expenses to be deemed substantiated under Reg. § 1.274-5 when the payor provides a per diem allowance; and b) an optional method for employees and self-employed who aren't reimbursed to use in computing deductible costs paid or incurred for M&IE while traveling away from home.

IRS updates Rev Proc 2011-47 annually to reflect current per diem rates.

Background—TCJA changes. Section 11045 of the TCJA amended Code Sec. 67 to temporarily suspend all miscellaneous itemized deductions that are subject to the 2% of adjusted gross income floor. For any tax year beginning after December 31, 2017, and before January 1, 2026 (suspension period), a taxpayer is not permitted to claim miscellaneous itemized deductions, including unreimbursed employee travel expenses.

Section 13304 of the TCJA amended Code Sec. 274 to generally disallow a deduction for expenses with respect to entertainment, amusement, or recreation incurred or paid after December 31, 2017. Otherwise allowable meal expenses remain deductible, subject to the 50% limitation in Code Sec. 274(n)(1).

Changes to rules, to reflect TCJA. IRS has amended three of the rules in Rev Proc 2011-47, to reflect the above TCJA changes:

...Section 7.05 (formerly Section 7.06) provides that an employee described in Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E) who pays or incurs meal expenses and does not receive a per diem allowance for food and incidental expenses may deduct an amount computed using the federal M&IE rate for the locality, in computing adjusted gross income. During the suspension period, a taxpayer may not deduct unreimbursed employee travel expenses as itemized deductions under Code Sec. 67 in computing taxable income. Before it was amended, this provision applied to all employees, as opposed to only those described in Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E), and it noted that the deduction was subject to the 2% floor in Code Sec. 67.

...Section 7.06 (formerly Section 7.07) provides that an employee described in Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E) who incurs incidental expenses, does not pay or incur meal expenses and does not receive a per diem allowance for incidental expenses, may deduct an amount that IRS publishes in an annual notice, in computing adjusted gross income. During the suspension period, a taxpayer may not deduct unreimbursed employee travel expenses as itemized deductions under Code Sec. 67 in computing taxable income. Before it was amended, this provision applied to all employees, as opposed to only those described in Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E), and it noted that the deduction was subject to the 2% floor in Code Sec. 67.

...Section 7.07 (formerly Section 7.05) provides that if the amount of the expenses that is deemed substantiated under the rules in Rev Proc 2011-47 and Rev Proc 2019-48 is less than the amount of an employee's business expenses for travel away from home, an employee described in Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E) may deduct, in computing adjusted gross income, the amount by which the business travel expenses exceed the amount that is deemed substantiated, provided the employee substantiates all the business travel expenses (not just the excess over the federal per diem rate), includes on Form 2106, "Employee Business Expenses," the deemed substantiated portion of the per diem allowance received from the payor, and includes in gross income the portion (if any) of the per diem allowance received from the payor that exceeds the amount deemed substantiated. Before it was amended, this provision applied to all employees, as opposed to only those described in Code Sec. 62(a)(2)(B)—Code Sec. 62(a)(2)(E), and provided that the deduction allowed was an itemized deduction, as opposed to a deduction in computing adjusted gross income.

The revenue procedure is effective for per diem allowances for lodging, meal and incidental expenses, or for meal and incidental expenses only that are paid to an employee on or after November 26, 2019, for travel away from home on or after November 26, 2019. For purposes of computing the amount allowable as a deduction for travel away from home, the revenue procedure is effective for meal and incidental expenses or for incidental expenses only paid or incurred on or after November 26, 2019.
Final Regulations Issued On Calculating Unrelated Business Taxable Income

TD 9886; Reg. § 1.512(a)-5

The IRS has issued final regs how voluntary employees' beneficiary associations (VEBAs) and supplemental unemployment benefit trusts (SUBs) must calculate unrelated business taxable income (UBTI).

Organizations that are otherwise exempt from tax under Code Sec. 501(a) are subject to tax on their UBTI under Code Sec. 511(a).

Code Sec. 512(a) generally defines UBTI of exempt organizations and provides special rules for calculating UBTI for organizations described in Code Sec. 501(c)(7) (social and recreational clubs), VEBAs described in Code Sec. 501(c)(9), and SUBs described in Code Sec. 501(c)(17).

Code Sec. 512(a)(1) provides a general rule that UBTI is the gross income from any unrelated trade or business regularly carried on by the organization, less certain deductions. Under Code Sec. 512(a)(3)(A), in the case of VEBAs and SUBs, UBTI is defined as gross income, less directly connected expenses, but excluding “exempt function income.”

Exempt function income is defined in Code Sec. 512(a)(3)(B) as gross income from two sources. The first type of exempt function income is amounts paid by members as consideration for providing the members or their dependents or guests with goods, facilities, or services in furtherance of the organization’s exempt purposes. The second type of exempt function income is all income (other than an amount equal to the gross income derived from any unrelated trade or business regularly carried on by the organization computed as if the organization were subject to Code Sec. 512(a)(1)) that is set aside: (1) for certain charitable purposes; (2) in the case of a VEOA or SUB, to provide for the payment of life, sick, accident, or other benefits; or (3) for reasonable costs of administration directly connected with a purpose described in (1) or (2).

Code Sec. 512(a)(3)(E) generally limits the amount that a VEOA or SUB may set aside as exempt function income to an amount that does not result in an amount of total assets in the VEOA or SUB at the end of the tax year that exceeds the account limit (defined under Code Sec. 419A) for the tax year. The account limit does not take into account any reserve for post-retirement medical benefits. (Code Sec. 512(a)(3)(E)(i)).

To implement Code Sec. 512(a)(3)(E), Reg. §1.512(a)-5T was published in the Federal Register on February 4, 1986, with an immediate effective date. (TD 8073) A cross-referencing Notice of Proposed Rulemaking (the 1986 proposed regulation) was issued contemporaneously with the temporary reg. The 1986 proposed regulation was withdrawn and replaced by a new proposed regulation (the 2014 proposed regulation) that was published in the Federal Register on February 6, 2014. (Preamble to Prop Reg REG-143874-10)

The final reg adopts the provisions of the 2014 proposed reg with no modifications other than the following changes:

(1) the addition of a clause modifying the definition of covered entity to include certain corporations described in Code Sec. 501(c)(2), as provided in Code Sec. 512(a)(3)(C);

(2) the addition of a clause which refers to the provision in Code Sec. 512(a)(3)(D) addressing nonrecognition of gain in the case of sales of certain property;

(3) the addition of language clarifying the limitation on amounts set aside for exempt purposes under Code Sec. 512(a)(3)(E); and

(4) a change in the applicability date to tax years beginning on or after December 10, 2019 (the date of publication of the final regulation). The final reg also removes the temporary reg. (Preamble to TD 9886)

Consistent with the 2014 proposed regulation, the final reg uses the uniform term “Covered Entity” to describe VEBAs and SUBs subject to the UBTI computation rules of Code Sec. 512(a)(3). (Reg. § 1.512(a)-5(a)(2)(ii))

The 2014 proposed regulation did not reflect the provision of Code Sec. 512(a)(3)(C), which provides that Code Sec. 512(a)(3)(A) applies to a corporation described in Code Sec. 501(c)(2), the income of which is payable to an organization described in Code Sec. 501(c)(7), Code Sec. 501(c)(9), or Code Sec. 501(c)(17), as if the corporation were the organization to which the income is payable. (Preamble to TD 9886) A clause has been added in the final reg to clarify that the term “Covered Entity” includes a corporation described in Code Sec. 501(c)(2) to the extent provided in Code Sec. 512(a)(3)(C). (Reg. § 1.512(a)-5(a)(2)(ii))

For tax years beginning after June 30, 1992, group legal services organizations (GLSOs) are no longer exempt as Code Sec. 501(c)(20) organizations. Therefore, a GLSO is no longer a Covered Entity. (Preamble to TD 9886)

The 2014 proposed regulation did not reflect the provision of Code Sec. 512(a)(3)(D) regarding nonrecognition of gain with respect to the sale of certain property. (Preamble to TD 9886) Code Sec. 512(a)(3)(D) provides that, if property used directly in the performance of the exempt function of a Covered Entity is sold by the Covered Entity, and other property is purchased and used by the Covered Entity directly in the performance of its exempt function within a four-year period beginning one year before the date of the sale, and ending three years after the date of sale, gain (if any) from the sale is recognized only to the extent that the sales price of the old property exceeds the Covered Entity’s cost of purchasing the other property. A clause has been added to the final reg to refer to that provision. (Reg. § 1.512(a)-5(c)(2)(ii)(B))

Code Sec. 512(a)(3)(E)(i) limits the amount of investment income a Covered Entity may treat as nontaxable exempt function income in any given year to the extent such income "result[s] in" a year-end account balance "in excess of" the modified Code Sec. 419A account limit. An account overage can be considered the result of, or essentially caused by, investment income only by considering all investment income earned during the year. Thus, in order to give an appropriate meaning to the term "result in," the total amount of investment income earned during the year should be considered when calculating whether an excess exists at the end of the year.

Certain taxpayers have taken a contrary position and asserted that investment income may be set aside and used separately before the end of a tax year for current benefit payments and related administrative costs (collectively, "benefit expenditures") and thereby avoid the limit imposed by Code Sec. 512(a)(3)(E)(i) on exempt function income. The Court of Appeals for the Sixth Circuit held that investment income that the VEOA earmarked and claimed was spent before year-end on reasonable costs of administration was

In contrast, the Court of Appeals for the Federal Circuit rejected this argument. The court stated that the “language of Code Sec. 512(a)(3)(E) is clear and unambiguous,” and upheld the Court of Federal Claims’ conclusion that a Veba “may not avoid the limitation on exempt function income in Code Sec. 512(a)(3)(E)(i) merely by allocating investment income toward the payment of welfare benefits during the course of the tax year.” (CNG Transmission Management Veba, (CA Fed Cir 2009) 104 AFTR 2d 2009-7699, 588 F3d 1376)

The IRS has concluded that the decision in Sherwin-Williams is contrary to the statute, the legislative history of Code Sec. 512(a)(3)(E), Reg. §1.512(a)-5T, and the 1986 and 2014 proposed regulations. The IRS’s interpretation is set forth in its non-acquiescence to the Sherwin-Williams decision (AOD 2005-02, 2005-35 I.R.B. 422). In AOD 2005-02, the IRS recognized the precedential effect of the decision to cases appealable to the Sixth Circuit and indicated that it would follow the decision in Sherwin-Williams with respect to cases within that circuit if the opinion could not be meaningfully distinguished. (Preamble to TD 9886)

The IRS has determined that the statutory provisions are not dependent upon a determination as to whether particular sources of income were used for benefit expenditures in any particular year. Rather, the "result in" language of Code Sec. 512(a)(3)(E)(i) means that amounts set aside for benefit expenditures are treated as exempt function income only to the extent the total amount set aside for such purposes as of the end of the year is equal to or less than the account limit determined under Code Sec. 419A for a tax year (not taking into account any reserve described in Code Sec. 419A(c)(2)(A) for post-retirement medical benefits). (Preamble to TD 9886) Accordingly, the final regulations reflect this rule, and, for tax years to which the final reg applies, the IRS will apply the final reg to cases arising in the Sixth Circuit. (Preamble to TD 9886)

The final reg specifically states that any investment income a Covered Entity earns during the tax year is subject to UBIT to the extent the total amount set aside for benefit expenditures are treated as exempt function income only to the extent the total amount set aside for such purposes as of the end of the year is equal to or less than the account limit determined under Code Sec. 419A for a tax year (not taking into account any reserve described in Code Sec. 419A(c)(2)(A) for post-retirement medical benefits). (Preamble to TD 9886)

Applicability date. The final reg applies to tax years beginning on or after December 10, 2019. (Reg. § 1.512(a)-5(e)(2)). For VEBAs within the Sixth Circuit’s jurisdiction, the position reflected in AOD 2005-02 would apply through the end of the Veba’s tax year in which the final reg is issued. (Preamble to TD 9886).

**IRS Delays Tax Basis Reporting Of Capital Accounts To 2020**


In a Notice, the IRS has delayed partnerships’ reporting of tax basis capital accounts until 2020. Partnerships will not be required to report partners’ shares of partnership capital on the tax basis method for tax years beginning in calendar year 2019 but will be required to use that method beginning in 2020 for partnership tax years beginning on or after January 1, 2020.

**Background**—reporting partner tax basis capital accounts. Drafts of the 2019 Schedule K-1 (Form 1065), 2019 Schedule K-1 (Form 8865) and the related draft instructions for the 2019 Form 1065, U.S. Return of Partnership Income (to which the draft instructions for the 2019 Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships, refer), proposed to require partner tax basis capital reporting by all partnerships and certain other persons and to prohibit the reporting of partner capital under Code Sec. 704(b), generally accepted accounting principles (GAAP), or any other method for 2019.

**Background**—reporting partners’ shares of net unrecognized section 704(c) gain or loss. The drafts of the 2019 Schedule K-1 (Form 1065), 2019 Schedule K-1 (Form 8865), and the related draft instructions for the 2019 Form 1065, U.S. Return of Partnership Income (to which the draft instructions for the 2019 Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships, refer), also proposed to require partnerships to report partners’ shares of net unrecognized Section 704(c) gain or loss as of the beginning and end of the partnership’s 2019 tax year. The draft instructions to these forms did not include a definition of “net unrecognized Section 704(c) gain or loss.”

For more information about the draft 2019 Form 1065, Schedule K-1 and the accompanying draft instructions, see IRS issues second draft of 2019 Form 1065, Sch K-1 (10/23/2019) and Draft instructions for 2019 Form 1065 and Schedule K-1 released (11/01/2019).

Delayed tax basis capital account reporting. The IRS has delayed partnerships’ reporting of tax basis capital accounts until 2020. Therefore, partnerships and other persons required to furnish and file Schedule K-1 (Form 1065) or Schedule K-1 (Form 8865), will not be required to report partner capital accounts using the tax basis method on the 2019 Schedule K-1 (Form 1065) or 2019 Schedule K-1 (Form 8865). Instead, for 2019 partnerships and other persons should report partner capital accounts consistent with the reporting requirements in the 2018 forms and instructions, including the requirement to report negative tax basis capital accounts on a partner-by-partner basis. (Notice 2019-66, 2019-52 IRB)

The IRS expects the final instructions for the 2019 Schedule K-1 (Form 1065) and Schedule K-1 (Form 8865) to include additional details on how such reporting should be done. In addition, in preparation for filing partnership tax returns for the 2020 tax year, the IRS will provide additional guidance on the definition of partner tax basis capital.

Notice 2019-66 also clarifies the 2019 requirement for partnerships to report a partner’s share of “net unrecognized Section 704(c) gain or loss” by defining this term for purposes of the reporting requirement.

Solely for purposes of completing the 2019 Forms 1065, Schedule K-1, and Form 8865, Schedule K-1, a partner’s share of “net unrecognized Section 704(c) gain or loss” is defined as the partner’s share of the net of all unrecognized gains or losses under Code Sec. 704(c) in partnership property, including Code Sec. 704(c) gains and losses arising from revaluations of partnership property.

Finally, the IRS has exempted publicly traded partnerships from the requirement to report their partners’ shares of “net unrecognized Section 704(c) gain or loss” for 2019, and thereafter, until further notice.

Taxpayers who follow the instructions in Notice 2019-66 will not be subject to any penalty for reporting in accordance with this guidance, including a penalty under Code Sec. 6722 for failure to furnish correct payee statements, Code Sec. 6698 for failure to file a partnership return that shows required information, and Code Sec. 6038 for failure
Taxpayer Advocate Service Updates Passport Certification Program Guidance

In a memorandum to Tax Advocate Service (TAS) employees, TAS has updated its advocacy guidance now that the IRS has stopped its temporary program under which it wasn't certifying taxpayers for passport revocation etc., if the taxpayer had delinquent tax debt but also had an open Taxpayer Advocate Service (TAS) case.

Background. Code Sec. 7345 authorizes (but does not require) the IRS to certify a taxpayer's seriously delinquent tax debt to the State Department for the purposes of passport denial, limitation, or revocation. A seriously delinquent tax debt is an assessed individual tax liability exceeding $50,000 (adjusted for inflation) for which either a notice of federal tax lien has been filed or a levy has been made. IRS must also send a decertification to the Department of State where the certification was in error or where there is no longer a seriously delinquent tax debt. (Code Sec. 7345(b))

The Internal Revenue Manual provides details as to how the IRS certifies and decertifies a taxpayer. (IRM 13.1.24) A decertification protects the taxpayer's passport from being denied, limited, or revoked merely because of a seriously delinquent tax debt.

The IRM also details how the TAS can open a case to help a taxpayer resolve a tax issue. (IRM 13.1.7.2(1) (2/4/2015))

The National Taxpayer Advocate (NTA) has long advocated excluding certain taxpayers with TAS cases from passport certification. In July 25, 2019, IRS announced that all open TAS cases with a certified taxpayer would be systemically decertified. New TAS taxpayers would also be systemically decertified. The IRS said that this decision was temporary and that new guidance would be issued once the IRS Commissioner makes a final decision on this issue.

But in October 2019, the IRS found that excluding cases from certification solely on the basis that the taxpayer is seeking assistance from TAS could allow a "won't pay" taxpayer to circumvent the intent of the legislation to obtain or renew a passport. Following the review of relevant considerations regarding these procedures, the IRS determined that a blanket, systemic exception for anyone with an open TAS case is overly broad and could undermine the effectiveness of Code Sec. 7345 to collect a seriously delinquent tax debt.

TAS guidance. Now that taxpayers working with TAS will no longer be automatically protected from certification, TAS will work with the IRS to identify and resolve the seriously delinquent tax debts of these taxpayers. Disagreements about how to address individual cases or whether to protect a specific taxpayer from certification who has already taken significant steps to resolve the debt will still be resolved with Taxpayer Assistance Orders (TAOs).

The memo tells TAS employees to elevate a case to the employee's Local Taxpayer Advocate (LTA) if the case meets all the following criteria. The taxpayer has:

- Imminent foreign travel plans, lives abroad, or has another compelling need for the passport;
- A significant risk of being certified before TAS will be able to help resolve the taxpayer's debt; and
- Taken demonstrable recent steps to get into compliance with the IRS that nevertheless fall short of the statutory and discretionary exclusions.

IRS Tax Tip Discusses Tax Treatment Of Forced Livestock Sales Due To Drought

In a Tax Tip, the IRS has provided information on the tax treatment of forced livestock sales due to drought. The Tax Tip notes that eligible taxpayers forced to sell livestock due to drought may have more than four years to replace the livestock and additional time to defer tax on any gains from the forced sales.

