TAX AND WEALTH ADVISOR ALERT: WISCONSIN FOLLOWS IRS, STATE TAX FILING DEADLINE EXTENDED TO JULY 15

Wisconsin law already provides that any extension granted by the IRS for filing income taxes also extends the time allowed for filing Wisconsin income taxes. Nevertheless, Governor Tony Evers and Department of Revenue Secretary Peter Barca announced on Saturday March 21, 2020 that Wisconsin law will automatically extend time and waive interest and penalties for taxpayers due to the President's declaration of a national emergency. A summary of what this means for Wisconsin taxpayers is below.

- Tax filers do not have to file any extension forms to be eligible for this new due date.
- There is no limit on the amount of payment to be postponed, and there are no income exclusions.
- This applies to individuals, trusts, estates, partnerships, associations, companies, and corporations.
- This relief is solely for income tax payments, estimated income tax payments, and returns due April 15, 2020.
- There will be no interest or penalty for the period of April 15, 2020 to July 15, 2020.
- Interest, penalties, and underpayment interest for failure to make quarterly estimated tax payments with respect to such postponed federal income tax filings and payments will begin to accrue on July 16, 2020.

We will continue to communicate updates as we receive them. If you are interested in learning more about the new tax filing guidance, please contact attorney Britany E. Morrison at O'Neil Cannon

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TAX AND WEALTH ADVISOR ALERT: IRS MOVING TAX DAY TO JULY 15 FROM APRIL 15

U.S. Treasury Secretary Steven Mnuchin just announced that the IRS will be moving the tax filing date to July 15 from April 15. Mnuchin says people and businesses will have more time to file and make payments without interest or penalties. Mnuchin made the announcement on Twitter, saying the move came at the direction of President Donald Trump. Further federal guidance in addition to guidance from states is expected.

If you are interested in learning more about the new tax filing guidance, please contact attorney Britany E. Morrison at O'Neil Cannon

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TAX AND WEALTH ADVISOR ALERT: TAXPAYERS MUST FILE BY APRIL 15 BUT CAN DELAY PAYMENTS FOR 90 DAYS

The Treasury Department issued guidance March 18, 2020 saying that taxpayers can delay paying some federal income taxes for 90 days but still must submit their forms to the Internal Revenue Service — or officially request an extension — by April 15.

Individuals can delay payments of up to $1 million in taxes and corporations can get payments of up to $10 million deferred until July 15 without interest and penalties, according to a notice published Wednesday. The guidance also stated that this tax relief would apply to 2020 estimated income tax payments owed by certain taxpayers, such as those who are self-employed.

Taxpayers failing to file their federal returns or request an extension by April 15 could get hit with large penalties—but only if they owe tax. The penalty for failing to file a tax return is 5% of the unpaid tax that should be reported, charged monthly for up to five months. If a person files more than 60 days late, the minimum penalty is the lesser of $435 or 100% of the unpaid tax.

As for state conformity, some states have already issued guidance, while most states,

including Wisconsin, have not. Therefore, payments will be due April 15 to the state of Wisconsin unless taxpayers officially request an extension.

If you are interested in learning more about the new tax filing guidance, please contact attorney Britany E. Morrison at O'Neil Cannon

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TAX AND WEALTH ADVISOR ALERT: PARTNERSHIP AND LLC AUDITS ARE

COMING—IS YOUR PARTNERSHIP OR LLC PREPARED FOR THE NEW RULES?

With all the tax changes taking effect in recent years, entities taxed as partnerships may have overlooked an important change from a few years ago—the new partnership audit rules. The changes to the partnership audit rules were unrelated to the highly publicized Tax Cuts and Jobs Act of 2017, and instead were introduced in the Bipartisan Budget Act of 2015 (BBA), effective as of January 1, 2018. The BBA dramatically overhauled the former rules for partnership audits, repealing and replacing the Tax Equity and Fiscal Responsibility Act (TEFRA) partnership rules.

Although the new rules are very complex, the biggest changes are that (1) partnerships rather than partners will now be liable for any tax deficiencies resulting from an IRS audit unless the partnership elects out of the new rules, and (2) the new position of "Partnership Representative" gives that person much greater power to make binding decisions than the traditional "Tax Matters Partner." Accordingly, it is important for members and partners to familiarize themselves with some of these changes and ensure that protections and plans are built into the partnership or operating agreements.

New Rule Changes

Prior to 2018 under TEFRA, if the IRS wanted to conduct an audit on the activity of a partnership, it was required to audit and collect tax from its partners. Thus, the IRS could audit the partnership as long as the IRS assessed and collected any understatement of partnership tax, interest, and penalties at the *partner level*. The amount of tax due from the partner depended on the partner's other tax attributes (i.e., the partner's other items of income, gain, loss, deduction, and credit), and the IRS collected the resulting tax from each partner. Over time, the application of TEFRA caused huge headaches for the IRS due to the administrative burden of matching and tracking each partner, collecting from or refunding each partner, and navigating tiered partnership complexities.

