



2023 WICPA TAX CONFERENCE

YOUR SOURCE FOR KEY UPDATES & INSIGHTS ON TIMELY ISSUES

HIGHLIGHTED TOPICS:



FEDERAL TAX UPDATE

Find out how to be prepared for the upcoming filing season challenges, receive useful strategies for the yearend tax planning and tax return preparation process



IRS UPDATE

Get the latest IRS updates, including new tools and programs all CPAs should be aware of, as well as the current status of IRS operations



PREPARING FOR SUNSET

Learn about the criticality of planning for the sunset of the TJCA as it relates to the enormous rewards for thinking ahead and the consequences of failing to do so

THURSDAY, NOV. 2 & FRIDAY, NOV. 3
BROOKFIELD CONFERENCE CENTER & WICPA CPE LIVESTREAM

CONFERENCE AT A GLANCE

THURSDAY, NOV. 2

Brookfield Conference Center & WICPA CPE Livestream

7 – 8 a.m.

Registration & Networking
Celebration Atrium

8 – 8:15 a.m.

Welcome & Opening Remarks
Connect B

8:15 – 9:45 a.m.

GENERAL SESSION
Federal Tax Update Part I
Connect B

9:45 – 10 a.m.

Networking Break
Celebration Atrium

10 – 11:30 a.m.

GENERAL SESSION
Federal Tax Update Part II
Connect B

11:30 – 12:45 p.m.

Networking Lunch
Collaborate

12:45 – 1:45 p.m.

BREAKOUT SESSIONS
Charitable Contributions of
Property
Connect B

Practice Management Panel
Connect C1

1:45 – 2 p.m.

Networking Break
Celebration Atrium

2 – 3 p.m.

GENERAL SESSION
IRS Update
Connect B

3 – 3:10 p.m.

Networking Break
Celebration Atrium

3:10 – 4 p.m.

BREAKOUT SESSIONS
Business Transactions & ESOPs
Connect C2

Qualified Appraisals
(Valuations) for Tax Reporting
Purposes
Connect B

Sec. 83 Overview & Issues
Connect C1

4 – 4:10 p.m.

Networking Break
Celebration Atrium

4:10 – 5 p.m.

GENERAL SESSION
Hot Tax & IRS Practice &
Procedure Issues
Connect B

5 – 6:30 p.m.

Networking Social
Celebration Atrium

CONFERENCE AT A GLANCE

FRIDAY, NOV. 3

Brookfield Conference Center & WICPA CPE Livestream

7 – 8 a.m.

Registration & Networking
Celebration Atrium

8 – 8:15 a.m.

Welcome & Opening Remarks
Connect B

8:15 – 9:20 a.m.

GENERAL SESSION
Wisconsin Tax Update
Connect B

9:20 – 9:40 a.m.

Networking Break
Celebration Atrium

9:40 – 10:40 a.m.

GENERAL SESSION
Wisconsin Department of
Revenue Update
Connect B

10:40 – 11 a.m.

Networking Break
Celebration Atrium

11 a.m. – 12 p.m.

BREAKOUT SESSIONS
Entity-Level Tax Election &
Other State Tax Credit
Connect B

Multistate Taxation of Trusts
Connect C1

The Employee Retention
Credit: Navigating Areas of
Ambiguity
Connect C2

12 – 1 p.m.

Networking Lunch
Collaborate

1 – 2 p.m.

BREAKOUT SESSIONS
How to Recognize & Correct
Code Section 409A Failures
Connect C1

Why Should You Care About
Social Security Benefits?
Connect B

2 – 2:15 p.m.

Networking Break
Celebration Atrium

2:15 – 3:45 p.m.

GENERAL SESSION
Preparing for Sunset
Connect B

3:45 p.m.