Generally, if a taxpayer if forced to sell livestock because of a drought (drought sale) that results in the taxpayer's area being designated for assistance by the federal government, the taxpayer has four years to replace that livestock in order to qualify for treatment under the involuntary conversion rules in Code Sec. 1033. The IRS may extend this 4-year period further, on a regional basis, if the drought continues for more than 3 years. (Code Sec. 1033(e)(2))

The 4-year replacement period is extended to the end of the taxpayer’s first tax year ending after the first drought-free year for the taxpayer’s region (extended-replacement period). The first drought free year is the first 12-month period that: (1) ends on August 31; (2) ends in or after the last year of the taxpayer's 4-year replacement period; and (3) does not include any weekly period for which exceptional, extreme, or severe drought is reported for any location in the taxpayer’s region. (Notice 2006-82, 2006-2 CB 529)

Taxpayers can determine whether drought conditions exist for their region by referring to either the U.S. Drought Monitor maps produced by the National Drought Mitigation Center (NDMC) or Notice 2019-54, 2019-42 IRB 935. See Annual list sets out extreme drought areas for extended livestock replacement period (10/01/2019).

Eligible taxpayers have until the end of the tax year after the first drought-free year to replace the sold livestock. To be eligible:

- the taxpayer must have held the sold livestock for draft, dairy or breeding purposes. Forced sales of other livestock, such as those raised for slaughter or held for sporting purposes, and of poultry are not eligible for the extended-replacement period.
- the taxpayer must be in an applicable region. An applicable region is a county, parish or district (county) designated as eligible for federal assistance because of drought conditions as well as counties contiguous to that county.
- the forced sales of livestock must be due solely to a drought that caused the region to be designated as eligible for federal assistance. For example, if the taxpayer normally sells 25% of its cattle held for breeding purposes annually, but sells all its cattle in one year because of a drought, the sale of 75% of the cattle is eligible for the extended-replacement period. (Notice 2006-82, example)

During the extended-replacement period, eligible taxpayers may also delay recognizing gains on forced sales of livestock. In the above example, the taxpayer may delay recognizing gain on the 75% of the cattle sold because of the drought to the extent that the gain exceeds the cost of the replacement property (property that is related in service or use) purchased during the extended-replacement period. (Notice 2006-82, example)
Because the normal drought-sale replacement period is four years, the extended-replacement period announced in Notice 2019-54 affects drought sales that occurred during 2015. However, because of previous drought-related extensions affecting some areas, the replacement periods for some drought sales before 2015 have also been extended. (See Notice 2015-69, 2015-41 IRB 550; Notice 2016-60, 2016-42 IRB 458; Notice 2017-53, 2017-42 IRB 318; and Notice 2018-79, 2018-42 IRB 606) The extended-replacement period also applies to taxpayers who were forced to sell livestock because of drought between Sept. 1, 2018 and Aug. 31, 2019.

To take advantage of this beneficial tax treatment for forced livestock sales, taxpayers should keep careful records of all their livestock sales and especially note when livestock is sold because of drought.

**IRS Changes Submission Process For FBAR Filing Verification**

The IRS has changed the process under which it accepts requests for verification that it has received a filed FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR).

**Background.** Before November 19, 2019, the IRS allowed FBAR filers to call its FBAR hotline to obtain verbal verification of filing for up to five FBARs, at no charge. (IRM 4.26.16.4.13(4)(a)

However, FBAR filers were required to make written requests (1) for verification of filing of more than five FBARs, (2) for paper copies of filed FBARs, and (3) for any verification or copy requested by an authorized representative. (IRM 4.26.16.4.13(4))

For written requests for FBAR filing verification, there is a $5.00 fee for verifying the filing status of five or fewer FBARs and a $1.00 fee for each additional FBAR filing verification requested. If the requester needs copies of the filed FBARs, there is an additional fee of $0.15 per copy of the entire FBAR. (IRM 4.26.16.4.13(4)(b))

New process. Effective November 19, 2019, the IRS will no longer accept verbal requests for verification of FBAR filings. All requests for verification of an FBAR filing must be submitted in writing. Consequently, the existing fee structure in IRM 4.26.16.4.13(4)(b) will apply to all verification requests.

In response to written requests, the IRS will send a letter stating whether the record shows that an FBAR was filed and if so, the date filed. If a copy of a paper-filed FBAR was requested, a copy will be included with IRS’s letter.

The IRS has made this process change so that it can have documentary evidence of all FBAR filing verification requests and the IRS’s responses to those requests.

**Overpayment And Underpayment Rates Remain The Same For First Quarter, 2020**

IRS has announced that the interest rates for tax overpayments and underpayments for the calendar quarter beginning Jan. 1, 2020 will be the same as for the fourth quarter of 2019.

For noncorporate taxpayers, the rate for both underpayments and overpayments for the first quarter of 2020 will be 5%.

The 5% rate also applies to estimated tax underpayments for the first calendar quarter beginning Jan. 1, 2020. Pursuant to Code Sec. 6621(b)(2)(B), in determining the addition to tax under Code Sec. 6654 for any tax year for an individual, the federal short-term rate that applies during the third month following the tax year also applies during the first 15 days of the fourth month following the tax year.

The rate of interest on Code Sec. 6603 deposits is 2% for the first quarter of 2020.

For corporations, the overpayment rate for the first quarter of 2020 will be 4%. Corporations will receive 2.5% for overpayments exceeding $10,000. The underpayment rate for corporations will be 5% but will be 7% for large corporate underpayments.

Interest factors for daily compound interest for annual rates of 2.5%, 4%, 5% and 7% are published in Tables 10, 13, 15 and 19 of Rev Proc 95-17, 1995-1 CB 556.

**IRS Finalizes 2019 Form 1040, Form 1040-SR and Schedules 2 and 3**

IRS has issued the final versions of 2019 Forms 1040 and 1040-SR and two of the three schedules that accompany those forms. The final forms are unchanged from the latest draft versions of those forms that were issued in the summer and early fall of 2019.

IRS has not yet finalized the instructions for the above forms.

IRS also has not yet finalized Schedule 1 (Form 1040 or 1040-SR), Additional Income and Adjustments to Income. The most recent draft of Schedule 1, issued on October 10, 2019, added a question related to virtual currency transactions.

**Editor’s Note:** These forms have been posted on the Resources page of ncpeFellowship.com.

**FAQs Address Rental Real Estate Not Covered By Sec. 199A Safe Harbor**

IRS website - Tax Cuts and Jobs Act, Provision 11011 Section 199A - Qualified Business Income Deduction FAQs

The IRS has issued a series of frequently asked questions (FAQs) regarding rental real estate that does not fall under a safe harbor that treats certain rental real estate businesses as trades or businesses solely for the purposes of Code Sec. 199A, the qualified business income deduction.

**Background**—trade or business under Sec. 199A. Congress enacted Code Sec. 199A to provide a deduction to non-corporate taxpayers of up to 20% of the taxpayer's qualified business income (QBI) from each of the taxpayer's qualified trades or businesses, including those operated through a partnership, S corporation, or sole proprietorship, as well as a deduction of up to 20% of aggregate qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership income.

Code Sec. 199A(d) defines a qualified trade or business as any trade or business other than a specified service trade or business (SSTB) or the trade or business of performing services as an employee. Reg § 1.199A-1(b)(14) defines trade or business, in relevant part, as a trade or business under Code Sec. 162 other than the trade or business of performing services as an employee.

**Background**—rental real estate safe harbor. The IRS issued a
revenue procedure that provides a safe harbor for taxpayers who seek to claim the deduction under Code Sec. 199A with respect to a rental real estate income. If the safe harbor requirements are met, the taxpayer's rental real estate business is treated as a single trade or business, as defined in Code Sec. 199A(d), for purposes of applying the regs under Code Sec. 199A, including the application of the aggregation rules in Reg § 1.199A-4. (Rev Proc 2019-38, 2019-42 IRB).

The safe harbor specifically excludes rental real estate rented or leased under a triple net lease.

FAQs. The FAQs emphasize a few points.

The safe harbor is not the only way that rental real estate is treated as a trade or business for purposes of the QBI deduction. The other two ways are: (1) the rental real estate rises to the level of a Code Sec. 162 trade or business, or (2) the rental or licensing of property is to a commonly controlled trade or business operated by an individual or a passthrough entity as described in Reg. § 1.199A-1(b)(14). The second way is often referred to as a self-rental. (FAQ 48). Commonly controlled trades or businesses are, in general, trade or businesses where one person owns 50% or more of each trade or business. (Reg. § 1.199A-4(b)(1)(i))

Whether rental real estate rises to the level of a trade or business under Code Sec. 162 depends on all facts and circumstances. (FAQ 50)

So, while triple net leases do not qualify for the safe harbor, if rental real estate involving a triple net lease is otherwise treated as a trade or business under Code Sec. 199A, then the income, gains, losses and deductions would be included in QBI. (FAQ 57)

One question asks if rental real estate that is treated as a trade or business for purposes Code Sec. 199A, is its income reported on Schedule C of Form 1040 (Profit or Loss From Business (Sole Proprietorship)), and is it subject to self-employment tax? The IRS says that, in general, the answer to both questions is no. How rental real estate is reported on Form 1040 has not changed due to the QBI deduction. Rental real estate is usually reported on Part I of Schedule E (Supplemental Income and Loss (From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)), and is not subject to self-employment tax. Even if rental real estate rises to the level of a Code Sec. 162 trade or business, it is generally reported on Schedule E, Part I, because rental real estate is generally excluded from self-employment taxable income under Code Sec. 1402(a)(1).

However, some rental real estate is subject to self-employment tax (e.g., boarding house, hotel or motel, and bed and breakfast, where substantial services are rendered for the convenience of the occupants). Rental real estate subject to self-employment tax is reported on Schedule C. (FAQ 52)

Code Sec. 199A does not have a material participation requirement. Eligible taxpayers with income from a qualified trade or business may be entitled to the QBI deduction regardless of their level of involvement in the trade or business. (FAQ 54)

IRS Updates Adequate Disclosure Rules For Reducing Or Avoiding Certain Penalties


IRS has updated its adequate disclosure procedure. The procedure identifies when disclosure of an item or position is adequate for purposes of reducing the accuracy-related penalty under Code Sec. 6662(d) and to avoid the tax return preparer penalty under Code Sec. 6694(a). If Code Sec. 6662 applies to any portion of an underpayment of tax required to be shown on a return, an amount equal to 20% of the portion of the underpayment is added to the tax.

The penalty increases to 40% in the case of gross valuation misstatements under Code Sec. 6662(h), nondisclosed noneconomic substance transactions under Code Sec. 6662(i), or undisclosed foreign financial asset understatements under Code Sec. 6662(i).

Except as provided in the next paragraph, there is a substantial understatement of income tax if the amount of the understatement exceeds the greater of (i) 10% of the amount of tax required to be shown on the return for the tax year or (ii) $5,000. (Code Sec. 6662(d)(1)(A))

For corporations (other than S corporations or a personal holding companies), a substantial understatement of income tax exists when the amount of the understatement exceeds the lesser of (i) 10% of the tax required to be shown on the return for a tax year (or, if greater, $10,000) or (ii) 10,000,000. (Code Sec. 6662(d)(1)(B))

An understatement is the excess of the amount of tax required to be shown on the return for the tax year over the amount of the tax that is shown on the return reduced by any rebate. (Code Sec. 6662(d)(2)(A)) Generally, the amount of the understatement is reduced when a taxpayer has a reasonable basis for the tax treatment of the item causing the understatement (except when the item is attributable to a tax shelter) and the relevant facts about the item’s tax treatment are adequately disclosed on the return or in a statement attached to the return. (Code Sec. 6662(d)(2)(B)(iii))

Code Sec. 6694(a) imposes a penalty on a tax return preparer who prepares a return or claim for refund reflecting an understatement of tax liability due to an “unreasonable position” if the tax return preparer knew (or reasonably should have known) of the position.

A position (other than a position with respect to a tax shelter or a reportable transaction to which Code Sec. 6662A applies) is unreasonable unless (i) there is or was substantial authority for the position, or (ii) the position was properly disclosed under Code Sec. 6662(d)(2)(B)(ii) and had a reasonable basis. A position taken with respect to a tax shelter or a reportable transaction is unreasonable unless it is reasonable for the return preparer to believe that the position would more likely than not be sustained on the merits.


Rev Proc 2019-42 provides guidance on how to adequately disclose an item or position on a return for purposes of reducing accuracy-related and avoiding preparer penalties. Generally, a taxpayer must furnish all required information in accordance with the applicable forms and instructions, and the amounts entered on these forms must be verifiable to comply with the Revenue Procedure.

In the Revenue Procedure, IRS has updated the tax years and tax forms to which the procedure applies, but has not made any substantive changes to the previously release guidance in Rev Proc 2019-9.
The Revenue Procedure applies to any income tax return filed on a 2019 tax form for a tax year beginning in 2019 and in to any income tax return filed on a tax form in 2020 for a short tax year beginning in 2020.

Jan. 31 Filing Deadline Remains For Employer Wage Statements, Independent Contractor Forms

The Internal Revenue Service today reminded employers and other businesses that wage statements and independent contractor forms still have a Jan. 31 filing deadline.

Before the Protecting Americans from Tax Hikes (PATH) Act, employers generally had a longer period of time to file these forms. But the 2015 law made a permanent requirement for employers to file their copies of Form W-2, Wage and Tax Statement, and Form W-3, Transmittal of Wage and Tax Statements, with the Social Security Administration by Jan. 31.

Certain Forms 1099-MISC, Miscellaneous Income, filed with the IRS to report non-employee compensation to independent contractors are also due at this time. Such payments are reported in box 7 of this form.

The early filing date means that the IRS can more easily detect refund fraud by verifying income that individuals report on their tax returns. Employers can avoid penalties by filing the forms on time and without errors. The IRS recommends e-file as the quickest, most accurate and convenient way to file these forms.

Get a jump on the due date

Employers should verify employees information. This includes names, addresses, and Social Security or individual taxpayer identification numbers. They should also ensure their company account information is current and active with the Social Security Administration before January. If paper Forms W-2 are needed, they should be ordered early.

Automatic extensions of time to file Forms W-2 are not available. The IRS will only grant extensions for very specific reasons. Details can be found on the instructions for Form 8809, Application for Time to File Information Returns.

IRS Criminal Investigation Releases Fiscal Year 2019 Annual Report; Celebrates 100 Years

The Internal Revenue Service today released the Criminal Investigation Divisions (CI) annual report, highlighting significant successes and criminal enforcement actions taken in fiscal year 2019. The report also commemorates CI’s 100th year anniversary as a law enforcement agency.

CI is critical to the overall enforcement efforts of the IRS in pursuing its Mission in a fair, impartial, diligent and, where appropriate, tenacious manner. said IRS Commissioner Chuck Rettig. The Fiscal Year 2019 Annual Report summarizes various CI activities throughout the year but vastly understates the importance of CI to the overall IRS mission. CI supports the efforts of compliant taxpayers by visibly demonstrating the risks of noncompliance thereby helping otherwise honest taxpayers stay honest and compliant.

Key focuses of CI in fiscal year 2019 included cybercrimes, with an emphasis on virtual and crypto currencies, traditional tax investigations, international tax enforcement, employment tax, refund fraud and tax-related identity theft. Other areas of emphasis included public corruption, corporate fraud and money laundering.

We are working smarter using data analytics to augment good old-fashioned police work and find those cases that have the biggest impact on tax administration, said Don Fort, Chief of CI. We are leading the world in our ability to trace virtual currency in financial investigations while still working our bread and butter tax enforcement mission areas.

CI initiated 2,485 cases in fiscal year 2019, applying approximately 75 percent of its time to tax related investigations. The number of CI special agents dropped to 2,009 by the end of fiscal year 2019, which is the lowest level since the early 1970s. Consequently, CI has increased its usage of data analytics and strengthened its international partnerships to assist in finding the most-impactful cases.

CI is the only federal law enforcement agency with jurisdiction over federal tax crimes. CI achieved a conviction rate of 91.2 percent in fiscal year 2019, which is among the highest of all federal law enforcement agencies. The high conviction rate reflects the thoroughness of CI investigations and the high caliber of CI agents. CI is routinely called upon by prosecutors across the country to lead financial investigations on a wide variety of financial crimes.

While we have published an annual report since 1920 to highlight our successes during the past year, this particular year had special meaning as we celebrated our 100th anniversary as a law enforcement agency, Fort said. Honor the Badge, Preserve the Legacy, Master Your Craft, Inspire the Future. These are the guiding principles that IRS Criminal Investigation lives by and that 2019 was defined by. The 2019 report is interactive, summarizes a wide variety of CI activity during the year and features examples of cases from each field office on a wide range of financial crimes. The federal fiscal year begins Oct. 1 and ends on Sept. 30.

IRS Proposes Regulations On Identifying, Recovering Misdirected Direct Deposit Refunds

The IRS has issued proposed rules for identifying and recovering misdirected direct deposit refunds. The proposed regs reflect changes made by the Taxpayer First Act (TFA, PL 116-25).

Under Code Sec. 6402(n), which was added by the TFA, the IRS is required to establish procedures to allow taxpayers to report when a refund is not direct deposited into the taxpayer’s account as the taxpayer requested.

Code Sec. 6402(n)(2) further directs the IRS to establish procedures for coordination with financial institutions to identify the account to which a misdirected direct deposit refund has been made and to recover such refunds.

Finally, under Code Sec. 6402(n)(3), the IRS is directed to establish procedures to allow a misdirected direct deposit refund to be delivered to the correct account of the taxpayer.

The proposed regs describe the procedures under Code Sec. 6402(n) that will be used when a taxpayer or a taxpayer’s authorized representative notifies the IRS that the requested refund was not received. Generally, the proposed regs adopt current IRS procedures for the reporting, identification, recovery, and delivery of misdirected direct deposit refunds.
The IRS has issued proposed regs under Code Sec. 162(m)(1), which limits the deduction for certain employee remuneration in excess of $1,000,000 (often referred to as executive compensation) for federal income tax purposes. The proposed regs implement the amendments made to Code Sec. 162(m)(1) by the Tax Cuts and Jobs Act. The proposed regs also clarify the application of the grandfather rule for remuneration that is provided under a written binding contract that was in effect as of November 2, 2017.