To combat these issues, the IRS created a streamlined audit approach under the BBA, called the Centralized Partnership Audit Regime (CPAR). CPAR provides that the IRS can still audit the activity of the partnership, however, the IRS can now access and collect any resulting understatement of tax, interest, and penalties (which under the new rules is referred to as the "imputed underpayment") directly from the partnership, rather than from the partners.

While the IRS can audit (within the statute of limitations) the partnership's items of income, gain, loss, deduction, credit, and partners' distributive shares for any particular year of the partnership (the "reviewed year"), any imputed underpayment due from the partnership will be assessed in the year that the audit or any judicial review is completed (the "adjustment

year"). By collecting the tax payable in the adjustment year rather than the reviewed year, ownership changes may produce what some partners consider unfair results. For instance, a new partner in an existing partnership may find it unfair to bear the tax burden for adjustments to the prior year's tax returns.

Additionally, under the new audit regime, instead of a tax assessment calculation based on the other tax attributes of each partner, the imputed underpayment assessed against the partnership is calculated by multiplying the total netted partnership audit adjustment for the reviewed year against a single tax rate. The tax rate will be the higher of (1) the highest income tax rate in effect for individuals (currently 37%) and (2) the tax rate applicable to corporations (currently 21%). Depending on a partner's individual tax situation this is an undesirable outcome if the partner falls into a lower tax bracket. However, following the rules published in the regulations, the partnership may modify the underpayment amount if the partnership can show the IRS that a partner's share of an adjusted item is subject to a lower tax rate, or if the partnership can establish that a partner has agreed to an adjustment and paid the resulting tax through an amended return. These potential modifications must be timely submitted and approved by the IRS.

Electing Out of New Partnership Audit Rules

The IRS does allow a partnership to elect out of the new audit regime under certain circumstances. In order to elect out of the new audit rules, the partnership must meet two requirements: (1) the partnership must have 100 or fewer partners during the tax year, and (2) all partners must be "eligible partners" at all times during the tax year. Eligible partners include individuals, C corporations, S corporations, or estates of deceased partners. The list of eligible partners does not include partnerships, trusts, disregarded entities, nominees or other similar persons that hold an interest on behalf of another person, and estates that are not estates of a deceased partner. If there is even one ineligible partner, the partnership cannot elect out of the new audit regime. Further, if the partnership has an S corporation as a partner, the shareholders of the S corporation will count toward the 100-partner rule.

An election to opt out must be made annually on a timely filed tax return and the partnership must notify partners of the election within 30 days of making the election. The partnership must also disclose the names and taxpayer identification numbers of all partners on its tax return. The result of this election moves the adjustment and assessment of tax to the partner level.

"Push-Out" Election

The new rules also provide that a partnership can make a "push-out" election, which allows a partnership to shift or "push-out" any tax liability due upon audit to the partners that were actually partners during the reviewed year (which eliminates the partnership's responsibility

to pay the tax). Unlike the election to opt out of the new audit rules, this election is available to all partnerships; however, this election can be made only by the Partnership Representative (as detailed below).

This election must be made within 45 days after the IRS issues the final adjustment and the partnership must then furnish statements to the reviewed year partners within 60 days of the final adjustment showing the partner's share of the adjustment. Based on statements, each reviewed year partner will calculate the partner's tax for the reviewed year and any interim years after the reviewed year and preceding the adjustment year. The partners then pay the aggregate tax plus interest (an additional 2% interest is charged using this election) and penalties with their income tax return for the adjustment year (i.e., the current year's tax return).

Goodbye Tax Matters Partner, Hello Partnership Representative

Under the new regime, a Partnership Representative replaces the familiar Tax Matters Partner. With TEFRA, a Tax Matters Partner would simply act as a go-between with the partnership and the IRS. In contrast, with the CPAR changes, the Partnership Representative has full authority to act on behalf of the partnership and take any necessary actions that are binding on the partnership and all its partners. Additionally, the Partnership Representative is not bound by a fiduciary duty to act in the best interest of the partnership.

Another departure from the old rules is that the Partnership Representative is not required to be a partner, unlike the Tax Matters Partner. It can be anyone that the partnership feels is capable and knowledgeable enough to make decisions on IRS assessments. The partnership must designate a Partnership Representative on its tax return filing each year. It is important to note that the old Tax Matters Partner does not automatically become the new Partnership Representative and if no Partnership Representative is appointed, the IRS will appoint one. A partnership can remove its Partnership Representative, but only after a Notice of Administration Proceeding is issued by the IRS.