Closing Remarks & Prize
Drawings
Connect B



HELPING INNOVATIVE COMPANIES & CPA FIRMS



Take Advantage of
THE R&D TAX CREDIT



COMPLIMENTARY
Feasibility & Evaluation



OPTIMIZED
Calculation & Substantiation



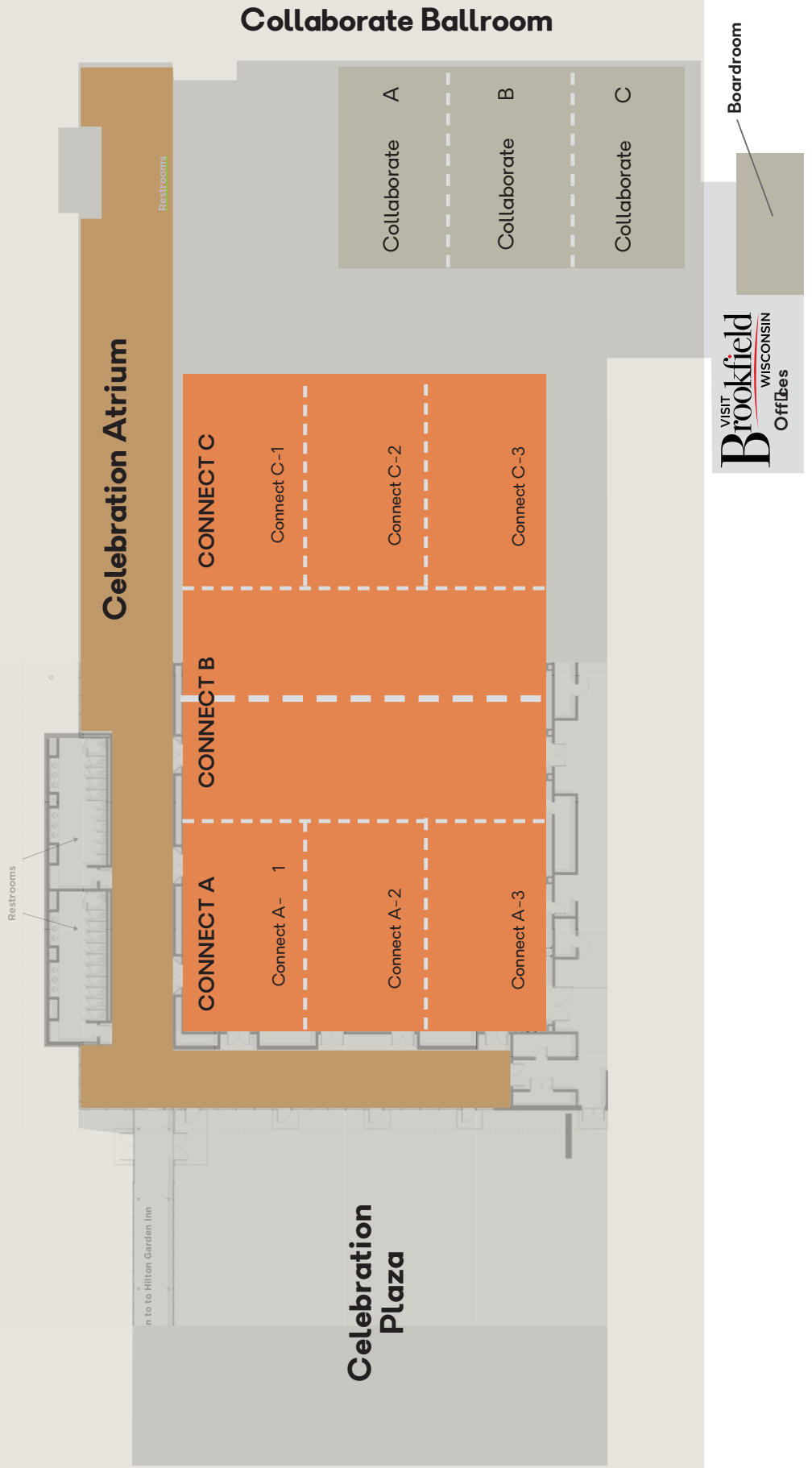
STREAMLINED
Process & Communication

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BROOKFIELD CONFERENCE CENTER

FLOOR PLANS AND CAPACITY CHARTS



FUTURE-PROOF YOUR CPA FIRM

Technology Built By CPAs for CPAs

“Every Monday we run a bunch of reports, distribute them and then use them to report on individual performance, It’s nice to be able to share that data in real-time so that our associates are ‘living’ it every day, versus waiting for a report.”