No deduction is allowed to any "publicly held corporation" for "applicable employee remuneration" for any "covered employee" in excess of $1 million for the tax year. (Code Sec. 162(m)(1))

Code Sec. 162(m)(1) was amended section 13601 of the Tax Cuts and Jobs Act (TCJA) (PL 115-97). The TCJA's amendments to Code Sec. 162(m) included the following: (1) an expansion of the definition of a "covered employee" who is subject to $1 million compensation deduction limitation; (2) the elimination of the exceptions to the $1 million compensation deduction limit for performance-based compensation and commission payments; and (3) an expansion of the definition of a "publicly held corporation" that's subject to $1 million compensation deduction limit, see FTC 2d ¶ H-3777.

But the TCJA added a grandfather rule. The amendments to the Code Sec. 162(m)(1) deduction limitation made the TCJA do not apply to remuneration that is provided under a written binding contract that was in effect as of November 2, 2017, and that was not materially modified on or after that date.

On August 21, 2018, the IRS released Notice 2018-68, 2018-36 IRB 418, which provides guidance on certain issues under Code Sec. 162(m). Specifically, the notice provides guidance on the amended rules for identifying covered employees. Furthermore, the notice provides guidance on the operation of the grandfather rule, including when a contract will be considered materially modified so that it is no longer grandfathered.

The proposed regs, following the language of Code Sec. 162(m), would define a publicly held corporation as any corporation that issues securities required to be registered under section 12(b) of the Exchange Act, or is required to file reports under section 15(d) of the Exchange Act, as of the last day of its tax year. (Prop Reg §1.162-33(c)(1)(i))

A publicly held corporation would include an affiliated group of corporations, as defined in Code Sec. 1504 (determined without regard to Code Sec. 1504(b)) that includes one or more publicly held corporations. In the case of an affiliated group that includes two or more publicly held corporations, each member of the affiliated group that is a publicly held corporation would be separately subject to the proposed regs, and the affiliated group as a whole would be subject to the proposed regs. (Prop Reg §1.162-33(c)(1)(ii)(A))

If, in a tax year, a covered employee (as defined in Prop Reg §1.162-33(c)(2)) of one member of an affiliated group is paid compensation by more than one member of the affiliated group, compensation paid by each member of the affiliated group would be aggregated with compensation paid to the covered employee by all other members of the affiliated group (excluding compensation paid by any other publicly held corporation in the affiliated group, of which the individual is also a covered employee).

In the event that, in a tax year, a covered employee is paid compensation by more than one publicly held corporation in an affiliated group and is also a covered employee of more than one publicly held payor corporation the affiliated group, the amount disallowed as a deduction would be determined separately with respect to each publicly held corporation of which the individual is a covered employee.

Any amount disallowed as a deduction by Prop Reg §1.162-33 would have to be prorated among the payor corporations (excluding any other publicly held payor corporation of which the individual is also a covered employee) in proportion to the amount of compensation paid to the covered employee by each such corporation in the tax year. This process is repeated for each publicly held payor corporation of which the individual is a covered employee. (Prop Reg §1.162-33(c)(1)(ii)(B))

A publicly held corporation would include a corporation that owns an entity that is disregarded as an entity separate from its owner within the meaning of Reg. §301.7701-2(c)(2)(i) if the disregarded entity issues securities required to be registered under section 12(b) of the Exchange Act, or is required to file reports under section 15(d) of the Exchange Act. (Prop Reg §1.162-33(c)(1)(iii))

A publicly held corporation would include an S corporation that owns a qualified subchapter S subsidiary as defined in Code Sec. 1361(b)(3)(B) (QSub) if the QSub issues securities required to be registered under section 12(b) of the Exchange Act, or is required to file reports under section 15(d) of the Exchange Act. (Prop Reg §1.162-33(c)(1)(iv))

Except as provided in Prop Reg §1.162-33(c)(2)(v), with respect to a publicly held corporation, for the publicly held corporation's tax year, a covered employee would mean any of the following:

- The principal executive officer (PEO) or principal financial officer (PFO) of the publicly held corporation serving at any time during the tax year, including individuals acting in either such capacity. (Prop Reg §1.162-33(c)(2)(i)(A))

- The three highest compensated executive officers of the publicly held corporation for the taxable year (other than the PEO or PFO, or an individual acting in such capacity), regardless of whether the executive officer is serving at the end of the publicly held corporation's tax year, and regardless of whether the executive officer's compensation is subject to disclosure for the last completed fiscal year under the executive compensation disclosure rules under the Exchange Act. The amount of compensation used to identify the three most highly compensated executive officers for the tax year would be determined pursuant to the executive compensation disclosure rules under the Exchange Act (using the tax year as the fiscal year for purposes of making the determination), regardless of whether the corporation's fiscal year and tax year end on the same date. (Prop Reg §1.162-33(c)(2)(ii)(B))

- Any individual who was a covered employee of the publicly held corporation (or any predecessor of a publicly held corporation, as defined in Prop Reg §1.162-33(c)(2)(ii), for any preceding tax year beginning after December 31, 2016. For tax years beginning prior to January 1, 2018, covered employees would be identified in accordance with the rules in Reg. §1.162-27(c)(2). (Prop Reg §1.162-33(c)(2)(i)(C))

A predecessor of a publicly held corporation would include a publicly held predecessor of a publicly held corporation. (Prop Reg §1.162-33(c)(2)(iii))
A predecessor of a publicly held corporation would include a publicly held corporation the stock or assets of which are acquired in a corporate reorganization (as defined in Code Sec. 368(a)(1)). (Prop Reg §1.162-33(c)(2)(ii)(B))

A predecessor of a publicly held corporation would include a publicly held corporation that is a distributing corporation (within the meaning of Code Sec. 355(a)(1)(A)) that distributes the stock of a controlled corporation (within the meaning of Code Sec. 355(a)(1)(A)) to its shareholders in a distribution or exchange qualifying under Code Sec. 355(a)(1) (corporate division).

This rule would apply only with respect to covered employees of the distributing corporation who commence the performance of services for the controlled corporation (or for a corporation affiliated with the controlled corporation that receives stock of the controlled corporation in the corporate division) within the period beginning 12 months before and ending 12 months after the distribution. (Prop Reg §1.162-33(c)(2)(ii)(C))

A predecessor of a publicly held corporation would include a publicly held corporation that becomes a member of an affiliated group. (Prop §1.162-33(c)(2)(ii)(D))

If a publicly held corporation, including one or more members of an affiliated group (acquiror), acquires at least 80% of the operating assets (determined by fair market value on the date of acquisition) of another publicly held corporation (target), then the target would be a predecessor of the acquiror.

For an acquisition of assets that occurs over time, only assets acquired within a 12-month period would be taken into account to determine whether at least 80% of the target's operating assets were acquired. However, this 12-month period would be extended to include any continuous period that ends on, or begins on, any day during which the acquiror has an arrangement to purchase, directly or indirectly, assets of the target.

Additions to the assets of target by a shareholder made as part of a plan or arrangement to avoid the application of this subsection to acquiror's purchase of target's assets would be disregarded in applying this rule. This rule would apply only with respect to covered employees of the target who commence the performance of services for the acquiror (or a corporation affiliated with the acquiror) within the period beginning 12 months before and ending 12 months after the date of the transaction (incorporating any extensions to the 12-month period made pursuant to this paragraph). (Prop Reg §1.162-33(c)(2)(ii)(E))

A reference to a predecessor of a corporation would include each predecessor of the corporation and the predecessor or predecessors of any prior predecessor or predecessors. (Prop Reg §1.162-33(c)(2)(ii)(F))

If a corporation that was previously publicly held (the first corporation) would be a predecessor to another corporation (the second corporation) under Prop Reg §1.162-33(c)(2)(ii) but for the fact that it is not a publicly held corporation at the time of the relevant transaction (or transactions), then the first corporation would be a predecessor of a publicly held corporation if the second corporation is a publicly held corporation at the time of the relevant transaction (or transactions) and the relevant transaction (or transactions) take place during a taxable year ending before the 36-month anniversary of the due date for the first corporation's U.S. Federal income tax return (excluding any extensions) for the last taxable year for which the first corporation was previously publicly held. (Prop Reg §1.162-33(c)(2)(ii)(G)(1))

If a corporation that is publicly held (the first corporation) at the time of the relevant transaction (or transactions) would be a predecessor to another corporation (the second corporation) under Prop Reg §1.162-33(c)(2)(ii) but for the fact that the second corporation is not a publicly held corporation at the time of the relevant transaction (or transactions), then the first corporation would be a predecessor of a publicly held corporation if the second corporation becomes a publicly held corporation for a tax year ending before the 36-month anniversary of the due date for the first corporation's U.S. Federal income tax return (excluding any extensions) for the first corporation's last tax year in which the transaction is taken into account. (Prop Reg §1.162-33(c)(2)(ii)(G)(2))

If a corporation that was previously publicly held (the first corporation) would be a predecessor to another corporation (the second corporation) under Prop Reg §1.162-33(c)(2)(ii) but for the fact that neither it nor the second corporation is a publicly held corporation at the time of the relevant transaction (or transactions), then the first corporation would be a predecessor of a publicly held corporation if the second corporation becomes a publicly held corporation for a taxable year ending before the 36-month anniversary of the due date for the first corporation's U.S. Federal income tax return (excluding any extensions) for the last tax year for which the first corporation was previously publicly held. (Prop Reg §1.162-33(c)(2)(ii)(G)(3))

If a corporation that was previously publicly held (the first corporation) would be a predecessor to another corporation (the second corporation) under Prop Reg §1.162-33(c)(2)(ii) but for the fact that the first corporation is (or its assets are) transferred to one or more intervening corporations prior to being transferred to the second corporation, and if each intervening corporation would be a predecessor of a publicly held corporation with respect to the second corporation if the intervening corporation or corporations were publicly held corporations, then Prop Reg §1.162-33(c)(2)(ii)(G)(1) through Prop Reg §1.162-33(c)(2)(ii)(G)(3) would also apply without regard to the intervening corporations. (Prop Reg §1.162-33(c)(2)(ii)(G)(4))

When a corporation makes an election to treat as an asset purchase either the sale, exchange, or distribution of stock pursuant to regulations under Code Sec. 336(e) or the purchase of stock pursuant to regulations under Code Sec. 338, then the corporation that issued the stock would be treated as the same corporation both before and after such transaction. (Prop Reg §1.162-33(c)(2)(ii)(H)) And the rule that a new target and old target are considered the same corporation would apply to the Code Sec. 162(m)(1) deduction limit rules. (Prop Reg §1.338-1(b)(2)(i))

The date that a transaction is treated as having occurred would be the date on which all events necessary for the transaction to be described in the relevant provision have occurred. (Prop Reg §1.162-33(c)(2)(ii)(I))

A publicly traded partnership would be a predecessor of a publicly held corporation if under the same facts and circumstances a
corporation substituted for the publicly traded partnership would be a predecessor of the publicly held corporation, and at the time of the transaction the publicly traded partnership is treated as a publicly held corporation. In making this determination, the rules in Prop Reg §1.162-33(c)(2)(ii)(A) through Prop Reg §1.162-33(c)(2)(ii)(J) would apply to publicly traded partnerships by analogy. (Prop Reg §1.162-33(c)(2)(i)(J))

If a publicly held corporation owns an entity that is disregarded as an entity separate from its owner under Reg. §301.7701-2(c)(2)(i), then the covered employees of the publicly held corporation would be determined pursuant to Prop Reg §1.162-33(c)(2)(i) and Prop Reg §1.162-33(c)(2)(ii). The executive officers of the entity that is disregarded as an entity separate from its corporate owner under Reg. §301.7701-2(c)(2)(i) would be neither covered employees of the entity nor of the publicly held corporation unless they meet the definition of covered employee with respect to the publicly held corporation, in which case they would be covered employees for its tax year. (Prop Reg §1.162-33(c)(2)(iii))

If a publicly held corporation owns an entity that is a QSub under Code Sec. 1361(b)(3)(B), then the covered employees of the publicly held corporation would be determined pursuant to Prop Reg §1.162-33(c)(2)(i) and Prop Reg §1.162-33(c)(2)(ii). The executive officers of the QSub would be neither covered employees of the QSub nor of the publicly held corporation unless they meet the definition of covered employee with respect to the publicly held corporation, in which case they would be covered employees for its tax year. (Prop Reg §1.162-33(c)(2)(iv))

A person who is identified as a covered employee for a publicly held corporation's taxable year would also be a covered employee for the taxable year of a publicly held corporation as defined in Prop Reg §1.162-33(c)(1)(ii). (Prop Reg §1.162-33(c)(2)(iv))

For purposes of the Code Sec. 162(m)(1) deduction limit, compensation would mean the aggregate amount allowable as a deduction under chapter 1 of the Internal Revenue Code for the taxable year (determined without regard to Code Sec. 162(m)(1)) for remuneration for services performed by a covered employee in any capacity, whether or not the services were performed during the taxable year. Compensation would include an amount that is includible in the income of, or paid to, a person other than the covered employee (including a beneficiary after the death of the covered employee) for services performed by the covered employee. (Prop Reg §1.162-33(c)(3)(i))

Compensation would include an amount equal to a publicly held corporation's distributive share of a partnership's deduction for compensation expense attributable to the remuneration paid by the partnership for services performed by a covered employee of the publicly held corporation. (Prop Reg §1.162-33(c)(3)(iii))

Compensation would not include:

- Remuneration covered in Code Sec. 3121(a)(5)(A) through Code Sec. 3121(a)(5)(D) (concerning remuneration that is not treated as wages for purposes of the Federal Insurance Contributions Act);
- Remuneration consisting of any benefit provided to or on behalf of an employee if, at the time the benefit is provided, it is reasonable to believe that the employee will be able to exclude it from gross income; or
- Salary reduction contributions described in Code Sec. 3121(v)(1). (Prop Reg §1.162-33(c)(3)(iii)).

In the case of a corporation that was a privately held corporation (within the meaning of (Prop Reg §1.162-33(c)(9))) and then becomes a publicly held corporation, the Code Sec. 162(m) (1) deduction limitation would apply to any compensation that is otherwise deductible for the tax year ending on or after the date that the corporation becomes a publicly held corporation. A corporation is considered to become publicly held on the date that its registration statement becomes effective either under the Securities Act or the Exchange Act. This applies to a partnership that becomes a publicly traded partnership that is a publicly held corporation. (Prop Reg §1.162-33(d))

The $1,000,000 compensation limitation would be reduced (but not below zero) by the amount (if any) that would have been included in the compensation of the covered employee for the tax year but for being disallowed by reason of Code Sec. 280G. (Prop Reg §1.162-33(e))

The $1,000,000 compensation limitation would also be reduced (but not below zero) by the amount (if any) of any payment (with respect to such employee) of the tax imposed by Code Sec. 4985 directly or indirectly by the expatriated corporation (as defined in Code Sec. 4985(e)(2)) or by any member of the expanded affiliated group (as defined in Code Sec. 4985(e)(4)) that includes such corporation. (Prop Reg §1.162-33(f))

Prop Reg §1.162-33 would not apply to the deduction for remuneration payable under a written binding contract that was in effect on November 2, 2017, and that is not modified in any material respect on or after such date (a grandfathered amount). Instead, Code Sec. 162(m), as in effect prior to its amendment by the TCJA, would apply to limit the deduction for such remuneration.

Accordingly, because Reg §1.162-27 implemented Code Sec. 162(m), as in effect prior to its amendment by the TCJA, the rules of Reg §1.162-27 would determine the applicability of the deduction limitation under Code Sec. 162(m) with respect to the payment of a grandfathered amount. Remuneration would be a grandfathered amount only to the extent that as of November 2, 2017, the corporation was and remains obligated under applicable law (for example, state contract law) to pay the remuneration under the contract if the employee performs services or satisfies the applicable vesting conditions.

Accordingly, Prop Reg §1.162-33 would apply to the deduction for any amount of remuneration that exceeds the grandfathered amount if the employee performs services or satisfies the applicable vesting conditions. If a grandfathered amount and non-grandfathered amount would otherwise be deductible for the same tax year and, under the rules of Reg §1.162-27, the deduction of some or all of the grandfathered amount may be limited (e.g., the grandfathered amount does not satisfy the requirements of Reg. §1.162-27(e)(2) through Reg. §1.162-27(e)(5) as qualified performance-based compensation), then the grandfathered amount would be aggregated with the non-grandfathered amount to determine the deduction disallowance for the tax year under Code Sec. 162(m)(1) (so that the deduction limit applies to the excess of the aggregated amount over $1 million).

If a portion of the remuneration payable under a contract is a grandfathered amount and a portion is subject to Prop Reg §1.162-33 and payment under the contract is made in a series of payments,
the grandfathered amount would be allocated to the first payment of an amount under the contract that is otherwise deductible. If the grandfathered amount exceeds the initial payment, the excess would be allocated to the next payment of an amount under the contract that is otherwise deductible, and this process would be repeated until the entire grandfathered amount has been paid. (Prop Reg §1.162-33(g)(1)(i))

If a written binding contract is renewed after November 2, 2017, Prop Reg §1.162-33 (and not Reg. §1.162-27) would apply to any payments made after the renewal. A written binding contract that is terminable or cancelable by the corporation without the employee’s consent after November 2, 2017, would be treated as renewed as of the earliest date that any such termination or cancellation, if made, would be effective. If the corporation will remain legally obligated by the terms of a contract beyond a certain date at the sole discretion of the employee, then the contract would not be treated as renewed as of that date if the employee exercises the discretion to keep the corporation bound to the contract.