Considerations for Partnership and Operating Agreement Amendments

As a result of the new audit rules, entities taxed as partnerships should begin preparing for the effect of the new regime and consider addressing potential issues with their existing partnership or operating agreements. For example, if the partnership is eligible and plans to opt out of the rules altogether, the operating agreement should require the Partnership Representative to make the election annually. Partners may even want to prohibit any transfer of a partnership interest to an ineligible partner that could prevent an opt-out election.

If the partnership is unable to opt-out or chooses not to, the operating agreement should

specify how the partnership will pay an imputed underpayment and how the imputed underpayment will be allocated amongst the partners, old and new. The operating agreement should also stipulate whether or not the partnership will make a push-out election.

Moreover, at the very least, given the broad discretion a Partnership Representative is allowed under the new regime, a partnership should appoint or designate a process for appointing a Partnership Representative in its operating agreement. The operating agreement should also address when/if the Partnership Representative will be liable to the partners for failure to make an election or making an election that was not in the best interests of the partnership. A partnership may also consider amending or adding indemnification provisions for the Partnership Representative.

A partnership may also want to consider including language that requires the Partnership Representative to notify partners upon certain stages in an audit or require the Partnership Representative to consult with or obtain consent of the partners before taking a position, agreeing to a settlement, or making an election. All of the foregoing issues can and should be addressed in amendments to operating agreements, and there is still time to do so before the IRS begins audits in earnest under the new regime.

If you are interested in learning more about the new partnership audit rules, please contact attorney Britany E. Morrison at O'Neil Cannon

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TAX AND WEALTH ADVISOR ALERT: NOT FEELING SO SECURE PART II: HOW THE NEW SECURE ACT MAY AFFECT YOUR RETIREMENT AND YOUR TAX SITUATION

The "Setting Every Community Up for Retirement Enhancement" Act (the SECURE Act), signed into law by President Trump on December 20, 2019, pointedly changes many requirements for employer-provided retirement plans, IRAs, and other tax-favored savings accounts. While some of the provisions of the SECURE Act may provide taxpayers with great tax savings opportunities, not all of the changes are helpful, and there may be steps taxpayers can take to minimize its impact. Below is a summary of the key provisions of the SECURE Act that taxpayers should be aware of now, especially since many of the provisions go into effect in 2020.

Repeal of the maximum age for traditional IRA contributions

Before 2020, individuals were prohibited from making traditional IRA contributions upon reaching the age of 70 ½. However, starting in 2020, the SECURE Act allows an individual of any age to make contributions to a traditional IRA if the individual has compensation, such as earned income from wages or self-employment.

This SECURE Act provision eliminates the age limitation, which previously prevented taxpayers older than 72 ½ from contributing to their IRAs. This will allow individuals working into their later years to increase, or catch up with, their retirement savings goals.

Required minimum distribution age raised from 70½ to 72

Pre-2020 retirement plan participants and IRA owners were typically forced to begin taking required minimum distributions, or "RMDs," from their plan when they reached age 70½. The age 70½ requirement was first established in the early 1960s and, until the SECURE Act, had not been adjusted to account for increases in life expectancy.

Under the SECURE Act, the age at which individuals must begin taking distributions from their retirement plan or IRA is increased from 70½ to 72. Notably, RMDs for individuals who turned 70½ in 2019 are not delayed, and instead, such individuals must continue to take their RMDs under the same rules prior to passage of the SECURE Act.

Increasing the age at which distributions are required allows additional time for the IRA to grow untouched. With many taxpayers remaining in the workforce longer, this provision might prove especially beneficial.

Partial elimination of stretch IRAs

If plan participants or IRA owners died before 2020, beneficiaries (both spousal and nonspousal) were generally allowed to draw from the account and pay taxes on their withdrawals over the beneficiary's life or life expectancy (in the IRA context, this is sometimes referred to as a 'stretch IRA').

However, under the SECURE Act, if a plan participant or IRA owner dies in 2020 or after, distributions to most ***nonspouse beneficiaries*** are generally required to be distributed within 10 years after the plan participant's or IRA owner's death. So, for those beneficiaries, the "stretching" strategy is no longer allowed.

Exceptions to the 10-year rule are allowed for distributions to beneficiaries who are (1) the surviving spouse of the plan participant or IRA owner; (2) a child of the plan participant or IRA owner who has not reached the age of majority; (3) a chronically ill individual; or (4) any other individual who is not more than 10 years younger than the plan participant or IRA owner. Beneficiaries who qualify under this exception may generally still take their distributions over their life expectancy (as allowed under the rules in effect for deaths

occurring before 2020).

Overall, this change will cause much larger distributions during peak earning years, which will have a significant impact on the tax obligation of nonspouse beneficiaries. Many retirement and estate plans were created to benefit from the pre-SECURE Act "stretch" tax deferral, so the SECURE Act's elimination of the "stretch IRA" might change how you plan to pass on accumulated accounts, or could influence how you need to handle accounts that are passed down to you. For more discussion on this potential tax impact, see Tax and Wealth Advisor Alert: Not Feeling so SECURE: Proposed Law Could be Costly for Non-Spouse IRA Beneficiaries.