Frank Vinopal
CPA, Partner, MBE CPAs

“The reporting and dashboards in PracticeERP save me 5 hours a week. I can keep the reports and customize them to each partner’s specifications. It is a gamechanger having real time data at the click of a button.”

Kali Burmester
Tax Manager, MBE CPAs

“In the accounting world, predicting future revenues is difficult. With PracticeERP, we have the ability to track clients through CRM, and then have a dashboard of predicted upcoming revenue based on new clients added or lost, is huge.”

Tim Moy
CPA, CGMA, Managing Partner MBE CPAs

“I like that time entry and workflow are all in one system as well as the fact that PracticeERP is customizable. Monitoring projects on the dashboards has helped make workflow and keeping tabs on your workload way easier.”

Dilyana Feneva
Assurance Services Manager, MBE CPAs

Benefits of an ERP:

- Accurate Reporting
- Dashboards with Real Time Data
- One True Source for Data
- Save Time & Increase Production
- Streamline Processes and Communication



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*based on 2020 Client Retention Rates

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We specialize in multi-state sales/use tax consulting,
serving companies of all sizes across most industries.

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mitigate sales/use tax exposure and improve compliance.

We partner with CPA and CFO firms on a national level
to help them support their clients' sales/use tax needs.

THE SALES TAX TEAM

State and Local Tax Specialists

With offices in California, Texas, and Wisconsin, and over 90 years of combined sales tax consulting experience, the firm assists businesses with:

- Sales tax audit representation
- M&A due diligence
- Multi-state taxability reviews
- Nexus determinations
- Internal audits
- Refund requests
- Training
- Registrations and returns

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TheSalesTaxTeam.com

YOUR TRUSTED TAX SOLUTION

The Tax Section of von Briesen & Roper, s.c. is your resource for tax situations ranging from the traditional to the most complex including: State and Federal Voluntary Disclosures, FBAR/Foreign Asset Disclosures, Transfer Pricing, Property Tax Exemption Requests, Employee Classification Issues and State Tax Nexus Studies. Our knowledge and experience have positioned us to be your trusted solution on unique tax matters. *The bottom line? We get results.*

To learn more about our Tax Section, please contact Daniel Welytok at daniel.welytok@vonbriesen.com.



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The worst brings out our best.®



WICPA Educational
FOUNDATION



YOU have the opportunity to impact thousands of students and educators in Wisconsin.

Through your contribution to the WICPA Educational Foundation, you can help us reach students and educators in high school and college to create awareness about the accounting profession.

As the end of 2023 draws near and you are thinking about tax planning, consider donating to the WICPA Educational Foundation.

Questions? Contact Tammy J. Hofstede, WICPA President and CEO at tammy@wicpa.org.

To contribute, visit wicpa.org/EF.



WICPA Educational
FOUNDATION

Join the WICPA Educational Foundation Board!

The WICPA Educational Foundation is seeking members to serve on its board of directors.



Some of the opportunities include:

- Assisting in efforts to attract students to the profession.
- Providing strategic governance in accordance with the WICPA Educational Foundation mission.
- Acquiring new leadership skills.

The WICPA Educational Foundation plays a pivotal role in supporting programs to improve awareness and perceptions by educating students and educators about the exciting opportunities available to accounting professionals.

To apply, visit wicpa.org/EFBoardApplication through Feb. 28, 2024. ► **Questions?** Contact tammy@wicpa.org.

TRACK YOUR CPE WITH THE WICPA'S CPE TRACKER

The CPE Tracker is an easy to use tool created to keep track of all your CPE in one convenient location.

- Automatically tracks WICPA formal learning activities
- Add any non-WICPA CPE courses
- Print reports for any reporting period

To get started, visit
wicpa.org/cpetracker



Join the WICPA Board of Directors!

The WICPA is seeking members to serve on its board of directors.