A contract would not be treated as terminable or cancelable if it can be terminated or canceled only by terminating the employment relationship of the employee. A contract would not be treated as renewed if upon termination or cancellation of the contract the employment relationship continues but would no longer be covered by the contract. However, if the employment continues after such termination or cancellation, payments with respect to such post-termination or post-cancellation employment would not be made pursuant to the contract (and, therefore, would not be grandfathered amounts). (Prop Reg §1.162-33(g)(1)(ii))

If a compensation plan or arrangement is binding, the deduction for the amount that the corporation is obligated to pay pursuant to written binding contract in effect on November 2, 2017, to an employee pursuant to the plan or arrangement would not be subject to Prop Reg §1.162-33 even if the employee was not eligible to participate in the plan or arrangement as of November 2, 2017, if the employee was employed on November 2, 2017, by the corporation that maintained the plan or arrangement, or the employee had the right to participate in the plan or arrangement under a written binding contract as of that date. (Prop Reg §1.162-33(g)(1)(iii))

If the corporation is obligated or has discretion to recover compensation paid in a taxable year only upon the future occurrence of a condition that is objectively outside of the corporation’s control, then the corporation’s right to recovery would be disregarded for purposes of determining the grandfathered amount for the tax year. If the condition occurs, only the amount the corporation would be obligated to pay under applicable law remains grandfathered taking into account the occurrence of the condition. Whether or not the corporation exercises its discretion to recover any compensation would not affect the amount of compensation that the corporation remains obligated to pay under applicable law. (Prop Reg §1.162-33(g)(1)(iv))

If a written binding contract is modified after November 2, 2017, Prop Reg §1.162-33 (and not Reg. §1.162-27) would apply to any payments made after the modification. A material modification would occur when the contract is amended to increase the amount of compensation payable to the employee. If a written binding contract is materially modified, then it would be treated as a new contract entered into as of the date of the material modification. Thus, amounts received by an employee under the contract before a material modification would not be affected, but amounts received subsequent to the material modification would be treated as paid pursuant to a new contract, rather than as paid pursuant to a written binding contract in effect on November 2, 2017. (Prop Reg §1.162-33(g)(2)(i))

A modification of the contract that accelerates the payment of compensation would be a material modification unless the amount of compensation paid is discounted to reasonably reflect the time value of money. If the contract is modified to defer the payment of compensation, any compensation paid or to be paid that is in excess of the amount that was originally payable to the employee under the contract would not be treated as resulting in a material modification if the additional amount is based on applying to the amount originally payable either a reasonable rate of interest or the rate of return on a predetermined actual investment as defined in Reg. §31.3121(v)(2)-1(d)(2)(i)(B), (whether or not assets associated with the amount originally owed are actually invested therein) such that the amount payable by the employer at the later date will be based on the reasonable rate of interest or the actual rate of return on the predetermined actual investment (including any decrease, as well as any increase, in the value of the investment). (Prop Reg §1.162-33(g)(2)(ii))

The adoption of a supplemental contract or agreement that provides for increased compensation, or the payment of additional compensation, would be a material modification of a written binding contract if the facts and circumstances demonstrate that the additional compensation is otherwise paid pursuant to the written binding contract. However, a material modification of a written binding contract would not include a supplemental payment that is equal to or less than a reasonable cost-of-living increase over the payment made in the preceding year under that written binding contract. In addition, the failure, in whole or in part, to exercise negative discretion under a contract would not result in the material modification of that contract. (Prop Reg §1.162-33(g)(2)(iii))

If a grandfathered amount is subject to a substantial risk of forfeiture (as defined in Reg. §1.409A-1(d)), then a modification of the contract that results in a lapse of the substantial risk of forfeiture would not be considered a material modification. For compensation received pursuant to the substantial vesting of restricted property, or the exercise of a stock option or stock appreciation right that do not provide for a deferral of compensation (as defined in Reg. §1.409A-1(b)(5)(i) and Reg. §1.409A-1(b)(5)(ii)), a modification of a written binding contract in effect on November 2, 2017, that results in a lapse of the substantial risk of forfeiture (as defined Reg. §1.83-3(c)) would not be considered a material modification. (Prop Reg §1.162-33(g)(2)(iv))

Taxpayers may no longer rely on Notice 2018-68 for tax years ending on or after December 20, 2019, but instead may rely on the proposed regs for those tax years. (Preamble to Prop Reg REG-122180-18)

Except as otherwise provided in Prop Reg §1.162-33(h)(2)(ii), the proposed regs would apply to tax years beginning on or after the date they are published as final regs. (Prop Reg §1.162-33(h)(2)(i))

The definition of covered employee in Prop Reg §1.162-33(c)(2)(i) would apply to tax years ending on or after September 10, 2018. However, for a corporation whose fiscal year and tax year do not end on the same date, Prop Reg §1.162-33(c)(2)(i)(B) would apply to tax years ending on or after December 20, 2019. (Prop Reg §1.162-33(h)(2)(i)(A))

The definition of predecessor of a publicly held corporation in Prop Reg §1.162-33(c)(2)(ii)(A) would apply to any publicly held corporation that becomes a privately held corporation for a taxable...
year beginning after December 31, 2017, and, subsequently, again becomes a publicly held corporation on or after the date the proposed regs are published as final regs. Accordingly, the definition of predecessor of a publicly held corporation in Prop Reg §1.162-33(c)(2)(ii)(C)) would apply to any publicly held corporation that became a privately held corporation for a tax year beginning before January 1, 2018, with respect to the earlier period as a publicly held corporation; or a publicly held corporation that becomes a privately held corporation for a tax year beginning after December 31, 2017 and, subsequently, again becomes a publicly held corporation before the date the proposed regs are published as final regs. (Prop Reg §1.162-33(h)(2)(ii)(B)(1))

The definition of compensation provided in Prop Reg §1.162-33(c)(3)(ii) (relating to allocable shares of partnership deductions for compensation paid) would apply to any deduction for compensation that is otherwise allowable for a tax year ending on or after December 20, 2019. However, this definition of compensation would not apply to compensation paid pursuant to a written binding contract that is in effect on December 20, 2019 and that is not materially modified after that date. For purposes of this paragraph, written binding contract and material modification have the same meanings as provided in Prop Reg §1.162-33(g)(1) and Prop Reg §1.162-33(g)(2). (Prop Reg §1.162-33(h)(2)(ii)(B)(2))

The definition of compensation in Prop Reg §1.162-33(c)(2)(ii)(B) through Prop Reg §1.162-33(c)(2)(ii)(H) would apply to corporate transactions that occur (as provided in the transaction timing rule of paragraph Prop Reg §1.162-33(c)(2)(ii)(I)) on or after the date the proposed regs are published as final regs. (Prop Reg §1.162-33(h)(2)(ii)(B)(2))

The rule in Prop Reg §1.162-33(d) (providing that the Code 163(m) (1) deduction limitation applies to a deduction for any compensation that is otherwise deductible for the tax year ending on or after the date that a privately held corporation becomes a publicly held corporation) would apply to corporations that become publicly held on or after December 20, 2019. A privately held corporation that becomes a publicly held corporation before December 20, 2019 may rely on the transition rules provided in Reg. §1.162-27(f)(1) until the earliest of the events provided in Reg. §1.162-27(f)(2). (Prop Reg §1.162-33(h)(2)(ii)(D))

The transition rules in Prop Reg §1.162-33(g)(1) and Prop Reg §1.162-33(g)(2) (the grandfather rule) would apply to tax years ending on or after September 10, 2018. (Prop Reg §1.162-33(h)(2)(ii)(E))

**Final Regulations Cover Predecessors, Successors And Taxable Spin-offs**

TD 9888; Reg §1.355-8

The IRS has released final regs that provide guidance for determining whether a corporation is a predecessor or successor of a distributing or controlled corporation for purposes of the exception under Code Sec. 355(e) to the nonrecognition treatment afforded qualifying distributions. The final regs adopt the 2016 proposed regs with limited modifications.

Under Code Sec. 355(a)(1), when certain requirements are met, a corporation (Distributing) may make a tax-free distribution of stock, or stock and securities, of a controlled corporation (Controlled) to Distributing’s shareholders, or to its shareholders and security holders (Distribution).

Generally, Code Sec. 355(c) provides that no gain or loss is recognized by Distributing when making a Distribution of qualified property that is not “in pursuit” of a plan of reorganization (Plan). Controlled stock and Controlled securities are “qualified property” for purposes of Code Sec. 355(c). (Code Sec. 355(c)(2)(B))

Generally, Code Sec. 361(c) provides that no gain or loss is recognized to Distributing upon a Distribution of qualified property in pursuit of a Plan. Under Code Sec. 361(c)(2), “qualified property” is (1) any stock, right to acquire stock, or obligation of Distributing, or (2) any stock, right to acquire stock, or obligation of Controlled received by Distributing as part of a divisive reorganization (spin-off, split-up, or split-off).

Under Code Sec. 355(e), stock or securities of Controlled generally will not be treated as qualified property if the stock or securities are distributed as part of a Plan or series of related transactions pursuant to which one or more persons acquire, directly or indirectly, stock representing a 50% or greater interest in the stock (Planned 50% Acquisition) of Distributing or Controlled.

The term “50% or greater interest” means stock possessing at least 50% of the total combined voting power of all classes of stock entitled to vote of at least 50% of the total value of shares of all classes of stock. (Code Sec. 355(e)(4)(A))

For purposes of Code Sec. 355(e), references to Controlled or Distributing include any predecessor or successor of such corporation. (Code Sec. 355(e)(4)(D)) The terms “predecessor” and “successor” are not defined in the Code, so to provide definitions of these terms, the IRS issued proposed regs in 2004 (2004 Proposed Regs) and temporary and proposed regs (the proposed regs cross-referenced the temporary regs) in 2016 (2016 Regs).

Under the 2016 Proposed Regs and the 2016 Regs, Code Sec. 355(e) applies if a Distribution is used to combine a tax-free division of the assets of a corporation other than Distributing or Controlled (Divided Corporation) with a Planned 50% Acquisition of the Divided Corporation. The IRS calls this type of transaction a “synthetic spin-off.” (Preamble to TD 9888)

The IRS drafted the 2004 Proposed Regs primarily to address combining and separating transfers carried out to effect synthetic spin-offs effectuated through a transaction to which Code Sec. 381(a) applied (Section 381 Transaction). See Proposed anti-Morris trust regs would provide guidance on successors and predecessors (12/01/2004).

The 2016 Regs removed the requirement of a Section 381 Transaction, but limited Predecessor of Distributing (POD) treatment to transactions in which all the steps involved in the tax-free division of POD's property occur as part of a Plan. (Preamble to TD 9888) See Temporary regs cover taxable spin-offs (12/22/2016).

The 2019 final regs adopt the 2016 proposed regs with limited modifications and remove the 2016 temporary regs. In general, the final regs follow the approach of the 2016 Regs while incorporating certain requested clarifications and minor revisions.

...Definition of POD. The final regs define the term “Potential Predecessor” as any corporation other than Distributing or Controlled, but only if either (i) as part of a Plan, the corporation transfers property in a Section 381 Transaction to a Potential Predecessor, Distributing, or a member of the same expanded affiliated group as Distributing, or (ii) immediately after completion
of the Plan, the corporation is a member of the same expanded affiliated group as Distributing. (Reg §1.355-8(b)(1)) Only a Potential Predecessor can be a POD. (Reg §1.355-8(a)(3)(ii))

Reflection of Basis Requirement. The final regs clarify that the Reflection of Basis Requirement is satisfied only if any Controlled stock that satisfies the Relevant Property Requirement had a basis prior to the Distribution that was determined, in whole or in part, by reference to the basis of Separated Property and such Controlled stock was neither distributed in a Code Sec. 355(e) distribution nor transferred in a transaction in which the gain, if any, on that Controlled stock was recognized in full. (Reg §1.355-8(b)(1)(ii))

Relevant Property. Relevant Property is one or more of the Potential Predecessor’s assets that were transferred to Controlled in one or more tax-deferred transactions prior to the Distribution. (Reg §1.355-8(a)(3)(ii)(A)) A Potential Predecessor’s assets include Controlled’s stock that, as part of a Plan, was transferred to Distributing in one or more tax-deferred transactions prior to the Distribution. (Reg §1.355-8(a)(3)(ii)(B))

Division of Relevant Property Requirement. The Division of Relevant Property Requirement is satisfied only if ownership of a Potential Predecessor’s Relevant Property has been divided as part of a Plan (Plan Limitation). (Reg §1.355-8(b)(1)(iii)) The Plan Limitation was added to ensure that Relevant Property acquired by a Potential Predecessor, during the relevant period but not pursuant to a plan of reorganization, will not result in an inappropriate application of Code Sec. 355(e)) (Preamble to TD 9888)

Successors. Under the final regs, a Successor of Distributing or of Controlled must be a corporation to which Distributing or Controlled transferred property in a Section 351 Transaction after the Distribution. A partnership can’t be a Successor of Distributing or Controlled. (Reg §1.355-8(d)(2))

Gain limitation rule. The final regs clarify the Gain Limitation Rules to make them easier to understand and apply. The final regs also refine the calculation of the gain limitation under Reg §1.355-8(e)(3) (the Distributing Gain Limitation Rule) to account for the possibility of more than one POD with respect to a single Distribution. (Reg §1.355-8(e))

Relevant equity. The final regs clarify the 2016 Regs by replacing the term “Relevant Stock” with the term “Relevant Equity.” Relevant Equity is Relevant Property that is an equity interest in a corporation or a partnership. This clarification relates only to the determination of the gain limitation, if any, under Reg §1.355-8(e))

No step transaction implications from examples. The IRS has added a specific disclaimer to the final regs that no inference should be drawn from the examples in Reg §1.355-8(h) as to the intended application of the step transaction doctrine and other federal income tax principles.

Examples. The IRS has modified three of the examples (Examples 5, 7, and 8) contained in the 2016 Regs and omitted one example (Example 6). All the retained examples have been updated to reflect modifications in the final regs. For example, the POD analyses in Examples 3 and 4 eliminate the statement that Controlled stock is Separated Property because that fact is no longer relevant under the revised Reflection of Basis Requirement. (Reg §1.355-8(h))

Effective/applicability dates. The final regs are effective on December 16, 2019. These regs apply to distributions occurring after December 15, 2019. (Reg §1.355-8(i)) For distributions occurring on or before December 15, 2019, see Reg §1.355-8T.

Feds Pull Financial Aid Tool After Potential Data Breach

Families applying for federal student aid are facing extra hurdles this year after a potential data breach led federal officials to remove an online tool that smoothed the process.

The Education Department and the Internal Revenue Service said that an online service known as the Data Retrieval Tool will stay offline for the rest of this application season. In the past, families could use the tool to import their tax information automatically to the Free Application for Federal Student Aid, a complex form needed to get federal aid.

Now families filing the form will have to fill out their tax information manually using old tax returns, an obstacle that some education experts fear will deter families from filing.

“It’s not impossible, but it’s going to make it more difficult,” said Justin Draeger, president and chief executive of the National Association of Student Financial Aid Administrators. “Not everybody has access to their prior year’s return.”

Federal officials unexpectedly removed the online tool in early March, at a time when many families across the U.S. were applying for aid. The IRS later said they shut it down because may have used personal information “obtained outside the tax system” to access the online tool in an attempt to steal further data.

Identity thieves could use that information to generate fake tax returns and claim the tax refunds. The IRS said it’s still trying to determine how many taxpayers might have been affected, but added that the agency had already stopped some questionable tax returns that were filed by users who accessed the tool.

IRS Commissioner John Koskinen acknowledged the inconvenience, but said the agency couldn't risk the safety of taxpayer data.

“Protecting taxpayer data has to be the highest priority, and we will continue working with (the Education Department office that handles aid) to bring this tool back in a safe and secure manner,” Koskinen said in a statement.

For families that don’t have copies of their tax returns, the IRS suggests trying to retrieve the documents from their tax preparers or the software they used to file it. If needed, the IRS can also provide a tax transcript that includes a summary of previously filed.

The tool's absence could cause extra work for colleges, too. The IRS routinely asks campuses to verify the on the form from certain students as a security measure. In the past, students who didn't use the were more likely to be selected for extra verification, Draeger said. Some colleges have already noticed an increase in verification requests this year.

“If nobody is using the IRS data retrieval tool, it’s unclear whether this is going to throw a wrench into their income verification modeling,” Draeger said.

Federal officials say the data tool will remain offline until the start of the next FAFSA season, which typically begins Oct. 1.
IRS Seeks Applications For The Electronic Tax Administration Advisory Committee for 2020

The Internal Revenue Service is seeking qualified applicants for nomination to the Electronic Tax Administration Advisory Committee (ETAAC).

The ETAAC is an organized public forum for discussion of electronic tax administration issues, such as prevention of identity theft and refund fraud in support of the overriding goal that paperless filing should be the preferred and most convenient method of filing tax and information returns. ETAAC members work closely with the Security Summit, a joint effort of the IRS, state tax administrators and the nation’s tax industry, to fight identity theft and refund fraud.

The IRS is looking for approximately 10 qualified individuals who will serve three-year terms beginning in September 2020. Applicants should have experience in such areas as state tax administration, cybersecurity and information security, tax software development, tax preparation, payroll and tax financial product processing, systems management and improvement and implementation of customer service initiatives.

The IRS also strongly encourages representatives from consumer groups with an interest in tax issues to apply.

Applications will be accepted through Feb. 14, 2020. Nominations of qualified individuals may be made by letter and received from organizations or the individuals themselves. Applicants should complete the ETAAC application and include a short statement of interest and a resume. Applicants should describe and document their qualifications, past and current affiliations, and dealings with cybersecurity and electronic tax administration. More information is available on IRS.gov.

Applicants must complete and submit a tax check waiver form and pass both an IRS practitioner background check and FBI criminal background check.

ETAAC is a Federal Advisory Committee established by the Internal Revenue Service Restructuring and Reform Act of 1998.

Questions about the ETAAC and the application process can be e-mailed to publicliaison@irs.gov.

IRS And TTB Formalize Process To Support Processing Of Claims Made To The IRS Whistleblower Office

The Internal Revenue Service announced a process has been formalized with the Alcohol and Tobacco Tax and Trade Bureau (TTB) that puts in place procedures between the IRS and TTB to process claims for whistleblower awards under internal revenue laws that are administered and enforced by TTB.

The IRS and TTB signed a Memorandum of Understanding on December 3, 2019, making these new procedures possible.

"This is another important step in our efforts to make the Whistleblower Program as effective as possible," said Lee D. Martin, Director of the IRS Whistleblower Office. "The IRS Whistleblower Office is always looking to do more for whistleblowers."

The new procedures enable a partnership with TTB to provide a consistent approach for claims for a whistleblower award administered under Internal Revenue laws.

TTB is a bureau of the Treasury Department and administers provisions of the Internal Revenue laws that impose a federal excise tax on distilled spirits, wine, beer, tobacco products, cigarette papers and tubes, as well as firearms and ammunition.

"The whistleblower program gives us another tool to fight for the level playing field that our law-abiding industry members expect and deserve," said Nicholas Colucci, TTB’s Assistant Administrator, Field Operations. "We appreciate this opportunity to partner with our colleagues at the IRS."

Since 2007, the IRS Whistleblower Office made awards totaling more than $811 million based on the collection of more than $5 billion in back taxes, interest and penalties.