If you are interested in learning more about the SECURE Act and how it might affect your retirement and estate planning goals, please contact attorney Britany E. Morrison at O'Neil Cannon to discuss how we are able to assist you.

TAX AND WEALTH ADVISOR ALERT: 'TIS THE SEASON FOR CHARITABLE GIVING AND TAX DEDUCTIONS

As we enter the holiday season and focus on what we are most thankful for, many of us will begin planning for our annual charitable contributions. While tax benefits are not the primary reason behind most giving—giving back is its own reward—the IRS has established these tax benefits to encourage charitable giving. This year, as you begin making decisions about your gifting, make sure you understand and consider the recent changes under tax reform so you can stay on the nice list and get the most out of your charitable giving tax deduction!

Standard or Itemized Deductions

A common thought with charitable giving is that you can take a charitable contribution deduction for the full amount of your donation and directly offset your income. This thought will get you on the naughty list! You can *only* receive a charitable donation tax deduction if you "itemized" your deductions. You will not receive a charitable donation tax deduction if you take the "standard deduction."

The Tax Code allows you to subtract a standard deduction based on your filing status or subtract your total itemized deductions—whichever is greater. For 2019, the standard deduction will be $12,200 for single taxpayers, $18,350 for heads of households, $24,400 for joint filers, and $12,200 each for married couples filing separately. Allowable itemized

deductions, sometimes subject to limits, include such expenses as mortgage interest, charitable contributions, state and local taxes and medical expenses. Look at the following example. If you are a single taxpayer, and the sum of your itemized deductions (contributions included) do not exceed $12,200, you will take the standard deduction over the itemized deduction. In this scenario, you will technically not receive a tax deduction for your charitable contribution.

Before the new Tax Cuts and Jobs Act, the standard deduction for each filing status was about the half the amount that it is for 2019. The increase in the standard deduction makes itemizing a difficult hurdle to jump, and many may now find it harder to itemize and take advantage of the charitable contribution deduction.

However, if you can itemize, the allowable charitable contribution deduction will depend on the type of contribution made (i.e., of cash, securities, property, etc.), as well as the type of organization to which the donation was made. While most charitable deductions are limited to 60% of your adjusted gross income (AGI), some are limited further—to 30% or, in some cases, even 20%. Therefore, your total AGI is an important consideration if you plan to benefit from a charitable donation deduction.

In short, at a minimum, you will be able to deduct 20% of your AGI. At a maximum, you will be able to deduct 60%. If you made charitable contributions during the year, and one or more limits described below apply, you can use the IRS's Worksheet 2 to help compute your deduction.

Eligible Donations

Before understanding the deduction limitations for each type of charitable contribution, it is important that your charitable contribution be eligible to claim as an itemized deduction. Only donations to 501(c)(3) public charities or private foundations are generally deductible as qualified charitable donations. Of note, gifts given to benefit specific individuals are not deductible, which includes most online crowdfunding websites. Moreover, gifts made to political parties, political campaigns, political action committees, labor unions, chambers of commerce, business associations, for-profit schools or hospitals and foreign governments are also not tax deductible.

Additionally, gifts to donor-advised funds, a recently popular vehicle for gift giving, have further eligibility restrictions which should be evaluated before funding. The IRS offers a search tool (Tax Exempt Organization Search) so you can confirm the 501(c)(3) status of an organization you are considering donating to.

Lastly, it is important to remember that your donation to a qualified charity is deductible only in the same year in which it is made. Therefore, if you plan to take a deduction for 2019, you

must make sure your deduction is made before December 31 and you ring in the new year!

Charitable Gifts of Cash

Under the old law, your deduction for charitable contributions of cash to qualified organizations was limited to 50% of your adjusted income. If your contributions exceeded this limit, you could carry them forward for up to five years. Under the new Tax Cuts and Jobs Act, until 2026 (unless otherwise extended), the limitation is raised to 60% of your adjusted gross income for gifts of cash to qualified organizations; the five-year carryforward is still allowed.

For example, if your adjusted gross income is $220,000 for the year, you can take a charitable deduction of up to $132,000 (60% of $220k) as long as the gift was in cash and made to a 501(c)(3) public charity. Therefore, if you made a gift of cash that year to the Salvation Army of $150,000, your gross income can be offset by the $132,000 charitable deduction limit (reducing it to $88k) and the remaining $18,000 of your charitable deduction that you were not able to utilize due to the percentage limitations can be carried forward for the next five years.

Charitable Gifts of Non-Cash Items

The IRS will allow a deduction for donations of non-cash items as well, if the item is in "good working condition or better." Therefore, stop and think before claiming a deduction for the donation of a dusty old toaster that is missing a few parts that you received 35 years ago as a wedding gift. There is no fixed method for determining the value of these items, but the IRS, Salvation Army, and Goodwill, all provide helpful valuation guidelines.