Opportunities include:

- Staying up to date on professional issues
- Providing strategic governance in accordance with the WICPA strategic plan, mission and vision
- Acquiring new leadership and training skills



To apply, visit
wicpa.org/BoardApplication
through Nov. 15, 2023.

Questions?

Contact tammy@wicpa.org.

Applicants must be WICPA CPA members in good standing. A "CPA member" is defined as a WICPA member who has obtained a certificate as a CPA from the Accounting Examining Board of the State of Wisconsin, or from a similar legally constituted authority in any other state, possession or territory of the United States or the District of Columbia.

VOLUNTEER

CELEBRATE
CPA
APPRECIATION
MONTH
NOVEMBER 2023

To help raise awareness of the accounting profession, we're looking for volunteers to go into high schools to talk about accounting as a career.

To learn more, visit wicpa.org/CPAMonth



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Certified Public Accountants

2024
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Excellence
★ ★ ★
★ ★ A W A R D S



**NOMINATE SOMEONE
FOR AN EXCELLENCE AWARD!**

View categories and submit your nomination at
wicpa.org/awards by Nov. 10, 2023.

Recipients will be announced in January and honored at the
Member Recognition Banquet & Annual Business Meeting on May 9, 2024.

8:15 – 9:45 a.m. and 10 – 11:30 a.m.

Federal Tax Update Part I & Part II

Doug Van Der Aa, CPA, JD, *President, Van Der Aa Tax Education*

2023 Federal Tax Update



2023 Federal Tax Update

Materials developed and presented by:
Douglas J. Van Der Aa, CPA, JD
Grand Rapids, Michigan

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Meet Doug Van Der Aa



Doug Van Der Aa is a lively and energetic speaker – especially on the subject of taxes and ethics. He has been a highly rated speaker and seminar leader for CPA Associations and other organizations throughout the country for more than 18 years.

Doug has over 25 years of professional experience, including tax practice in CPA firms and the practice of transactional business and real estate law as an attorney. As a CPA, Doug’s practice concentrated on the tax needs of closely held businesses, with their related pass-through entities, complex individual returns, estates and trusts.

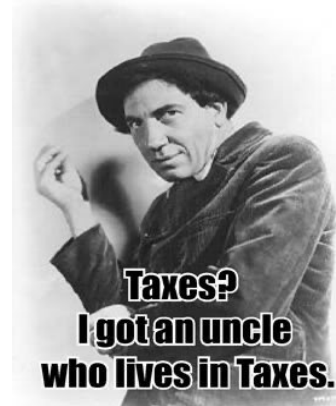
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2023 Federal Tax Update

Course Development Resources

- ❖ The author gratefully acknowledges **RIA Checkpoint** for use of certain materials included in this presentation.
- ❖ Additional materials are adapted from various authoritative pronouncements of the IRS.
- ❖ The opinions expressed within, however, are solely the responsibility of the author.



3

Learning Objectives



- ❖ Highlight significant tax changes impacting 2023 and 2024 returns, including:
 - **American Rescue Plan Act of 2021**
 - **Inflation Reduction Act**
- ❖ Discuss the latest **proposed** tax legislation impacting individual and business taxpayers.
- ❖ Provide practical suggestions to help save taxes in today's **extremely** uncertain tax environment.

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2023 Federal Tax Update

Are You Ready for Tax Planning?

There are lots of opportunities to begin the tax planning conversation!

Understanding last years return is a great starting point!



5

Employee Retention Credit

In **Notice 2021-49** IRS applied the related party rules to hold that if the majority owner of a business has any living relatives (other than a spouse) then the owner's wages are **NOT** eligible for the ERC!



6

Employee Retention Credit

Only in the rare situation when the majority owner does not have any living relatives can you use the owner's wages for claiming the ERC



7

Employee Retention Credit

In light of **Notice 2021-49** you should **consider** amending previously filed ERC claims if you included the majority owner's compensation in the calculation!



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2023 Federal Tax Update

Employee Retention Credit

FYI – the ERC statute of limitations is open for **5 years!**

(Not the usual 3)



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Employee Retention Credit

There are a lot of people hustling Employee Retention Credit Claims.