IRS Reminds Tax-exempt Organizations Of Obligation To E-file Returns

In an Information Release, the IRS has reminded tax exempt organizations that for tax years beginning after July 1, 2019, they may be required to file information returns and related forms electronically. Sec. 3101(a) of The Taxpayer First Act (TTFA, PL 116-25, 07/01/2019), requires tax-exempt organization to electronically file their information returns and related forms for tax years beginning after July 1, 2019. Transition relief was provided for organizations that would suffer an undue hardship from the e-filing requirement. (TTFA, Sec. 3101(d)) Under the transition relief, the IRS must implement the requirement to file electronically for these organizations not later than tax years beginning July 1, 2021.

The following forms commonly filed by tax-exempt organizations were included in the TTFA electronic filing mandate:

- Form 8872, Political Organization Report of Contributions and Expenditures. Form 8872 is generally filed by political organizations exempt from tax under Code Sec. 527 (Code Sec. 527 organizations), such as political parties, political action committees and campaign committees of candidates for federal, state or local office. (Form 8872, Instructions)

- Form 990, Return of Organization Exempt from Income Tax. Generally, Form 990 is filed by tax-exempt organizations with (1) gross receipts of $200,000 or more, or (2) total assets of $500,000 or more at the end of the tax year. (Form 990, Instructions)

- Form 990-PF, Return of Private Foundation or Section 4947(a) (1) Trust Treated as Private Foundation. Form 990-PF generally is filed by tax-exempt private foundations, taxable private foundations, and non-exempt charitable trusts treated as private foundations. (Form 990-PF, Instructions)

- Form 990-EZ, Short Form Return of Organization Exempt from Income Tax, is filed by tax-exempt organizations with (1) gross receipts more than $50,000 and less than $200,000, and (2) total assets less than $500,000 at the end of the tax year. (Form 990-EZ, Instructions)

New electronic filing requirements. The IRS has reminded tax-exempt organization that for tax years beginning after July 1, 2019, they may be required to file information returns and related forms electronically.
must file it electronically for periods beginning on or after January 1, 2020. The IRS will no longer accept paper Forms 8872 from Code Sec. 527 organizations for periods beginning on or after January 1, 2020.

To file electronically, a Code Sec. 527 organization must have the username and password it received from the IRS after electronically filing its Form 8871, Initial Notice. In the event a Code Sec. 527 organization has lost its user name or password, the organization should contact: IRS, Attn: Request for 8872 Password, Mail Stop 6273, Ogden UT 84201; Fax (855) 214-7520. Code Sec. 527 organizations can file electronically using the IRS website at IRS.gov/polorgs.

Form 990 and Form 990-PF. Tax-exempt organizations that file Form 990 or Form 990-PF must electronically file those forms for tax years beginning after July 1, 2019.

However, until further notice, the IRS will continue to accept paper filings for short year returns, and in certain other circumstances detailed in the Form 990 and Form 990-PF instructions, because its systems are not able to receive these forms electronically.

Form 990-EZ. The IRS will postpone the required e-filing of Form 990-EZ, while optional e-filing continues to be available. Tax-exempt organizations that file Form 990-EZ will be required to electronically file that form beginning with tax years ending on or after August 31, 2020.

Forms 990-T and 4720. In 2020, the IRS will continue to accept paper forms that are pending conversion into electronic format. These include Form 990-T, Exempt Organization Business Income Tax Return, and Form 4720, Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code. The IRS plans to have these returns ready for e-filing in 2021 (reporting on tax year 2020).

Proposed Regulations On Charitable Contributions In Exchange For State And Local Tax Credits

The IRS has released proposed regs clarifying how to treat certain contributions made to a charity in return for state and local tax credits.

Code Sec. 164(b)(6), as added by section 11042(a) of the Tax Cuts and Jobs Act (TCJA, PL 115-97), provides that an individual’s deduction for state and local taxes paid during a calendar year is limited to $10,000. The $10,000 limit applies to: (1) real property taxes; (2) personal property taxes; (3) income war profits and excess profits taxes; and (4) general sales taxes. This limitation applies to tax years beginning after December 31, 2017, and before January 1, 2026. The $10,000 limit does not apply to foreign taxes or state and local taxes that are paid or accrued in carrying on a trade or business or an investment activity.

In response to the limitation in Code Sec. 164(b)(6), some taxpayers have considered tax planning strategies to avoid or mitigate its effects. Some of these strategies rely on state and local tax credit programs under which states provide tax credits in return for contributions to certain charitable entities, contributions to which are tax deductible under Code Sec. 170. In response to these tax planning strategies, the IRS has issued various forms of guidance, including proposed (Preamble to Prop Reg REG-112176-18) and final regs (TD 9864).

The new proposed regs provide guidance on issues that remain unclear despite previous guidance. These issues include: (1) the treatment of business entity payments to entities described in Code Sec. 170(c); (2) the treatment of payments by individuals with total state and local tax liabilities that were less than or equal to the Code Sec.164(b)(6) limitation; and (3) application of the quid pro quo principle under Code Sec. 170 to benefits received or expected to be received by the donor from a party other than the done.

IRS And The Taxpayer First Act

The Taxpayer First Act, enacted July 1, 2019, requires tax-exempt organizations to electronically file information returns and related forms. The new law affects tax-exempt organizations in tax years beginning after July 1, 2019.

The following IRS forms are included in the mandate:

- Form 990, Return of Organization Exempt from Income Tax.
- Form 990-PF, Return of Private Foundation or Section 4947(a) (1) Trust Treated as Private Foundation.
- Form 8872, Political Organization Report of Contributions and Expenditures.
- Form 1065, U.S. Return of Partnership Income (if filed by a Section 501(d) apostolic organization).

Those who previously filed paper forms will receive a letter from the IRS informing them of the change. Filing deadlines vary by form type. The IRS will postpone the required e-filing of Form 990-EZ for one year, while optional e-filing continues to be available. Although Forms 990-T and 4720 will come under the e-filing requirement next year, the IRS will continue to accept these forms on paper pending conversion to electronic format.

Form 8872

The IRS will no longer accept paper Forms 8872 reporting on periods after 2019. Forms 8872 reporting information for periods starting on or after Jan. 2020, will be due electronically by Section 527 organizations. These include political parties, political action committees and campaign committees of candidates for federal, state or local office.

Among other requirements, most tax-exempt political organizations have a requirement to file semiannual, quarterly or monthly reports on Form 8872. To file electronically, the organization must have the username and password it received from the IRS after electronically filing its initial notice (Form 8871). Organizations can file electronically using the IRS website at IRS.gov/polorgs. To replace a username or password, please contact: IRS

Attn: Request for 8872 Password
Mail Stop 6273,
Ogden, UT 84201 Fax (855) 214-7520

Form 990 & 990-PF E-filing

Under the legislation, most e-filings won’t be due before Dec. 15, 2020, from charities and other exempt organizations that generally file Form 990 or 990-PF by the 15th day of the 5th month after the tax year-end. In other words, Forms 990 and 990-PF with tax years ending July 31, 2020, and later MUST be filed electronically. Forms 990 and 990-PF filings for tax years ended on or before June 30,
The Taxpayer First Act aims to expand and strengthen taxpayer rights and to reform the IRS into a more taxpayer friendly agency. The legislation specifically allowed a postponement (“transitional relief”). For tax years ending on or before July 31, 2020, the IRS will accept either paper or electronic filing of Form 990-EZ, Short Form Return of Organization Exempt from Income Tax. For tax years ending Aug. 31, 2020, and later, Forms 990-EZ must be filed electronically. Generally, Form 990-EZ is for organizations with annual gross receipts less than $200,000 and total assets at tax year-end less than $500,000.

Pre-existing E-file Rules

In effect, the legislation supersedes the pre-existing e-file regulation for large exempt organizations. Until tax years beginning after July 1, 2019, exempt organizations with total assets of $10 million or more at tax year-end that had filed 250 or more returns of any type during the calendar year were required to e-file Forms 990 and 990-PF. E-filing was also required of Form 8872 filers that had or expected more than $50,000 of contributions or expenditures in the calendar year. These prior rules will continue to apply to some e-filings in 2020.

Form 990-EZ Transition Relief

For small exempt organizations, the legislation specifically allowed a postponement (“transitional relief”). For tax years ending on or before July 31, 2020, the IRS will accept either paper or electronic filing of Form 990-EZ, Short Form Return of Organization Exempt from Income Tax. For tax years ending Aug. 31, 2020, and later, Forms 990-EZ must be filed electronically. Generally, Form 990-EZ is for organizations with annual gross receipts less than $200,000 and total assets at tax year-end less than $500,000.

Paper Forms 990-T & 4720

In 2020, the IRS will continue to accept paper forms. These include Form 990-T, Exempt Organization Business Income Tax Return, and Form 4720, Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code. The IRS plans to have these returns ready for e-filing in 2021 (reporting on tax year 2020).

Employee FAQs

4. My tax situation is simple. Do I have to complete all of the steps?

No. The form is divided into 5 steps. The only two steps required for all employees are Step 1, where you enter personal information like your name and filing status, and Step 5, where you sign the form. Complete Steps 2 - 4 only if they apply to you. Doing so will make your withholding more accurately match your liability.

5. What happens if I only fill out Step 1 and then sign the form?

Your withholding will be computed based on your filing status’s standard deduction and tax rates, with no other adjustments.

6. When should I increase my withholding?

You should generally increase your withholding if:

- you hold more than one job at a time or you and your spouse both have jobs (Step 2) or
- you have income from sources other than jobs or self-employment that is not subject to withholding (Step 4(a)). If you do not make adjustments to your withholding for these situations, you will very likely owe additional tax when filing your tax return, and you may owe penalties. For income from sources other than jobs, you can pay estimated tax instead of having extra withholding.

7. When should I decrease my withholding?

You should generally decrease your withholding if:

- you are eligible for income tax credits such as the child tax credit or credit for other dependents (Step 3), and/or
- you are eligible for deductions other than the basic standard deduction, such as itemized deductions, the deduction for IRA contributions, or the deduction for student loan interest (Step 4(b)).

8. I want a refund when I file my tax return. How should I complete the redesigned Form W-4?

The redesigned Form W-4 makes it easier for you to have your withholding match your tax liability. But if you prefer to have more tax than necessary withheld from each paycheck, you will get that money back as a refund when you file your tax return (keep in mind...
though you do not earn interest on the amount you overpay). The simplest way to increase your withholding is to enter in Step 4(c) the additional amount you would like your employer to withhold from each paycheck. Note, even if you don't have any income tax withheld from your wages, you may get a refund if you are eligible for tax credits such as the Earned Income Credit, the Additional Child Tax Credit, or American Opportunity Credit.

9. Why do I need to account for multiple jobs (Step 2)? I have never done that before.

Tax rates increase as income rises, and only one standard deduction can be claimed on each tax return, regardless of the number of jobs. Therefore, if you have more than one job at a time or are married filing jointly and both you and your spouse work, more money should usually be withheld from the combined pay for all the jobs than would be withheld if each job was considered by itself. Adjustments to your withholding must be made to avoid owing additional tax, and potentially penalties, when you file your tax return. All of this has been true for many years; it did not change with the recent tax law changes. The old Form W-4 accounted for multiple jobs using detailed instructions and worksheets that many employees may have overlooked. Step 2 of the redesigned Form W-4 lists three different options you should choose from to make the necessary withholding adjustments. Note that, to be accurate, you should furnish a 2020 Form W-4 for all of these jobs.

10. Which option in Step 2 should I use to account for my multiple jobs? Which is most accurate? What if I don't want to reveal to my employer on my W-4 that I have a second job?

Step 2 allows you to choose one of three options, which involve tradeoffs between accuracy, privacy, and ease of use:

• Step 2(a): For maximum accuracy and privacy, use the Tax Withholding Estimator at www.irs.gov/W4app. You will generally be guided to enter an additional amount to withhold in Step 4(c). While you will need to know the approximate amount of pay for each job, you will enter the additional amount of withholding in Step 4(c) on the Form W-4 for only one of the jobs. If pay for any of the jobs changes significantly, you will need to use the Tax Withholding Estimator again and furnish a new Form W-4 to change the amount in Step 4(c) to have accurate withholding.

• Step 2(b): If you do not have access to the Tax Withholding Estimator but wish to have roughly accurate withholding and retain privacy, you may use the Multiple Jobs Worksheet on page 3. You will be guided to enter an additional amount to withhold in Step 4(c). While you will need to know the approximate amount of pay for each job, you will enter the additional amount of withholding in Step 4(c) on the Form W-4 for only one of the jobs. If a change in pay for any of the jobs changes the additional withholding amount in the lookup table used with this worksheet, you will need to furnish a new Form W-4 to change the amount in Step 4(c) to have accurate withholding. If you (and your spouse) have a total of only two jobs and the pay at the higher paying job is more than double the pay at the lower paying job, this option is generally more accurate than choosing Step 2(c). If the pay at each job is more similar, choosing Step 2(c) is more accurate than choosing Step 2(b).

• Step 2(c): If you (and your spouse) have a total of only two jobs held at the same time, you may check the box in Step 2(c) on the Forms W-4 for both jobs. That is, to use this option, you should complete a Form W-4 for each job with the box in Step 2(c) checked. The standard deduction and tax brackets will be cut in half for each job to calculate withholding. You will not need to furnish a new Form W-4 to account for pay changes at either job. This option is accurate for jobs with similar pay; otherwise more tax than necessary may be withheld from your wages. This extra amount will be larger the greater the difference in pay is between the two jobs.

11. The instructions above Step 3 say that in multiple job households, adjustments in Steps 3 – 4b are to be made on only one form, and that withholding will be most accurate if the adjustments are made on the W-4 for the highest paying job. But what happens if pay at two jobs is relatively similar or if changes in pay over time result in another job becoming the highest paying?

In general, making these adjustments on the Form W-4 for the highest paying job increases accuracy. However, if the jobs in your household pay about the same or if changes in pay over time change which is the highest paying job, it is less important which Form W-4 is used to make the adjustment.

12. What if I have side work where I’m not treated as an employee?

If you have income from self-employment (including as an independent contractor), you will generally owe both income tax and self-employment tax. Form W-4 is primarily intended to be used by employees who are not subject to self-employment tax. Thus, like the old Form W-4, the redesigned Form W-4 does not compute self-employment tax. If you would like to use Form W-4 to make an adjustment to your withholding to account for self-employment income that you will receive from another source, use the Tax Withholding Estimator at www.irs.gov/W4app or refer to IRS Publication 505.

13. What if I don't want to reveal the amount of my non-job income, such as income from earnings on investments or retirement income, on my Form W-4 (Step 4(a))?

You are not required to have tax on non-job income withheld from your paycheck. Instead, you can pay estimated tax on this income using Form 1040-ES, Estimated Tax for Individuals. However, if you want to use Form W-4 to have tax for this income withheld from your paycheck and you do not want to report this income directly in Step 4(a), you have several options. First, you can use the Tax Withholding Estimator at www.irs.gov/W4app. The estimator will help you calculate the additional amount of tax that should be withheld from your paycheck. You will then enter that amount in Step 4(c), without reporting the income to your employer. Second, you can determine for yourself the amount of extra withholding needed to pay the tax on your other income (for example, by using Publication 505), divide that amount by the number of pay dates in the year, and enter the result in Step 4(c). Third, if this is the only job in your household, you can check the box in Step 2(c), which will increase your withholding and significantly reduce your paycheck. The amount of this extra withholding varies across taxpayers and ranges from zero to $20,000 annually—and you may not know how much extra is being withheld. Also, whether this extra withholding in turn is too little or too much—and results in a balance due or refund—depends on the amount of your non-job income.

14. Is there a computer program I can use to help me complete Form W-4?

Yes. To provide maximum accuracy, you are encouraged to use
19. Will there still be an adjustment for nonresident aliens?

Yes. The IRS will provide instructions in the 2020 Publication 15-T, Federal Income Tax Withholding Methods, on the additional amounts that should be added to wages to determine withholding for nonresident aliens. Additionally, nonresident alien employees should continue to follow the special instructions in Notice 1392 when completing their Forms W-4.

20. When can we start using the new 2020 Form W-4?

The new 2020 Form W-4 can be used with respect to wages to be paid in 2020.

**IRS Internal Guidance On Centralized Partnership Audit Regime Field Audits**

In an Internal Memorandum, the IRS has provided its examiners with procedures for conducting field audits of partnerships under the centralized partnership (BBA) audit regime.

**Background.** For tax years covered by the previous set of partnership rules, partnerships were audited under the unified partnership audit and litigation rules enacted as part of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA, PL 97-248), which are commonly referred to as the TEFRA partnership procedures. Some partnerships were not subject to the TEFRA partnership procedures (Code Sec. 6230(a)(1); Code Sec. 6240(b)(1)); those partnerships were said to be covered by “Non-TEFRA” rules.

In 2015, Section 1101 of the Bipartisan Budget Act of 2015 (BBA, PL 114-74) repealed the TEFRA partnership procedures and the Non-TEFRA rules, replacing them entirely with an entirely new centralized partnership audit regime (BBA audit regime).

Generally, the BBA audit regime provides for adjustments of partnership returns, and assessment and collection of tax attributable to such adjustments, at the partnership level. (BBA Sec. 1101(c)) The BBA allows certain partnerships to elect out of the BBA audit regime. (Code Sec. 6221(b) as amended by the BBA)

Under the BBA regime, a partnership must designate a partnership representative (PR) who has the sole authority to act on behalf of the partnership. (Code Sec. 6223(a)) A partnership’s partners are bound by the decisions made by the PR. (Code Sec. 6223(b))

The BBA audit regime applies to all partnerships for tax years beginning after December 31, 2017 (BBA Sec. 1101(g)(1)) However, the BBA audit regime also applies to partnerships that elect into the BBA regime for tax years beginning after November 2, 2015 and before January 1, 2018. (BBA Sec. 1101(g)(4))

Under proposed regs, a partner’s treatment of each item of income, gain, loss, deduction, or credit attributable to a partnership would have to be consistent with the treatment of those items on the partnership return, including treatment of the amount, timing, and characterization of those items. (Prop Reg §301.6222-1(a)(1))

BBA audit regime field exam procedures. The new BBA audit regime field exam procedures, which will be housed in new Internal Revenue Manual (IRM) Chapter 4.31.9, cover the following:

- the scope of a BBA audit.
- planning the examination.
- determining whether a partnership is subject to the BBA audit...
Northern District of Illinois.

...determining whether a partnership subject to the BBA audit regime made a valid election out.

...whether the partnership designated a PR on (1) Page 3, of Form 1065, U.S. Return of Partnership Income, or (2) Form 8979, Partnership Representative Revocation, Designation, and Resignation.

...how the examiner should designate a PR if the partnership hasn’t designated one.

...how to handle a partnership’s administrative adjustment request (AAR), including the scope of an AAR and executing an AAR examination.