If you make noncash contributions, your deduction for the noncash contribution is limited to 50% of your adjusted gross income minus your cash contributions subject to the 60% limit. If your total deduction for all noncash contributions for the year is over $500, you must complete Form 8283 and list the donated items, as well as their value, and attach it to your Form 1040. Additionally, any non-cash contribution over $5,000 will most likely require a qualified appraisal attached to the Form 8283 to substantiate the value (publicly traded stock may be an exception).

Charitable Gifts Quid Pro Quo

If you receive some sort of compensation for your donation (such as tickets to a charity gala, a theatrical performance, a sporting event, or merchandise, goods, or services), you can only deduct the amount of the donation that exceeds the fair market value of what you received. Moreover, you cannot deduct the cost of raffle, bingo, or lottery tickets bought from a charitable organization or deduct the value of your donated time or professional services, or the value of donated blood. Additionally, important for all of those college sports fans to know, is that under the new Tax Cuts and Jobs Act, if you make contributions in exchange for

the right to buy college athletic tickets, you are not allowed a deduction for this donation (previously, you could deduct 80%).

Charitable Gifts of Securities

Direct donation of publicly traded securities (or other illiquid gifts) is another common way to fund a charity for donors. This is a particularly tax-efficient method if you have long-term appreciated stock, because with a direct charitable gift of appreciated securities held long-term, you avoid paying the capital gains tax (typically 20% of the appreciated value). If you were to sell the shares and donate the cash proceeds instead, while you would get the higher percentage limitation with the donation of cash (60%), you would have to pay the capital gains tax upon the sale of the shares. This usually does not result in a greater tax benefit than a direct donation of securities.

The amount of the charitable deduction and the limitation on the deduction depends on how long the securities (or other illiquid gifts) have been held and, in part, on the type of charity receiving the property (for example, private foundations are subject to different limitations – but that is beyond the scope of this discussion). If you donate short-term securities to a public charity, a deduction is allowed only for the lesser of (1) the FMV of the securities or (2) your cost basis. In most cases, if the stock appreciated, this will mean your deduction is your cost basis. You may then deduct up to 50% of AGI, reduced by the amount of any cash contributions you made that year allowed under the 60% limit. If you donate long-term securities to a public charity, a deduction is generally allowed for the FMV of the securities. You may then deduct the lessor of (1) 30% of your AGI or (2) 50% of your AGI less other contributions to 50% charities and cash contributions allowed under the 60% limit.

Charitable Gifts from Your IRA

If you meet the requirements, you can also make a charitable contribution from your IRA. However, your ability to take a charitable deduction will depend on whether the contribution is made from your traditional IRA or Roth IRA. If you are age 70½ or older, you may make direct charitable gifts from your traditional IRA (which counts toward your required minimum distributions) of up to $100,000 to public charities (other than donor advised funds and supporting organizations) and not have to report the IRA distributions as taxable income on your federal income tax return. There is no charitable deduction for the distributions, so you benefit from this if you do not itemize your deductions. However, not paying tax on otherwise taxable income is essentially the equivalent of a charitable deduction.

Assuming the Roth IRA distribution requirements are met (generally, over the age of 59½ and held Roth for over 5 years), your cash distribution from a Roth IRA will be tax free. You can then use this distribution to make a cash donation to a charity. The bonus here is that there are no restrictions on the type of charity like there are with the traditional IRAs. Additionally,

unlike traditional IRAs, you can claim an itemized deduction for your charitable cash contribution up to the 60% of AGI limitation. Nevertheless, it generally is not the best option to take distributions from your Roth IRA and donate to charity because the tax rules for Roth IRAs are so favorable. Usually, it is best to leave your Roth balances untouched and earning more tax-free income rather than taking money out for charitable contributions if you can make your contributions from a different source.

Documentation

No matter what you end up donating and how limited your deduction may be, the most important thing to remember if you intend to reap the tax benefits of your charitable contribution is that you must keep accurate records of your contribution. Any contribution over $250 must be acknowledged with a receipt from the charity indicating the organization's name, the date of the contribution and the amount. The IRS notes that you, the donor, are responsible for requesting and obtaining the written acknowledgment from the charity. Typically, charities will provide donors with written letters of acknowledgement or receipt; however, you can write it yourself ahead of time, and simply have it signed when you drop off your items. This way you can trust that the receipt is correct and that it includes all the information you need.

The IRS can disallow charitable donations of $250 or more if you do not have a written acknowledgment from the charity to document your gift. So, while your canceled checks, receipts, bank statements, telephone bills or photographs (all of which you should keep) can be useful if your return is audited, the IRS may not allow the deduction in case of a missing acknowledgement receipt or letter.