Offering to file amended 941s claiming the credit
In exchange for a percentage of the refund.



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2023 Federal Tax Update

Employee Retention Credit



Department of Employee Retention Credit
Accelerate Tax Notice
New York, NY 10009

Notice: ERIC Employee Retention Credit
Notice Date: 01/13/23
Business Name: [REDACTED]
Proprietor: [REDACTED]
To contact us: 877.515.4433
Your Callor ID: 1026452
Page 1 of 1

Contact us 877.515.4433
(Mon-Fri 8am-5pm EST)

Your notice of pending Employee Retention Tax Credit
Amount of estimated Tax Credit: \$468,000

We are attempting to provide you with an ERC refund estimate that has been instituted by Congress to compensate your business losses due to the COVID-19 pandemic. Please call us immediately to verify your ERC refund estimate.

ERC Estimate Summary	
Business name	[REDACTED]
Estimated tax refund	\$468,000
Estimated employee count	18
Quarterly loss estimate	Pending
Total estimated tax refund due	\$468,000

*Eligibility for all businesses that were affected by COVID-19
*Estimated Tax Credit of up to \$26,000 per employee
*No restrictions on use of tax refund
*Past PPP loan does not affect ERC tax refund

Tax Refund [REDACTED]

Notice: ERIC Employee Retention Credit
Notice date: 01/13/23
SIC Code: [REDACTED]

Tax refunds may be paid in a series of payments made out to [REDACTED] and qualifying businesses may receive their refunds in as little as 5 business days.

Amount of estimated tax credit: **\$468,000**

Department of Employee Retention Credit
New York, NY 10009

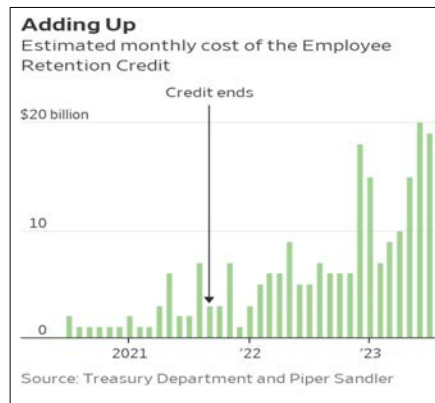
Contact us 877.515.4433
(Mon-Fri 8am-5pm EST)

3663 555553 889335 33109 3378

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Employee Retention Credit

According to the Wall Street Journal, the total cost of the ERC is already 3x Congress' original estimate



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2023 Federal Tax Update

Employee Retention Credit

- ❖ On September 14, the IRS announced an immediate Moratorium on the processing of **new** ERC claims through at least the end of the year.
 - No new claims will be processed until early 2024



Department of the Treasury
Internal Revenue Service

Existing claims will be processed, but with **detailed compliance reviews**

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New IRS Eligibility Flowchart

Part A: Checking your eligibility

This chart can help a business or other organization quickly decide if they may qualify for the Employee Retention Credit. This is a very technical area of the law, but this chart includes the main eligibility factors. Answer these questions in numerical order to see if you may be eligible to claim the ERC.

Eligibility questions	Next steps
1. Did you have employees and pay wages to them between March 13, 2020, and December 31, 2021? For more info, see irs.gov/ercqualified	<ul style="list-style-type: none"> • If yes, go to #2. • If no, you aren't eligible to claim the ERC. If you improperly claimed ERC, see Part C.
2. During that time, were you: <ul style="list-style-type: none"> • A self-employed individual who didn't have employees? • A household employer? 	<ul style="list-style-type: none"> • If yes to either question, you aren't eligible to claim the ERC. If you improperly claimed ERC, see Part C. • If no, go to #3.
3. Did your trade or business experience a significant decline in gross receipts during the eligibility periods during 2020 or the first three calendar quarters (Jan. through Sept.) of 2021? For more info and examples, see the ERC frequently asked questions: irs.gov/ercdecline	<ul style="list-style-type: none"> • If yes, you may be eligible for the ERC. You will need to confirm that your decline in receipts meets requirements. See the ERC frequently asked questions: irs.gov/ercdecline. If you meet the requirements, skip to Part B. • If no, go to #4.
4. Were you a recovery startup business? That's	<ul style="list-style-type: none"> • If yes, you may be eligible for the ERC, but you

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2023 Federal Tax Update

Employee Retention Credit Audits are Beginning!