...initiating a BBA examination, including sending a Notice of Administrative Proceeding (NAP).

...how to spot a partner’s inconsistent treatment of partnership items.

...the statute of limitations on making adjustments and how and when to ask a partnership to extend the limitations period; and

...resolving the examination, including report writing and case disposition guidelines.

The BBA audit regime field examination procedures note that examiners should correctly document and file all actions, determinations, forms, letters etc. using these procedures.

Clarification On Increased Section 6713 Penalties For Unauthorized Disclosure

The IRS e-News included an update to IRC section 6713. To clarify, the penalty is still $250 (with a $10,000 maximum per person per calendar year) for each unauthorized disclosure or use of return information.

The Taxpayer First Act of 2019 increased the penalty to $1,000 (with a $50,000 maximum per person per calendar year) if a disclosure or use is made in connection with a crime relating to the misappropriation of another person’s taxpayer identity, whether or not such crime involves any tax filing.

This increased penalty amount applies to disclosures or uses that are made on or after July 1, 2019 (the date the Taxpayer First Act of 2019 was enacted).

Tax Pros in Trouble

Federal Court Shuts Down Illinois Tax Return Preparer

A federal court has permanently barred Jackelin Brooks, a Bolingbrook, Illinois tax return preparer, from preparing federal tax returns for others, the Justice Department announced today. The civil injunction order was entered by the U.S. District Court for the Northern District of Illinois.

According to the government’s complaint, Brooks, a Bolingbrook resident, prepared returns that reported false income and expenses from Schedule C businesses and improperly claimed the American Opportunity Tax Credit and the Residential Energy Credit, resulting in refunds to which her customers were not entitled. The complaint alleges that the falsified tax returns cost the United States tens of thousands of dollars in tax revenue. The injunction was entered against Brooks by default because she failed to defend against the government’s allegations.

Return preparer fraud is one of the IRS’s “Dirty Dozen” tax scams for 2019. In the past 10 years, the Justice Department’s Tax Division has obtained injunctions against hundreds of return preparers and tax-fraud promoters. Information about these cases is available on the Justice Department website.

Maryland Tax Preparer Pleads Guilty To Preparing False Returns And Aggravated Identity Theft

Office Sign Advertised Identities for Sale

A Maryland tax return preparer pleaded guilty to aiding and assisting in filing false tax returns and aggravated identity theft, announced Principal Deputy Assistant Attorney General Richard E. Zuckerman of the Justice Department’s Tax Division and U.S. Attorney Robert K. Hur of the District of Maryland.

According to court documents and statements made in court, Maria Espinal owned and operated a tax return preparation business located in Gaithersburg, Maryland. From 2011 through 2017, Maria Espinal prepared and filed fraudulent tax returns on behalf of her clients with the Internal Revenue Service (IRS) and the Comptroller of Maryland that claimed tax refunds to which the clients were not entitled. To generate a fraudulent refund, Espinal altered legitimate Forms W-2 in the names of third parties and replaced the third party’s name with her client’s name. As a result, her client claimed the third-party’s withholdings as his or her own, which generated fraudulent tax refunds.

In addition, Espinal displayed a sign on her office wall that read in Spanish “If you have lost your [identification] number or passport we have these people” and which listed the identifying information for several individuals. Espinal used the personal identifying information for one of those individuals to obtain a fraudulent refund on behalf of another client. Espinal also filed a tax return using another individual’s personal identifying information to generate a fraudulent refund that Espinal deposited into her own personal bank account.

U.S. District Judge Theodore Chuang set sentencing for April 2, 2020. Espinal faces a mandatory sentence of two years in prison for aggravated identity theft, and three years in prison for aiding in the preparation of a false tax return. She also faces a period of supervised release, restitution, and monetary penalties.

Principal Deputy Assistant Attorney General Zuckerman and U.S. Attorney Hur thanked Special Agents of IRS - Criminal Investigation and Enforcement Agents of the Comptroller of Maryland who conducted the investigation, and Trial Attorney Carl Brooker of the Tax Division and Assistant United States Attorney Erin Pulice of the District or Maryland, who are prosecuting the case.
Richland Tax Preparer Indicted For Filing Fraudulent Returns

A Richland tax preparer was indicted on federal charges he filed individual returns for clients who claimed inflated refunds.

Jonathon F. Schumann, the owner of J’s Income Tax, allegedly prepared and filed at least 16 false and fraudulent returns for 2015 and 2016.

Some of the clients may have been involved in the fraud both years, according to the six-page indictment filed in U.S. District Court showing the same initials for four different people.

While the grand jury was given the full identity of each client, they are only referred to in the public documents by their initials.

Schumann charged fees for preparing the 1040 and itemized deduction forms, and normally deducted his bill from the clients’ inflated refunds, federal prosecutors said in the document.

It does not say if his business fees were based on a percentage of the refund amount.

The indictment is for 16 counts of aiding and assisting in the preparation and filing of a false income tax return.

Schumann could not be reached Wednesday about the criminal charges.

If convicted, he faces up to three years in federal prison, along with a fine, restitution and the costs of prosecution.

Schumann reportedly lives in both Richland and Las Vegas.

He was the sole proprietor of the now-closed J’s Income Tax, which once operated out of a West Gage Boulevard office, in addition to his Richland home, according to the Washington state Department of Revenue.

In March 2003, Schumann applied for and was assigned an identification number by the Internal Revenue Service to use the electronic filing program, or e-file.

At the same time, he was approved by the agency to become an electronic return originator — an individual or entity authorized to submit electronic returns on behalf of clients for a preparation or processing fee.

Then, starting in January 2011, the IRS required all paid federal tax return preparers to have an identification number specifically for that purpose. Schumann applied for his in October 2012, according to the indictment.

Federal prosecutors allege Schumann knew his clients were not entitled to the money when he prepared individual income tax returns claiming inflated refunds.

The illegal refunds were based on itemized deductions by falsely claiming things like charitable contributions, unreimbursed employee business expenses and personal property and sales taxes, the indictment states.

“Each of these categories of deductions has different requirements and limitations on the amount a taxpayer can deduct,” according to the court document.

Employee business expenses cover everything from vehicle and travel expenses to meals and entertainment.

Court records do not show when Schumann will first appear in federal court. The case has been assigned to Judge Sal Mendoza Jr.

Tax Return Preparers Gregory Doneal Mack Plead Guilty To Filing False Tax Returns

U.S. Attorney Andrew Murray announced that Gregory Doneal Mack, 56, of Charlotte, appeared in federal court today and pleaded guilty to preparing false tax returns while working for a tax return preparation business. The owner of the tax preparation business, Sean Dalton Williams, 48, of Charlotte, previously pleaded guilty to aiding and assisting the preparation of a false tax return.

U.S. Attorney Murray is joined by Matthew D. Line, Special Agent in Charge of the Internal Revenue Service, Criminal Investigation Division (IRS-CI), in making today’s announcement.

“Tax preparers are the gatekeepers of our tax system, tasked with safeguarding its integrity and complying with our nation’s tax laws, not using their expertise to help clients evade their tax obligations at the expense of honest taxpayers. My office’s tax prosecutors are dedicated to uncovering tax fraud and holding cheats accountable for their actions,” said U.S. Attorney Murray.

“Taxpayers should choose carefully when hiring a tax return preparer. While most return preparers are honest and provide excellent service, a few unscrupulous tax preparers file false returns to defraud the government and their clients. All taxpayers should know that IRS Criminal Investigation will vigorously pursue those dishonest tax return preparers and hold them accountable for their illegal actions,” said Special Agent in Charge Line.

According to filed plea documents and today’s plea hearing, from 2012 to 2017, Mack worked as a tax return preparer at SW Financial Group (SWFG), a Charlotte-area tax preparation business owned and operated by Williams. According to court records, while working at SWFG, Mack and Williams prepared fraudulent U.S. Individual Income Tax Returns, Forms 1040, and related IRS Schedules and Forms, that contained fabricated and/or fraudulent items on Schedules A and C. As a result, the defendants’ clients’ tax liabilities were reduced, resulting in inflated refunds.

According to court records, the tax loss to the government associated with the inaccurate tax returns prepared by Mack for tax years 2012 to 2017 is approximately $282,967. The tax loss associated with the fraudulent tax returns prepared by Williams for tax years 2012 to 2015 is $276,540. Court records show that during the time that Williams perpetrated the tax fraud, he was also on pretrial release on federal charges related to a mortgage fraud scheme.

Both defendants pleaded guilty to aiding and assisting the preparation of a false tax return. The charge carries a maximum penalty of three years in prison and a $250,000 fine. A sentencing date for Mack and Williams has not been set.

In a separate case, Cletise Hammonds, 48, of Charlotte, has pleaded guilty to preparing false tax returns. Court documents filed in this case show that, from 2011 to 2017, Hammonds owned and operated Accurate Tax and Bookkeeping LLC (Accurate Tax), a tax preparation business located in Charlotte. As Hammonds previously admitted in
plea documents, through Accurate Tax, Hammonds prepared and filed false tax returns for clients that included fraudulent Schedule C income expenses, education credits, and dependents, among other things. The false and fraudulent items resulted in the fraudulent reduction of the clients’ tax liabilities, and the receipt of fraudulently inflated refunds. According to court records, Hammonds charged between $200 to $700 for preparation of tax returns, and his tax preparation fees were taken directly from the clients’ tax refunds. According to court records, the tax loss associated with the fraudulent returns prepared and filed by Hammonds is $329,568. Hammonds has pleaded guilty to aiding and assisting in the preparation of false tax returns and is currently awaiting sentencing.

In making the announcement, U.S. Attorney Murray commended IRS-CI for handling these investigations.

Assistant United States Attorney Caryn Finley of the U.S. Attorney’s Office in Charlotte is prosecuting the cases.

**Nevada Fraudster Pleads Guilty To Role In Scheme To File False Tax Returns Using Stolen Identities**

**Had More Than 200 Stolen Identities in His Backpack**

A Las Vegas resident pleaded guilty today to aggravated identity theft, wire fraud, theft of government property, and access device fraud, relating to a stolen identity tax fraud, announced Principal Deputy Assistant Attorney General Richard E. Zuckerman of the Justice Department’s Tax Division and U.S. Attorney Nicholas A. Trutanich for the District of Nevada.

According to court documents and statements made in court, Josiah Ntekume was involved in a scheme to file false tax returns using stolen identities in order to obtain tax refunds. Coconspirators provided Ntekume with names, addresses, dates of birth, and social security numbers, and Ntekume used these stolen identities to establish prepaid debit card accounts. The coconspirators then caused fraudulently obtained federal tax refunds to be deposited into those accounts.

When Ntekume was arrested on March 13, 2012, he had in his backpack approximately 250 prepaid debit cards in others’ names on which more than more than $200,000 in fraudulent tax refunds had been loaded. The backpack also contained several pages of paper listing stolen identities for nearly 200 individuals that were used either to file false tax returns or to establish additional prepaid debit cards.

Sentencing is scheduled for March 4, 2020. At sentencing, Ntekume faces a statutory maximum sentence of up to 20 years in prison on the wire fraud count, as well as up to ten years in prison on each count of theft of government property and fraud in connection with access devices. He also faces a mandatory minimum of two years for aggravated identity theft. In addition to a prison sentence, Ntekume faces a period of supervised release, restitution, and monetary penalties.

**North Carolina Tax Return Preparer Sentenced to Prison for Tax Fraud**

A Raleigh, North Carolina, man was sentenced to 45 months in prison today for conspiring to defraud the United States, announced Principal Deputy Assistant Attorney General Richard E. Zuckerman of the Justice Department’s Tax Division and U.S. Attorney for the Eastern District of North Carolina, Robert J. Higdon Jr.

According to court documents and statements made in court, from 2011 through 2014, Garvey Imhotep conspired with others to file false tax returns for clients of several tax return preparation businesses, including Tax Kings, Two Brothers Tax Service, and Taxes Done Right. Imhotep and his co-conspirators filed returns claiming false education expenses and other fraudulent items in order to increase clients’ tax refunds. To conceal his involvement and evade Internal Revenue Service (IRS) detection, Imhotep used tax preparer identification numbers that are assigned to other individuals. Imhotep’s conduct caused a tax loss of more than $1.5 million to the United States.

In addition to the prison term, U.S. District Judge James C. Dever III, ordered Imhotep to serve three years of supervised release and to pay $2,144,888 in restitution to the IRS.

Principal Deputy Assistant Attorney General Zuckerman and U.S. Attorney Higdon commended special agents of IRS-Criminal Investigation, who investigated the case, and Assistant United States Attorney Ethan Ontjes and Trial Attorney Lauren Castaldi of the Tax Division, who are prosecuting this case.

**News From The Justice Departments Tax Division**

The Justice Department announced that it has filed a complaint with a U.S. District Court in Norfolk, Virginia, seeking entry of a court order requiring Franchise Group Intermediate L 1 LLC, (Liberty) the national franchisor and owner of Liberty Tax Service stores, to refrain from specific acts, enact enhanced internal compliance controls regarding the detection of false tax returns, and pay for an independent monitor to oversee Libertys compliance with the proposed court order.

Separately, the United States and Liberty filed a joint motion and proposed order that, if adopted by the court, would resolve the matter.

**Tax Accountant Sentenced To 42 Months For Scamming Clients In Fraud And Money Laundering Scheme**

Geoffrey S. Berman, the United States Attorney for the Southern District of New York, announced that Salvatore Arena was sentenced on December 13 to 42 months in prison for defrauding clients who trusted him to prepare and pay their taxes. Arena misappropriated over $780,000 of client money from approximately 170 victims for his own use. Arena pled guilty on August 23, 2019, before United States District Judge Katherine Polk Failla, who imposed Friday’s sentence.

U.S. Attorney Geoffrey S. Berman said: “Salvatore Arena misappropriated money his clients intended would be used to pay their taxes. He defrauded his clients and the United States, and now he has been sentenced to prison for his crimes.”

According to allegations in the criminal complaint, the information, and other documents filed in federal court, as well as statements made in public court proceedings:

During the relevant time period, Arena purported to offer tax services,
including the preparation and payment of taxes, to clients of an accounting firm in Manhattan. Instead of making payments on behalf of those clients, as Arena represented, he diverted client funds for his own use. Arena executed this fraudulent scheme in two primary ways – first, by diverting pre-payments of taxes to his own tax account and later claiming illegitimate refunds; and second, by misappropriating tax payments clients had wired into a bank account controlled by Arena.

Arena defrauded approximately 170 victims during the period from January 2014 through March 2019, and agreed as part of his guilty plea to forfeit $789,195.35 in United States currency, representing proceeds traceable to the charged offenses, and was ordered by the Court to pay restitution of at least $726,608.42.

Arena, 46, of Queens, New York, was sentenced to concurrent terms of 42 months in prison for mail fraud, money laundering, and wire fraud. In addition to the prison term, ARENA was also sentenced to three years of supervised release.

Mr. Berman praised the outstanding investigative work of Special Agents from TIGTA, Criminal Investigators from the NYSDTF, and Special Agents from the U.S. Attorney's Office for the Southern District of New York.

The prosecution of this case is being handled by the Office's General Crimes Unit. Assistant United States Attorney Jarrod L. Schaeffer is in charge of the prosecution.

South Carolina Return Preparer Charged With 8 Counts

A tax preparer is accused of helping create false tax returns over a two-year period.

The S.C. Department of Revenue (SCDOR) said in a statement that agents arrested Annmedra Cornelia Brown, 41, of Spartanburg.

Brown is accused of assisting in the preparation of several false tax returns between 2015 and 2017.

According to SCDOR, Brown is charged with eight counts of willfully assisting in the preparation of a false return.

Brown allegedly reported “false deductions and losses of more than $304,000” in eight tax returns for four clients.

She faces up to 40 years in prison and $80,000 in fines if convicted of all charges, according to SCDOR.

Brown was arrested by SCDOR agents.

Brown was in the Spartanburg County jail awaiting a bond hearing as of Wednesday morning.

"While the majority of certified tax preparers are honest and trustworthy, there are those who seek to take advantage of unsuspecting clients," SCDOR said in a statement.

A Former IRS Employee Was Sentenced To Nearly Three Years In Prison For Tax Evasion—Even IRS Employees Aren't Above The Law

A recent Newsweek article reported that a former IRS employee had been sentenced to nearly three years in prison for refusing to settle back taxes. The former Utah IRS employee reportedly "made a career of committing tax fraud," according to federal prosecutors, and amassed more than $500,000 in back taxes between the years of 1993 and 2006. The former employee, who was also an attorney, apparently made "frivolous" bankruptcy claims and inaccurately reported his assets to prevent the IRS from collection his tax payments.

"This example of an IRS employee going to prison for tax evasion should be a clear demonstration to taxpayers that no one who fails to pay taxes year after year will get away with it," said Sherri Gastelum, CEO of Platinum Tax Defenders. "When taxpayers fail to settle their back taxes, they risk wage garnishment, high fees, and interest, or worse, prison. Those looking to file back taxes—no matter how high or low they are—should contact Platinum Tax Defenders immediately.''

Because the Utah IRS employee did not settle his back taxes, the former Utah IRS employee has been ordered to pay nearly $1 million in restitution, which includes penalties and interest charges on his missed tax payments. According to the Newsweek article, the former IRS employee is planning to file an appeal.

The Newsweek report also states that in one instance, the former Utah IRS employee filed a false income tax return in 2009, which claimed a deduction worth more than $400,000 based on an abandoned investment in a Ponzi scheme involving Utah company VesCor. However, the former IRS employee was proved never to have been an investor in the project from which he claimed to lose money.

Ragin Cagin

Tax Professional's Need to Buckle Their Seatbelts - It Will Be A Bumpy Ride

Just off the road for the holidays and then off to New Jersey and finally Baton Rouge (so close to Zachary I can smell my wife's gumbo) with the 1040 Fall Update.

I have had a great time seeing you and sharing all ncpe knew about the Taxpayer First Act and some proposed legislation. Then a couple of weeks ago, Washington finally woke up - of the legislation that had been proposed both houses of Congress passed and the President signed into law the SECURE Act which will change retirement plans and planning.

Additionally, Congress gave some relief to military families which was badly needed.
But the BIG ONE, is the EXTENDER PACKAGE!

Tax Professionals waited throughout the 2018 filing season for an act to extend the Extenders which expired on 12/31/2017. We extended 2018 tax returns, not wanting to file and later amend. We finally got down to the October 15th deadline for timely filing and filed the returns.