Conclusion

While taxes might not be at the forefront of your mind when gifting this holiday season, the tax deduction for charitable contributions is a nice added benefit under the tree! To make the most out of this tax benefit it is important to familiarize yourself with the deduction rules and limitations.

The attorneys at O'Neil, Cannon, Hollman, DeJong and Laing S.C can ensure that you are making donations that best serve organizations while helping you maximize tax benefits this holiday season. If you need assistance in developing individual tax strategies or have questions about tax and estate planning, please contact Attorney Britany E. Morrison to discuss how we can assist you in your needs.

ATTORNEYS CARL HOLBORN AND BRITANY MORRISON PUBLISHED IN THOMSON REUTERS JOURNAL

Attorneys Carl D. Holborn and Britany E. Morrison were recently published in the *Taxation of Exempts*, a Thomson Reuters journal.

There is a big unresolved public policy issue in the philanthropic world—private foundations and their use of donor-advised funds (DAF). Specifically, the issue is whether distributions made by private foundations to donor-advised funds should be treated as "qualifying distributions" for purposes of the 5% annual payout rule.

While the issue was sparsely debated before, the IRS really stirred the debate in the charitable world with the issuance of Notice 2017-73. The Notice specifically requests comments on whether a contribution to a DAF by a private foundation should be considered a distribution that counts as a "qualifying distribution" for the purposes of the annual 5% payout rule. [1] Comments in response to the Notice poured in and opinions were deeply divided between those in favor of reform to disallow or limit "qualifying distributions" to DAFs and those in full defense of the IRS maintaining the status quo.

Two years have passed since the Notice issuance and the IRS has yet to issue an any regulations or proposed regulations. This article highlights some of the major arguments for reform, limits, and the status quo regarding private foundations distributions to DAFs "counting" as qualified distributions.

Read full article here.

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[1]See Notice 2017-73, 2017-51 IRB 562 available at https://www.irs.gov/pub/irs-drop/n-17-73.pdf.

TAX AND WEALTH ADVISOR ALERT: PROPOSED BIPARTISAN BILL TO EXPAND RESEARCH AND DEVELOPMENT TAX CREDIT

Late July, Senator Maggie Hassan (D-NH), a member of the Senate Finance Committee, and Senator Thom Tillis (R-NC) introduced the bipartisan Research and Development Tax Credit

Expansion Act that aims to double the refundable research and development (R&D) tax credit and increase the alternative simplified credit rate for new and small businesses. If enacted, the bill would provide additional cash savings for eligible businesses that perform qualified R&D activities.

Background

While the R&D tax credit has been around for a while, historically, many small businesses and start-up companies could not immediately benefit from the R&D credit as they were not generating income in early years and thus they had no regular tax for the R&D credit to offset. Noticing this limitation, the PATH Act of 2015 added new IRC Sections to allow qualified small businesses to apply the R&D credit against their employer's payroll tax liability (up to $250,000 annually). For these purposes, a "qualified small business" is generally defined as a corporation, partnership or sole proprietorship with: (1) gross receipts of less than $5 million for the tax year and (2) no gross receipts for any tax year before the five tax years ending with the election year.

New R&D Credit Bill

The new bill aims to double the amount of R&D credit that can be used to offset an employer's payroll tax liability by increasing the annual cap from $250,000 to $500,000 and then automatically indexing for inflation. In addition, the bill would expand the number of eligible businesses that qualify for the credit by raising the maximum amount of gross receipts from $5 million to $10 million per year. It would also allow the R&D credit to offset *all* payroll taxes so businesses can apply the credit against Medicare and unemployment taxes, in addition to Social Security taxes. Lastly, the bill would increase the alternative simplified credit rate (a method used to calculate the R&D credit), which provides a credit of 14% for research that exceeds half of the average research spending from the last three years. The bill would increase the alternative simplified credit rate from 14% to 20% for new and small businesses that qualify for the credit.

Implications

If enacted, eligible taxpayers would doubly benefit by both generating a higher credit amount and being able to apply more of the credit generated against their payroll tax. Additionally, the bill would increase both the availability of the payroll offset option as well as the ability to generate cash tax savings for eligible taxpayers. The proposed Act certainly removes many of the barriers that limit a new or small businesses' ability to claim the credit. Nevertheless, while we wait to see if Congress will approve the Research and Development Tax Credit Expansion Act, we will continue to advise our clients to ensure their R&D tax credit compliance and counsel on effective tax planning opportunities should the Act go into effect.

If you are interested in learning more about your eligibility or effective tax planning opportunities for the current and/or proposed R&D tax credit, please contact Attorney Britany E. Morrison at O'Neil Cannon to discuss how we are able to assist you in your needs.