As part of the Budget Act, allowing the government to stay open, the President signed on December 20, 2019 provisions that allow certain Extenders to be considered in 2018, retroactively, and through December 31, 2020. They include:

1. Deduction for mortgage insurance premiums as qualified residence interest
2. Deduction for tuition and related expenses
3. Nonbusiness Energy Property Credit, including insulation, storm doors and windows, etc
4. Income exclusion from debt cancellation that is acquisition indebtedness on the taxpayer's principal residence of up to $2M
5. Depreciable life of certain race horses as 3-year property
6. Depreciable life for motor sports entertainment complexes of 7-year property
7. Accelerated depreciation for business property on Indian Reservations
8. Energy Efficient Homes Credit for Builders
9. Qualified Fuel Cell Motor Vehicles Credit
10. Alternative Fuel Refueling Property Credit
11. 2-Wheeled Plug-in Electric Vehicle Credit
12. Black-Lung Disability Trust Fund Excise Tax
13. Indian Employment Credit
14. Railroad Track Maintenance Credit
15. Mine Rescue Team Training
16. Expensing for certain productions under IRC 181(g)
17. Various incentives for Empowerment Zone Activities
18. Economic Development Credit for American Samoa
20. Second Generation Biofuel Producer Credit
21. Electricity Produced from Certain Renewable Resources Credit
22. Indian Coal Facilities Credit
24. Energy Efficient Commercial Buildings Deduction
25. Special Rule for Sales or Dispositions to Implement Ferc or State Electric Restructuring Policy for Qualified Electric Utilities
26. Extension and Clarification of Excise Tax Credits relating to alternative fuels
27. Oil Spill Liability Trust Fund Rate

For deductible Medical Expenses, the 10% rate increase in 2019 will remain at 7.5% as an exclusion. The 7.5% rate was used on the 2018 return.

The following were scheduled to expire at the end of 2019, however they have now been extended through 2020. They include:

1. New Markets Credit
2. Employer Credit for Paid Family & Medical Leave
3. Work Opportunity Credit
5. Look-thru Rule for Related Controlled Foreign Corporations
6. Credit for Health Insurance Costs of Eligible Individuals

What an opportunity! Tax professionals, heads up for this outstanding Amendment Opportunity for 2018 tax returns, but don't take it on the chin, charge appropriately for your service. Make certain your taxpayers know you did not make an error on their 2018 tax return - this was caused by Congressional delay, and in fact, what an excellent reason for amending a return "due to Congressional delay in passing the Extender provisions."

I do regret that no Technical Corrections Act addressed the writing error in the Tax Cuts and Jobs Act on depreciation.

Until next time,

Jerry

Taxpayer Advocacy

IRS Provides New Guidance On Processing Certain FOIA Requests

In an internal memorandum, the IRS has provided interim guidance on processing Freedom of Information Act (FOIA) requests for access to tax records protected by Code Sec. 6103 that are not accompanied by the proper authorization.

Background—confidentiality. Generally, Code Sec. 6103(a) provides that returns and return information are confidential and cannot be disclosed by IRS officers or employees.

A “return” is any tax or information return (including amended returns) and all supporting schedules and attachments to such returns, or claim for refund, filed with the IRS. (Code Sec. 6103(b)(1))

Generally, “return information” is any information prepared by, furnished to, or collected by, the IRS with respect to a return or the determination of the existence of a liability of any taxpayer. (Code Sec. 6103(b)(2))

Background—FOIA. FOIA allows members of the public to access records from any federal agency. Federal agencies are required to disclose information requested under FOIA unless the information falls under one of nine exemptions, which protect interests such as personal privacy, national security and law enforcement. FOIA places the burden on the agency to establish that requested records are exempt from disclosure. (5 USC §552)

Background—IRS regs regarding FOIA requests. The IRS has published regs that provide the rules for making a FOIA request for IRS records. (Reg §601.702) Under these regs, a person requesting records protected under Code Sec. 6103 must establish their identity and their right to obtain the protected records. (Reg §601.702(c)(4)(i)(E)).

Generally, a person requesting records protected by Code Sec. 6103 on behalf of, or pertaining to, another person needs to furnish a properly executed power of attorney (Form 2848, Power of Attorney and Declaration of Representative) or Form 8821, Tax Information Authorization. (Reg §601.702(c)(5)(iii)(C))

Procedural change. The IRS has changed its procedures for processing FOIA requests for access to tax records protected by
The FATCA international tax code was designed to stop Americans stashing money abroad to evade tax. It forces banks worldwide to start revealing, via national tax agencies, information on clients with links to America. And it spawned the Common Reporting Standard, whereby over 100 countries swap data with each other to discourage cross-border tax dodging.

Unlike most countries, the United States levies income taxes based on citizenship rather than residency. Accidental Americans have US citizenship because they were born in the country but don’t identify with that nationality because they have mainly lived abroad.

But many Americans living overseas have found it has also caused problems for them. Banks have warned that they could be forced to close accounts belonging to US citizens because of ongoing difficulties with FATCA.

The majority of active foreign-based enrolled agents reside in India, the UK, Canada, China, South Korea and Japan, according to the data. In total their numbers - which include US and non-US citizens - have surged from 2,078 in 2016 to 3,083 as of late September 2019.

Tax authorities around the world are warning expats to own up to offshore tax avoidance as a new international data sharing network is switched on to full capacity.

Treasury, IRS Issue Final Regulations On The Foreign Tax Credit

The Internal Revenue Service issued final regulations today on the Foreign Tax Credit, a long-standing tax benefit that generally allows individuals and businesses to claim a credit for income taxes paid or accrued to foreign governments.

The Tax Cuts and Jobs Act (TCJA) made major changes to the tax law, including revamping the U.S. international tax system. Specifically, several Foreign Tax Credit provisions were changed, including repeal of section 902, which allowed deemed-paid credits in connection with dividend distributions based on foreign subsidiaries’ cumulative pools of earnings and foreign taxes. TCJA also added two separate limitation categories for foreign branch income and amounts includible under the Global Intangible Low-Taxed Income (GILTI) provisions.

Additionally, the TCJA changed how taxable income is calculated for purposes of the Foreign Tax Credit limitation by disregarding certain expenses and repealing the use of the fair market value method for...
allocating interest expense.

Finally, the TCJA made systemic changes to U.S. taxation of international income that impact the Foreign Tax Credit calculation. These systemic changes include the introduction of a participation exemption through a dividends received deduction for certain dividends in section 245A and the introduction of GILTI, which subjects to current U.S. taxation foreign earnings that would have been deferred under previous law, albeit at a lower tax rate and subject to extra Foreign Tax Credit restrictions.

The IRS also issued Proposed Regulations relating to the allocation and apportionment of deductions and creditable foreign taxes, foreign tax redeterminations, availability of Foreign Tax Credits under the Transition Tax, and the application of the Foreign Tax Credit limitation to consolidated groups.

**IRS Again Delays Applicability Date Of Final Foreign Currency Regulations**


In a Notice, the IRS has announced that it will again delay the applicability date of final foreign currency regs under Code Sec. 987, as well as certain related final and temporary regs, by one additional year.

In December 2016, the IRS issued final regs under Code Sec. 987 (TD 9794) that provided rules for: (1) translating income from branch operations conducted in a currency different from the branch owner’s functional currency into the owner’s functional currency; (2) calculating foreign currency gain or loss with respect to the branch’s financial assets and liabilities; and (3) recognizing such foreign currency gain or loss when the branch makes a transfer of any property to its owner. (2016 final regs). For more details, see "Final regs explain income and currency gain or loss for Code Sec. 987 qualified business unit" (12/15/2016).

At the same time, the IRS issued temporary regs under Code Sec. 987 (TD 9795) that provided rules for dealing with combinations and separations of Code Sec. 987 qualified business units (section 987 QBUs) and the recognition and deferral of foreign currency gain or loss under Code Sec. 987 in connection with certain QBU terminations and certain other transactions, among other rules (2016 temporary regs). The IRS also concurrently published proposed regs (2016 proposed regs) by cross-reference to the temporary regs (Preamble to Prop Reg REG-128276-12). For more details, see "Temp foreign currency regs cover gain or loss for terminated qualified business units" (12/15/2016).

In April 2017, President Trump issued Executive Order (EO) 13789, which instructed the IRS to review all “significant tax regulations” issued on or after January 1, 2016, and identify those that (1) imposed an undue financial burden on U.S. taxpayers; (2) added undue complexity to the Federal tax laws; or (3) exceeded the IRS’s statutory authority.

In Notice 2017-38, 2017-30 IRB 147, the IRS identified, among others, the 2016 regs under Code Sec. 987 as qualifying for review under the EO. See "Eight significant tax regs listed on the chopping block under executive order" (07/13/2017).

In Notice 2017-57, 2017-42 IRB 324, the IRS announced it would delay the applicability date of the 2016 final regs and certain of the 2016 temporary regs under Code Sec. 987 by one year. See "IRS pushes back effective date of foreign currency regs while considering further changes" (10/05/2017).

In Notice 2018-57, 2018-26 IRB 774, the IRS announced it would again delay the applicability date of the 2016 final regs and certain of the 2016 temporary regs under Code Sec. 987 by one year. According to the delay announced in Notice 2018-57, the 2016 final regs would apply to tax years beginning on or after the first day of the first tax year following December 7, 2019. See "IRS again pushes back effective date of foreign currency regs." (06/14/18)

In May 2019, the IRS finalized some of the 2016 temporary regs (TD 9857) dealing with combinations and separations of section 987 QBUs and the recognition and deferral of foreign currency gain or loss under Code Sec. 987 in connection with certain QBU terminations and certain other transactions (2019 final regs). The rest of the temporary regs are outstanding. For more details see "IRS issues final regs on recognition and deferral of foreign currency gain or loss." (05/13/2019)

IRS again amends applicability date. The IRS intends to amend Reg §1.985-5, Reg §1.987-11, Reg §1.988-1, Reg §1.988-4, and Reg §1.989(a)-1 of the 2016 final regs and Reg §1.987-2 and Reg §1.987-4 of the 2019 final reg to apply to tax years beginning on or after the first day of the first tax year following December 7, 2020 (the amended applicability date).

According to the Notice, following the amendments, for a taxpayer whose first tax year after December 7, 2020, begins on January 1, 2021, the 2016 final regs and Reg §1.987-2(c)(9), Reg §1.987-4(c) (2), and Reg §1.987-4(f) of the 2019 final regs would apply for the tax year beginning on January 1, 2021.

Taxpayers may rely on Notice 2019-65 regarding these proposed amendments pending issuance amended regs. (Notice 2019-65, Sec. 4)

**State News of Note**

**FAQ: Answers To Your Questions On Utah’s New Tax Law**

1. How will the new tax law affect me personally?

It’s difficult to say without knowing your specific income or household size. But we can tell you that about 85 percent of Utahns will pay less under our new tax system than they paid under the old one. Factoring in adjustments to sales tax and gas tax, we have cut taxes by over $160 million for this coming fiscal year.

In fact, that number includes taxes paid by tourists and others moving through our state. Utahns will experience over $200 million in tax cuts this coming year.

Much of that net tax cut is targeted directly to low- and middle-income Utahns.

You can also view legislative projections to get a better sense of how the new law will impact you.
2. Will this tax bill hurt the poor?

Absolutely not.

This bill does increase the existing state sales tax rate on food from 1.75 percent to the standard state sales tax rate, which is a 4.85 percent state rate. This does not include local government taxes imposed on food.

Food provided by SNAP, WIC, and charitable organizations like food pantries is not subject to sales tax, and that does not change under this new law.

The standard tax rate on food is expected to bring in $250 million in taxes for the state. We were concerned that adjusting this tax would impact low- and middle-income individuals and families, so we built in tax credits going directly to those who otherwise could have felt burdened by adjustments to the grocery tax.

Specifically, we built in a $135 million grocery tax credit to offset the burden of this tax on low- and middle-income families. This tax credit is expected to more than cover the amount these families will spend on increased food taxes.

The Governor’s Office and the Governor’s Office of Management and Budget worked with the legislature to add in a $6 million earned income tax credit targeted specifically to benefit working families experiencing intergenerational poverty. The bill also includes Social Security tax credits for seniors. Additionally, S.B. 2001 increases the Utah dependent exemption amount from $565 to $2,500. In addition to dependents, joint filers with no dependent children can now receive one exemption.

The new system will collect money in new and different ways, but it will not collect more tax revenue or increase the tax burden on Utahns.

It’s worth noting that under every projection we have run, lower- and middle-income individuals are better off under the new tax system than they were under the old one.

If you have further questions about why adjusting the food tax was necessary, see question #8.

3. Who qualifies for the new earned income tax credit, and how do you apply for it?

Utah’s new earned income tax credit for families in intergenerational poverty is designed to function in tandem with the federal earned income tax credit. In fact, Utah’s EITC is calculated off the amount provided in the federal earned income tax credit, and provides 10 percent of that total amount to qualifying individuals and families.

For example, a single mother earning $20,000 a year, in intergenerational poverty, with two children at home, would qualify for a federal earned income tax credit of a little over $5,600. Thanks to the creation of Utah’s new EITC, she could also receive an additional $560 from the state.

As the saying goes, we should not only give a fish to those in need, we should also help them learn how to fish. Providing this benefit only to those who have earned wage income helps incentivize and reward work efforts, which are essential in helping lift individuals and families out of poverty. This money will make a real difference in helping break the cycle of generation-to-generation poverty.

The Utah Department of Workforce Services will assess eligibility for the Utah EITC. Families who have experienced poverty for more than one generation are encouraged to contact their office to determine whether or not they will be eligible for Utah’s EITC. Approximately 25,000 Utahns in intergenerational poverty are expected to qualify.

The federal tax credit is targeted to low- and middle-income households, so it gradually phases out as income increases, fully phasing out at a little over $50,000 per year for single filers with three or more children, and $56,000 for a married couple with three or more children. Smaller households will phase out at lower income levels. Utah’s EITC is based off of these numbers, but it is worth noting that the federal EITC does not have an intergenerational poverty requirement.

It’s pretty simple to apply for both the federal and state EITCs when filing your federal and state tax returns. You can find the link to apply for an earned income tax credit here. If you make too little to pay taxes and do not currently file a tax return, contact the Department of Workforce Services, which can help you through the filing process.

We encourage anyone who thinks they might qualify for this tax credit to contact the Department of Workforce Services, which will determine eligibility for the credit. They can also assist applicants in filing their federal and state tax returns.

4. How do I know if I am eligible for the grocery tax credit? How much will it be? How do I apply?

The grocery tax credit fully phases out at 175 percent of the federal poverty level, so your eligibility will be determined by factoring your income in relation with your household size. For example, a family of four with an income of $45,000 will receive a full, unadjusted grocery tax credit of $500. If that same family’s income were to rise much above $45,000, the credit would begin to phase-out. Larger families may continue to receive a portion of the credit even if they are making up to $81,300 a year.

The grocery tax credit amounts to $125 a year, per person in a family of four, with an additional $50 dollars per additional child.

If you currently file a tax return, you don’t have to take any extra steps to receive the benefit of the grocery tax credit. If you make too little to pay taxes and do not currently file a tax return, contact the Department of Workforce Services, which can help you through the filing process.

5. The claim is that there is an issue with collecting revenue. How can that be when Utah had a billion dollars in new revenue last year?

The issue isn’t how much we’re collecting, but how we’re collecting it. Utah is the only state in the nation that reserves all revenue gathered through income tax for education spending. That means all other state funding has to come through the general fund, which is supported by sales tax.

In 1960, goods accounted for about 53 percent of consumer spending in Utah. Today, in our ever-changing economy, they make up 31 percent of consumer spending, with nearly 70 percent going to largely untaxed services. It’s not fair or moral to make a shrinking segment of our economy shoulder an increasingly larger burden. The new system begins the work of fixing this by broadening the sales tax to a variety of services that were exempted.

Our economy is thriving, and year after year, income tax revenues increase significantly. But the general fund, while increasing, is not
Solid tax policy relies on taxing places where everyone pays, in good times and in hard times. Returning to collecting a 4.85 percent state tax on groceries will bring in essential funds to our slow-growing general fund, which is supported by sales tax. This fund pays for core government services, and the grocery tax will generate approximately $250 million for the state. It bears repeating that stabilizing the general fund and diversifying our system have remained the main goals of tax reform.

This is a very stable revenue source. By collecting less in income tax from Utahns, but a little more in sales tax on food, we take a big step toward stabilizing revenue gathered from taxes year-to-year.

8. Why was it necessary to increase the sales tax on food to 4.85 percent?

Strengthening the general fund is a long-term step toward creating a more stable system to support our state and its citizens in the future.

It may help to think of the state’s tax structure like a retirement savings portfolio that needs to be balanced to ensure both growth and stability over the long-term.

6. Will I be part of the “15%” of Utahns that will see an increase in their taxes?

It’s hard to say without knowing the specifics of your income and household size, but you can take a look at some of the legislative projections yourself by clicking below.

7. You claim this is a tax cut for Utahns. How can you justify that when you are cutting education funding? And how can you justify cutting education spending when we rank last in the nation in per pupil spending?

This is a tax cut for Utahns. Even with adjusting for added sales and gas taxes, Utahns will see over $200 million in net tax cuts in this coming fiscal year because a portion of the sales tax increases are shifted to tourists and other nonresidents.

We can afford to give this tax cut, and continue increasing education funding by the same amount we have each year for the last four years. In the last four years, we’ve given $1 billion of new ongoing money to education — that’s $250 million of new ongoing money per year. (In fact, we’ve put $2 billion of new ongoing money toward education over the course of the last decade.) The governor remains committed to dedicating at least that same increase amount — $250 million of new ongoing money — to education in his upcoming budget recommendations.

Moreover, what is good for the general fund isn’t just good for government services. It’s also good for education.

Income tax is a historically unstable revenue source, and it drops dramatically during an economic downturn. This puts education funding at risk. For example, during the recession of 2008, when income tax revenues dropped by over 20 percent, we had to dip into the general fund to make up the difference. Back then, the general fund contained enough money to supplement losses in the education fund, but with our current imbalance, this would no longer be possible.

Strengthening the general fund is a long-term step toward creating a more robust and equitable foundation for education funding.

Not only is there not a cut to education funding, but the steps we are taking this year will provide for increased education funding into the future; general fund dollars spend just as well as income tax dollars. It’s also worth noting that while we’re dedicated to providing more funding to education, spending more is not the end goal — improving outcomes for our students is the goal. By that standard, Utah is doing quite well. For example, we have some of the highest ACT and AP scores in the nation and our graduation rates continue to rise steadily.