TAX AND WEALTH ADVISOR ALERT: TIME TO ACT ON ACT 368: WISCONSIN PASS-THROUGH ENTITY-LEVEL TAX ELECTION

In December of 2018, Wisconsin enacted tax legislation—Wisconsin Act 368—that specifically impacted LLCs, S-Corps, and partnerships ("pass-through entities"). The Act allows pass-through entities to make an annual election to be taxed at the entity-level, rather than at the individual level. This election may provide significant tax savings to Wisconsin businesses and their owners, but this election won't work for everyone. While the new Wisconsin law certainly brings some tax saving opportunities, there are election rules and potential issues that Wisconsin owners of pass-through entities must consider before deciding whether to make the election.

BACKGROUND

Historically, individuals were not limited in what they could deduct for state income and property taxes. However, starting in 2018, due to the Tax Cuts and Job Act, the deduction for state income and property taxes is now limited to $10,000. Wisconsin has attempted a creative approach with Act 368 to circumvent this limitation by allowing pass-through entities to be taxed at the entity-level. The idea is that the Tax Cuts and Job Act deduction cap applies to individuals and not businesses, so by allowing the pass-through entity to be taxed at the entity-level, the deduction is shifted from a capped deduction to an uncapped deduction.

TREATMENT

The new provision allows for pass-through entities to elect to be taxed at the entity-level which is a flat rate of 7.9% (the WI corporate income tax rate) rather than passing the income to shareholders to be taxed on their individual return (7.65% for individuals at the highest income tax rates). The entity-level tax would then be deductible by the pass-through on its Federal return resulting in a decrease of Federal income and corresponding Federal tax. Therefore, even though the entity-level rate is higher than the individual rate, this could still result in beneficial tax savings if pass-through owners were previously limited by the cap.

ELECTION

S-Corps can begin making the election beginning with the 2018 tax year, while partnerships and LLCs may make this election starting with the 2019 tax year. For S-corps, persons holding more than 50% of shares on the day of election must consent, while for partnerships, persons holding more than 50% of capital and profits interest on the day of election must consent. The advantageous feature about this election is that it is flexible, in that it can be made on an annual basis. Pass-through entities can opt in or out each year without limitation or penalty. Additionally, the election must be made on or before the due date or extended due date of the WI return.

POTENTIAL ISSUES

While this may sound like a straight forward decision to make the election for a Wisconsin owner of a pass-through entity, there are several potential issues to consider before making the election.

- *Tax Rate*: If taxpayers in pass-through entities are not subject to the top individual income tax rate of 7.65%, it is possible they may not receive enough of a benefit from the entity-level deduction to offset the cost of having to pay tax at a higher 7.9% rate.
- *Credits*: The only credit that pass-through entities may claim against the WI entity-level tax is the credit for income taxes paid to other states. The loss of the ability to claim manufacturing and agricultural credits in addition to research and development credits, for example, may outweigh the benefits of the election.
- *Loss Position:* The election would not be advisable for pass-through entities experiencing losses as there would be no deductible state taxes anyway and such losses would effectively be wasted.
- *Out -of-State Owners*: If the pass-through entities have a substantial number of out-of-state owners they may not benefit from the election if the owners are not allowed a corresponding exclusion or credit for the income tax being paid at entity-level in WI on their individual home state returns.
- *Lack of IRS Support*: There has been no guidance or reaction from the IRS yet, so there is a risk that future Federal laws or regulations could render this WI election ineffective. Other states have attempted workarounds and the IRS has made those ineffective by proposed regulations and notices. Although WI's workaround is a bit different than the state's that have tried, and there is support, there is still risk.
- *Legal Document Compliance*: The election may require amendments to the Wisconsin pass-through entities' operating agreement and formation documents. This should be discussed with legal counsel and the documents should be amended, if necessary, before the election is made.

Ultimately, pass-through entities in an income position that do not have any applicable WI credits or out-of-state owners have the best potential for tax savings. However, because the election does not have to be made until the extended due date, there is a real opportunity for Wisconsin owners of pass-through entities to analyze the above-mentioned issues with both tax advisors and legal counsel to determine whether the election is beneficial and/or worth the extra compliance costs before committing to the election.
If you are interested in learning more about Act 368 and WI's entity-level tax election or need assistance in tax and/or legal planning to take advantage of the election, please contact Attorney Britany E. Morrison at O'Neil Cannon to discuss how we are able to assist you in your needs.

IRS UNVEILS SIGNIFICANT VIRTUAL CURRENCY TAXATION ENFORCEMENT INITIATIVE

The Internal Revenue Service (IRS) recently announced that, by the end of August 2019, more than 10,000 taxpayers would receive mailed letters relating to virtual currency. The IRS is sending the letters to taxpayers who may have failed to report income, pay taxes, or properly report virtual currency transactions. For this purpose, virtual currency includes cryptocurrency and non-crypto virtual currency, including Bitcoin, Ether and JPM Coin.
There are three different types of letters being sent to taxpayers. Each of the three versions are intended to provide information to help taxpayers understand their tax and filing obligations and how to correct previous errors. However, the letters differ from one another in tone and in the response required by the recipient taxpayer.
Two of the letters invite taxpayers to voluntarily report and pay previously unreported virtual currency income, penalties, and interest. The other letter alleges likely noncompliance in stronger terms and requires specific action by a stated deadline. The text of this final letter indicates that the recipient should expect significant IRS scrutiny, as well as potential examination or enforcement action.

Three Letter Versions

- **Letter 6174** (available here) notifies a taxpayer that the IRS has information regarding a potential failure to report income from a virtual currency transaction. The letter provides information regarding the taxation and reporting rules which apply regardless of whether the taxpayer received a payee statement (such as a Form W-2 or Form 1999) for a virtual currency transaction. Taxpayers need not respond to the letter, but are advised to file amended tax returns or delinquent tax returns if a virtual currency transaction was not previously accurately reported on a federal income tax return.
- **Letter 6174-A** (available here) is worded nearly identically to Letter 6174. A key

difference is that this letter informs the recipient taxpayer that the IRS is likely to send additional correspondence about potential virtual currency tax enforcement in the future.
- **Letter 6173** (available here) asserts that federal tax filing and reporting requirements appear to have been unmet by the recipient taxpayer for one or more of the tax years 2013 through 2017. The letter then directs the taxpayer to file amended tax returns. If the taxpayer believes that all tax reporting requirements have already been properly met, the taxpayer must formally respond to the IRS to attest to that position. Supporting detail and documentation must also be submitted. The taxpayer is required to sign the attestation under penalties of perjury that the submission, including all attachments, are true, correct, and complete. Any taxpayer-submitted information will be checked for accuracy against information received by the IRS from banks, financial advisors, and other sources. If a taxpayer does not respond to this letter within 30 days of the date on which the letter was mailed, the IRS will refer the account for audit.

Second Round of Additional Letters

In addition to the more than 10,000-letter initiative that the IRS publicly announced, as described above, some taxpayers are also reporting receipt of an apparent second group of letters in the form of a CP2000 Notice. The CP2000 Notice states that the IRS has received information from a third party that doesn't match information on the taxpayer's submitted tax return. The notices acknowledge that a virtual currency trading exchange, rather than the taxpayer, may have made the error. In any event, receipt of a CP2000 Notice indicates that the IRS is aware of a reporting discrepancy. A response to the letter is imperative and additional detail on responding is available here).

IRS Regards Virtual Currency as Property

The current IRS Virtual Currency enforcement initiatives conform to IRS guidance previously published in Notice 2014-21, which provides that virtual currency is treated as property for federal tax purposes. As is the case with any property, tax law requires reporting and taxation of amounts that are transferred for services or sold. Among other things, this means that:

- A payment made (or received) in virtual currency is subject to information reporting to the same extent as any other payment made (or received) in property.
- Payments using virtual currency made to independent contractors and other service providers are taxable, and self-employment tax rules generally apply. Typically, payers must issue Form 1099-MISC.
- Wages paid to employees using virtual currency are taxable to the employee, must be reported by an employer on a Form W-2 and are subject to federal income tax withholding and payroll taxes.
- Certain third parties who settle payments made in virtual currency on behalf of merchants that accept virtual currency from their customers are required to report payments to those merchants on Form 1099-K, Payment Card and Third-Party Network Transactions.
- A taxpayer that successfully "mines" virtual currency (for example, uses computer

resources to validate Bitcoin transactions and maintain the public Bitcoin transaction ledger) realizes gross income upon receipt of the virtual currency resulting from those activities.
- The character of gain or loss from the sale or exchange of virtual currency depends on whether the virtual currency is a capital asset in the hands of the taxpayer.

Expect Additional IRS Enforcement Efforts

The IRS has stated its awareness that because transactions conducted using the more than 1,500 known virtual currencies can be difficult to trace and have an inherently pseudo-anonymous aspect, some taxpayers may be tempted not to report virtual currency-related income to the IRS. The mailing of the more than 10,000 letters and the CP2000 Notices, to taxpayers believed to have engaged in unreported virtual currency transactions, is therefore likely to be only the first of many virtual currency enforcement actions. Additional IRS guidance is expected to be published on virtual currency reporting and taxation rules soon, updating the last official guidance issued in 2014

In the meantime, even taxpayers who do not receive a letter or notice should be aware that a failure to properly report the income tax consequences of virtual currency transactions could result in liability for tax, penalties, interest, and in some cases, exposure to criminal prosecution. Criminal charges could include tax evasion and filing a false tax return. Anyone convicted of tax evasion is subject to a prison term of up to five years and a fine of up to $250,000. Anyone convicted of filing a false return is subject to a prison term of up to three years and a fine of up to $250,000.

The attorneys of O’Neil Cannon can assist in reviewing, or responding to any of the three types of IRS Virtual Currency letters, the CP2000 Notices, and other tax-related notice or assessment letters received from the IRS.