8. Why was it necessary to increase the sales tax on food to 4.85 percent?

Solid tax policy relies on taxing places where everyone pays, in good times and in hard times. Returning to collecting a 4.85 percent state tax on groceries will bring in essential funds to our slow-growing general fund, which is supported by sales tax. This fund pays for core government services, and the grocery tax will generate approximately $250 million for the state. It bears repeating that stabilizing the general fund and diversifying our system have remained the main goals of tax reform.

This is a very stable revenue source. By collecting less in income tax from Utahns, but a little more in sales tax on food, we take a big step toward stabilizing revenue gathered from taxes year-to-year.

9. Why did you choose to call a special session now with the regular legislative session right around the corner? What couldn’t wait another six weeks?

Early in the legislative session, budget analysts and legislators undertake the arduous and necessary task of setting base budgets for government for the year. It’s a complex process that is dependent on accurate projections. Passing the bill ahead of the session was vital to getting legislators and economists reliable projections they can use to set those budgets.

The general session will also give us the opportunity to make any tweaks for technical issues in the bill that need to be addressed.

10. I thought you had said you would not call a special session unless there was consensus? Everyone I have spoken with is against the bill that just passed.

When the governor calls a special session, he relies on consensus from the legislature in determining whether or not to make a call. Specifically, he waits for legislative leadership to express that they have reached accord on an issue.

The governor determined that it was necessary to pass the tax bill in a special session so that legislators and economists would have more reliable projections to set budgets for the coming fiscal year. Tax changes come with anxiety, but the governor is hopeful that that anxiety will subside as Utahns experience the lightened burden of our tax system in 2020.

Massachusetts Income Tax Drops To 5% Flat Rate — 20 Years After Passage

By Mary Markos, Boston Herald

After two decades of waiting, Massachusetts residents are finally getting the flat 5 percent income tax rate they voted for — but some advocates who pushed for the reduction didn’t live to see their work come to fruition.

“There are a lot of taxpayers who worked on that campaign who never saw the income tax reach 5 percent, as the voters mandated 20 years ago,” Director of the Citizens for Limited Taxation Chip Ford said. “Finally, it’s going to go back to 5 percent as promised. I’d say too little, too late, but that’s what you get from state government.”

The individual income tax rate will be reduced from 5.05 percent to 5 percent effective Jan. 1, the Baker Administration announced Friday. Voters approved a slash in the tax rate from 5.9 percent to 5 percent in 2000, but the Legislature decided to reduce the rate gradually based on certain economic triggers.

Ford and Barbara Anderson, a longtime anti-tax activist, cultivated an effort to get the question on the ballot through their nonprofit about 30 years ago. He lamented that Anderson, his partner of 20...
Wayne's World

The Affordable Care Act In 2019

The ACA has been altered substantially since President Barack Obama first signed it into law in March 2010.

A most significant change came in 2019 with regard to the associated tax penalty for not maintaining insurance coverage.

Subsidy eligibility remains the same.

Additionally, changes to previous rules now allow short-term plans to compete with ACA-approved coverage.

Taxpayers are still obligated to carry health insurance, either through their employers, through the ACA Exchange, or by independently selecting and paying for their own ACA-compliant plans. But they no longer have to pay a financial penalty if they don’t beginning in 2019, due to changes made by the 2018’s Tax Cuts and Jobs Act (TCJA). This change went into effect on Jan. 1, 2019, so 2019 tax filings will be the first year taxpayers without health insurance will not face a penalty for not having coverage...

At least a portion of taxpayers were expected to stop paying for insurance in 2019 because they were only doing so to avoid the tax penalty. Others might change over to the short-term limited duration health plans that can now expand to compete with ACA coverage.

Approximately 4 million taxpayers were assessed the individual mandate penalty in 2016 alone however ACA Exchange insurers made adjustments to compensate for the expected lost revenue.

Taxpayers still had to cough up the penalty when they filed their 2018 tax returns in 2019 because it was applicable in the 2018 tax year.

Individuals will still have to pay penalties for not carrying insurance, at least at the state level. New Jersey, the District of Columbia, and Massachusetts continue to impose penalties for not maintaining insurance.

Vermont intends to add to the list of states requiring insurance in 2020 as the result of legislation passed in 2018. Lawmakers in Rhode Island voted to adopt a similar provision in July 2019, also effective Jan. 1, 2020.

The ACA Healthcare Exchange continues to offer a variety of healthcare plans to those who want to purchase them. Things remain largely unchanged in this respect in 2019.

Bronze, Silver, Gold, and Platinum plans are still offered at varying cost and coverage levels.

The second-lowest-cost Silver plan remains the only one that provides adjusted premiums for low-income taxpayers. Bronze plans offer the least coverage, but they also provide more in the way of cost-sharing of deductibles and co-pays. Platinum plans offer the most comprehensive coverage.

Monthly premiums for the second lowest cost Silver plan, considered the "benchmark" plan, are more or less holding steady in 2019, according to the Kaiser Family Foundation (KFF), although some states have experienced spikes while others have seen some decreases.

A sharp increase occurred in 2018, even as subsidized enrollees increased to 9.2 million from 8.7 million in 2018. But the number of unsubsidized enrollees correspondingly dropped.

The states where premiums are expected to increase most dramatically through the end of 2019 include:

- North Dakota: 30%
- Vermont: 23%
- District of Columbia: 21%
- Delaware: 16%
- New York: 15%
- Colorado: 13%
- Washington State: 12%
- West Virginia: 11%
- Hawaii: 10%

States where premiums are anticipated to decrease the most significantly by the end of 2019 include:

- Pennsylvania: -27%
- North Carolina: -20%
- Arizona: -17%
- Tennessee: -17%
- New Hampshire: -15%
- New Jersey: -15%
- New Mexico: -15%
- Connecticut: -12%

These changes are based on premium rates in these states’ most major cities.

The remaining 25 states not listed here are expected to experience increases or decreases of less than 10%.

The premium tax credit remains the mechanism by which the ACA attempts to make health coverage affordable for low- and moderate-income Americans.

The credit is refundable, which means that it can be paid directly to taxpayers or the money can go to their insurers, reducing premiums in the upcoming year.

The amount of the credit depends on a taxpayer’s income, and it is not available for those who qualify for Medicaid or the Children’s Health Insurance Program (CHIP), those who are eligible for Medicare Part
A, or those who have employer-sponsored coverage available that's considered to be affordable.

These terms all remain the same, but the income guidelines shift ever so slightly from year to year based on changes in the federal poverty level.

According to the Kaiser Family Foundation, the 400% level in 2019 means incomes of no higher than:

- $48,560 for single taxpayers
- $65,840 for a family of two
- $83,120 for a family of three
- $100,400 for a family of four
- $117,680 for a family of five
- $134,960 for a family of six
- $134,960 plus $17,280 for each additional family member over six

The credit is based on a specifically calculated version of modified adjusted gross income (MAGI). The taxpayers modified adjusted gross income must fall between 100% and 400% of the federal poverty level for eligibility, or 139% if you live in a state that expanded its Medicaid program subsequent to the passage of the ACA.

Depending on your modified adjusted gross income, a taxpayer is expected to financially contribute a portion of your premiums, and the taxpayer receives a subsidy tax credit to cover the remaining cost of health insurance.

Individuals with modified adjusted gross income between 300% to 400% of the federal poverty level are expected to contribute 9.86% of their premiums in 2019. Those earning 133% or less must contribute 2.08%.

If the taxpayers modified adjusted gross income is more than anticipated when the tax return for the year is prepared, the taxpayer must pay back the overage on the tax return at tax time. The premium tax credit might be increased based upon a lesser modified adjusted gross income and will be otherwise refundable unless the taxpayer owes federal income tax.

Years of lobbying and other efforts by companies and other health care payers, aimed at repealing the Affordable Care Act’s excise tax on high-value health plans, appear to have finally achieved their mission.

Leaders of both houses of Congress, who worked with the White House to finalize the fiscal 2020 federal government spending bill before the Dec. 20 extended deadline, reached agreement to repeal the so-called “Cadillac tax.”

Companies will no longer be subject to a 40% tax on the value of health care benefits above certain thresholds. The tax was currently scheduled to take effect in 2022. The way the ACA excise tax provision was written, it was expected that most or all companies would have become subject to it within no more than a few years.

The federal funding bill also would repeal two other ACA taxes. One, a 2.3% excise tax on medical devices, assessed against device manufacturers, originally took effect in 2013. It was suspended for 2016 and 2017 following stiff resistance from the device industry and again became effective last year.

The other tax expected to be repealed by Friday, assessed against insurers providing individual and fully insured group health plans, is currently slated to take effect in 2020. Here too, it’s been widely expected that employers and individuals would have ultimately taken the cost hit in the form of higher premiums.

So just when you thought it "safe" to go back into tax preparation with no ACA penalty for not having health insurance, remember to ask your taxpayers, "did you buy your health insurance from the exchange"? If so, remember to reconcile the amount of the advanced premium with the modified adjusted gross income of your taxpayer.

The ACA lives on and does it relate to the tax return we prepare - "depends"!

Wayne

Letters to the Editor

Hi, Beanna

Just wanted to say that VeriFyle is great. I’m switching from my CCH firm account the first of the year after several months testing. The latest upgrade makes it even better and fixes the few shortcomings it had before.

Thank you and the Fellowship for providing this service.

Earl Wooten

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Dear Beanna

Thank you for the guidance that you provided on the basis issue that I asked about last week.

As a sole practitioner, having NCPE and the NCPE Fellowship as resources is so beneficial to my practice. I have been attending NCPE seminars for well over 20 years and no other organizations providing income tax classes come close.

Jeff

Tax History

Historical Highlights of the IRS

1862 - President Lincoln signed into law a revenue-raising measure to help pay for Civil War expenses. The measure created a Commissioner of Internal Revenue and the nation’s first income tax. It levied a 3 percent tax on incomes between $600 and $10,000 and a 5 percent tax on incomes of more than $10,000.

1867 - Heeding public opposition to the income tax, Congress cut the tax rate. From 1868 until 1913, 90 percent of all revenue came from taxes on liquor, beer, wine and tobacco.

1872 - Income tax repealed.

1894 - The Wilson Tariff Act revived the income tax and an income tax division within the Bureau of Internal Revenue was created.
1895 - Supreme Court ruled the new income tax unconstitutional on the grounds that it was a direct tax and not apportioned among the states on the basis of population. The income tax division was disbanded.

1909 - President Taft recommended Congress propose a constitutional amendment that would give the government the power to tax incomes without apportioning the burden among the states in line with population. Congress also levied a 1 percent tax on net corporate incomes of more than $5,000.

1913 - As the threat of war loomed, Wyoming became the 36th and last state needed to ratify the 16th Amendment. The amendment stated, "Congress shall have the power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration." Later, Congress adopted a 1 percent tax on net personal income of more than $3,000 with a surtax of 6 percent on incomes of more than $500,000. It also repealed the 1909 corporate income tax. The first Form 1040 was introduced.

1918 - The Revenue Act of 1918 raised even greater sums for the World War I effort. It codified all existing tax laws and imposed a progressive income-tax rate structure of up to 77 percent.

1919 - The states ratified the 18th Amendment, barring the manufacture, sale or transport of intoxicating beverages. Congress passed the Volstead Act, which gave the Commissioner of Internal Revenue the primary responsibility for enforcement of Prohibition. Eleven years later, the Department of Justice assumed primary prohibition enforcement duties.

1931 - The IRS Intelligence Unit used an undercover agent to gather evidence against gangster Al Capone. Capone was convicted of tax evasion and sentenced to 11 years.

1932 - Prohibition repealed. IRS again assumed responsibility for alcohol taxation the following year and for administering the National Firearms Act. Later, tobacco tax enforcement was added.

1942 - The Revenue Act of 1942, hailed by President Roosevelt as "the greatest tax bill in American history," passed Congress. It increased taxes and the number of Americans subject to the income tax. It also created deductions for medical and investment expenses.

1943 - Congress passed the Current Tax Payment Act, which required employers to withhold taxes from employees' wages and remit them quarterly.

1944 - Congress passed the Individual Income Tax Act, which created the standard deductions on Form 1040.

1952 - President Truman proposed his Reorganization Plan No. 1, which replaced the patronage system at the IRS with a career civil service system. It also decentralized service to taxpayers and sought to restore public confidence in the agency.

1953 - President Eisenhower endorsed Truman's reorganization plan and changed the name of the agency from the Bureau of Internal Revenue to the Internal Revenue Service.

1954 - The filing deadline for individual tax returns changed from March 15 to April 15.

1961 - The Computer Age began at IRS with the dedication of the National Computer Center at Martinsburg, W.Va.

1965 - IRS instituted its first toll-free telephone site.

1972 - The Alcohol, Tobacco and Firearms Division separated from the IRS to become the independent Bureau of Alcohol, Tobacco and Firearms.

1974 - Congress passed the Employee Retirement and Income Security Act, which gave regulatory responsibilities for employee benefit plans to the IRS.

1986 - Limited electronic filing began. President Reagan signed the Tax Reform Act, the most significant piece of tax legislation in 30 years. It contained 300 provisions and took three years to implement. The Act codified the federal tax laws for the third time since the Revenue Act of 1918.

1992 - Taxpayers who owed money were allowed to file returns electronically.

1998 - Congress passed the IRS Restructuring and Reform Act, which expanded taxpayer rights and called for reorganizing the agency into four operating divisions aligned according to taxpayer needs.

2000 - IRS enacted reforms, ending its geographic-based structure and instituting four major operating divisions: Wage and Investment, Small Business/Self-Employed, Large and Mid-Size Business and Tax Exempt and Government Entities. It was the most sweeping change at the IRS since the 1953 reorganization.

2001 - IRS administered a mid-year tax refund program to provide advance payments of a tax rate reduction.

2003 - IRS administered another mid-year refund program, this time providing an advance payment of an increase in the Child Tax Credit. Electronic filing reached a new high - 52.9 million tax returns, more than 40 percent of all individual returns.

2019 - Taxpayer First Act passed and signed into law on July 1, 2019, restructuring of the IRS required by Congress.

Direct link to ncpeFellowship Webinars: http://ncpefellowship.com/fellowshipwebinar.html

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GET THE CYBER COVERAGE YOU NEED – INCLUDED WITH OUR TAX PREPARERS E&O POLICY.

As a tax preparer or bookkeeper, you increasingly rely on technology to do business. Information technology is essential to everyday tasks – it decreases operational costs, increases speed to market, improves customer service and opens the door to opportunity. However, it can also lead to risks to your business.

Know the risks and the potential damages.

Hackers, malicious software, rogue employees and hardware loss or theft are all very real risks to your business, and the damages can be significant. Should a cyber event occur, The Hartford's new endorsement is designed to cover your business for the damages that typically result. What's more, this endorsement is automatically included with all Tax Preparer E&O policies at no additional premium.

COVERAGES INCLUDED IN THE ENDORSEMENT

NETWORK SECURITY WRONGFUL ACT

Helps protect against claims alleging negligence in connection with the performance or failure to perform tax preparation and bookkeeping services, which result in:

- Denial of services. The inability of an authorized third party to gain access to the insured’s online marketplace, to conduct e-commerce, transmit email or to affect file transfers.

Fictional Scenario: A disgruntled client is unhappy with the manner in which his taxes have been handled. To exact revenge, he brings down the tax preparer’s website. Employees can’t send emails or files. Other clients sue the tax preparer for damages incurred as a result of their inability to access the website and submit information via email.

Prepare. Protect. Prevail.

continued
• Inadvertent transmission of malicious code.

**Fictional Scenario:** A tax preparer sends confidential information via email to a client. Unbeknownst to the tax preparer, his computer was infected with a virus that was sent along with the email. The client opens the email, and the virus is activated and infects the client's server, damaging their computer system. The client sues the tax preparer for damages incurred from the inadvertent transmission of a malicious code to their network.

• Identity theft. Unauthorized taking or misuse of nonpublic personal information from the insured's computer.

**Fictional Scenario:** A tax preparer visits the office of one of his clients. En route, he leaves his laptop unattended, and it's stolen. The thief sells the laptop, downloads all of the files and steals the identity of all of the tax preparer's clients, who then sue the tax preparer for damages incurred from identity theft.

• Unauthorized access to an entity's information utilized in e-commerce, email, and file transfer.

**Fictional Scenario:** A hacker uses a security deficiency to enter a tax preparer's server and steals data from emails and files. The hacker then sells the data to third parties who used the data to steal identities. An irate client sues the tax preparer for damages that result from having their identity stolen.

**CRISIS MANAGEMENT EXPENSES**

Provides reimbursement for crisis management services performed by a public relations firm, crisis management firm, or law firm to mitigate potential harm to the insured's reputation in the event of a Network Security Wrongful Act.

**CREDIT MONITORING AND NOTIFICATION EXPENSES**

Provides reimbursement for credit monitoring and notification expenses in connection with statutory or regulatory mandate requiring credit monitoring or notice to specified individuals in compliance with state or U.S. federal data privacy laws.

**CYBER INVESTIGATION EXPENSES**

Provides reimbursement for expenses to conduct an investigation of its computer system by a third party to determine the source or cause of Network Security Wrongful Acts.

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Robert Dole

The purpose of a tax cut is to leave more money where it belongs: in the hands of the working men and working women who earned it in the first place.

Rob Knauerhase

Isn't it appropriate that the month of the tax begins with April Fool's Day and ends with cries of 'May Day'?

Roger Jones

I guess I think of lotteries as a tax on the mathematically challenged.

Jean-Baptiste Colbert

The art of taxation consists in so plucking the goose as to obtain the largest amount of feathers with the least amount of hissing. Benjamin Franklin, "Poor Richard's Almanac"

It would be a hard government that should tax its people one-tenth part of their income.

The tax advisor had just read the story of Cinderella to his four-year-old daughter for the first time. The little girl was fascinated by the story, especially the part where the pumpkin turns into a golden coach. Suddenly she piped up, "Daddy, when the pumpkin turned into a golden coach, would that be classed as income or a long-term capital gain?"

The difference between the short and long income tax forms is simple. If you use the short form, the government gets your money. If you use the long form, the tax advisor gets your money.

A couple of weeks after hearing a sermon on Psalms 51:2-4 (knowing my own hidden secrets) and Psalm 52:3-4 (lies and deceit), a man wrote the following letter to the IRS:

"I have been unable to sleep, knowing that I have cheated on my income tax. I understated my taxable income, and have enclosed a check for $150.

If I still can't sleep, I will send the rest."

What is the difference between tax avoidance and tax evasion? The jail walls.