A hand is shown writing the word "AUDIT" in blue marker on a white surface. A horizontal blue line is drawn under the word.

10:16

Ed Zollars, CPA Retweeted

Dan Chodan @dancho... · 13m

Replying to @cbriancpa

This is an unbelievable level of audits right here.

accounting TODAY

Tax professionals have been seeing clients with legitimate claims also coming under suspicion. The Top 100 Firm Sikich hosted a program earlier this month for financial clients to give an A-to-Z rundown of employee retention credit rules and regulations. It heard a stunning admission from attendees that day during a poll of the participants. Sikich learned a whopping 96% of the attendees who have already applied for and received their company's ERC-related refund now are targets of a nationwide IRS crackdown. IRS audits are underway on 135 of 140 attendees' refund claims. In addition, 58% of respondents said they are being approached daily or weekly by ERC providers offering "claim


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Employee Retention Credit Audits are Beginning!



A hand is shown writing the word "AUDIT" in blue marker on a white surface. A horizontal blue line is drawn under the word.

Department of the Treasury
Internal Revenue Service
SBSSE / Employment Tax
11 SW 1st Avenue, Stop 4448
Miami, FL 33130

Date: 04/04/2023
Taxpayer ID number: [REDACTED]
Form: 941X
Tax periods: Years 2020, 2021
Person to contact: [REDACTED]
Employer ID number: [REDACTED]
Contact phone number: [REDACTED]

Dear [REDACTED]:

Your employment tax return for the year(s) or period(s) shown above has been selected for examination. I have scheduled the following appointment to meet with you regarding this examination.

Date: 05/04/2023 Time: 9:30 am

Place: Interview will be conducted by phone.

What you need to do
Please call me on or before 5/02/2023, to confirm this appointment. You can reach me at the number shown above between the hours of 8:00 am to 4:00 pm. If this date and time is not convenient, please give me a call so that we can schedule a more convenient time.

We understand that the COVID-19 pandemic may present challenges that could impact your ability to effectively prepare for an examination. During our conversation we can discuss any concerns or questions you may have.

To reduce the amount of time spent on this examination, please have available the items listed on the attached Form 4564, Information Document Request, at our scheduled appointment. During our telephone conversation, we will talk about these items so if you have questions, feel free to ask.

Someone can represent you
You may have someone represent you during any part of this examination. If you want someone to represent you, please provide me with a completed Form 2848, Power of Attorney and Declaration of Representative, or Form 8821, Tax Information Authorization, at our first meeting or mail it to me prior to our first appointment. You can get these forms from our office, from our web site at www.irs.gov, or by calling 800-TAX-FORM (800-829-3676). If you decide you want to have someone represent you after the examination has started, we will delay further examination activity until you are able to secure representation.

Your rights as a taxpayer
We have enclosed Publication 1, Your Rights as a Taxpayer, and Notice 609, Privacy Act Notice. We encourage you to read the Declaration of Taxpayer Rights found in Publication 1. This publication discusses general rules and procedures we follow in examinations. It explains what happens before, during, and after an examination, and provides additional sources of information.

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2023 Federal Tax Update

Employee Retention Credit Audits are Beginning!




Please provide the following documentation as it pertains to the 2020 and 2021 employment tax examination discussed on Letter 3850. To facilitate the examination process, please provide documents by the date and method listed below (Excel, or Word are preferred) for the tax credit claimed with a cover sheet explanation in the same order requested below:

1. Copy of worksheets and/or reconciliation used to compute the credits and other amounts included on the employment tax returns (each form 941X) related to the credits.
2. Copy of the original F941 for 3rd quarter year 2020 ending September 30, 2020.
3. A list of employees who were paid wages for which the Employee Retention Credit was claimed.
4. Whether any of the employees who received wages included in the Employee Retention Credit are related individuals.
5. The date and amount of wages paid to each employee for which the Employee Retention Credit was claimed.
6. For large employers, documentation on how the employer determined that the employees were not providing services.
7. Documentation that the business was eligible to claim the Employee Retention Credit (whichever of the following is applicable):
 - a) Documentation with the dates that operations were fully or partially suspended due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19 or a supply chain disruption caused a suspension. Provide a copy of any governmental order in effect during the period July 1, 2020, through September 30, 2020, highlighting the specific provisions of the governmental order causing the full or partial suspension of business operations. (Do not include recommendations by governmental or other authorities or other statutes, orders or other documents that are not related to COVID-19.)
 - b) Documentation that you experienced a significant decline in gross receipts during the calendar quarter for which the Employee Retention Credit was claimed. Provide a complete copy of financial or earning statements detailing the gross receipts for the 3rd quarter of 2020 ending September 30, 2020, as well as for the taxable quarter ending December 31, 2020, March 31, 2021, June 30, 2021, and September 30, 2021. Provide the name(s) of the effected employees, and the amount of wages paid to each worker for each date of the decline in gross receipts.
 - c) Documentation that is a recovery startup business during the calendar quarter for which the Employee Retention Credit was claimed.
8. U.S. Income Tax Return for a Corporation for 2020 and 2021, for information only.
9. Copies of consolidated employment tax returns, and Forms W-2 for related entities (if the business is a member of an aggregated group) for information only.
10. Form 1040, U.S. Individual Income Tax Return for all officers and shareholders for 2020 and 2021. (Include all Schedules), for information only.
11. Copies of State Unemployment Tax Returns for the tax year(s) 2020 and 2021. (all 4 quarters – for information only).
12. Copies of all prior audit reports relating to income or employment by any Federal or State Agencies.

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Employee Retention Credit Audits are Beginning!



Form 4564	Department of the Treasury-Internal Revenue Service	Request Number: 01
INFORMATION DOCUMENT REQUEST		
To: Name of Taxpayer and Company, Division or Branch	Subject: ET Exam: F941X Years 2020 and 2021	
EIN number:	Submitted to:	
Dates of Previous Requests:		

Description of documents requested

13. Are any of the employees who were paid employee retention wages related individuals to a shareholder owning 50 percent of the capital and profits interests in the entity? If yes, please provide name of the employee or employees.
14. Documentation whether the business received forgiveness of a PPP loan (if applicable).
15. Copy of the employer's forgiveness letter received from loan provider and/or SBA (if applicable).
16. Documentation related to any PPP loans and related forgiveness including what wages were included on that loan application. (Include a comparison to show which employee wages made up the PPP loans and which employee wages made up the Employee Retention Credits to ensure there was no overlap).

Information Due by **5/04/2023** at Next Appointment: Mail in or E-FAX

Additional records may be request as the examination progresses.

The applicable corporate officer(s) and shareholder(s) should be present on 05/04/2023, at the initial appointment to answer specific questions about the business operations as well as their specific duties and responsibilities.

If you have any questions, concern about documents requested, please call me at 305-982-5153. The requested documentation may be faxed, mailed, or emailed. See below for instructions.

- For **faxes**, please fax the requested information directly to me at (877) 658-9020.
- For **documentation** you wish to **mail**, please send to the following address:
Internal Revenue Service
51 SW 1st Avenue, STOP 4448
Miami, FL 33130
- For **emails**, please send to ana.perdomo@irs.gov

NOTE: The choice to transmit documents via email is solely that of the taxpayer.

All documents sent via unencrypted email over the internet are not secure. If you choose to send information via email, your emails should only contain minimal identifying information in the subject line and body of the email. The email with attachments to transmit the documents should use password-protected encrypted attachments via Secure Zip or another encryption. The acceptable document types of files must be tiff, jpg, jpeg, pdf, Microsoft Office suite, or Zip. Prior to sending documents to Revenue Agent, please contact by telephone and provided password. Do NOT email password in a separate email.

The taxpayer or representative should include a statement, either in the form of an attached cover letter or within the body of the email to the effect, "The attached [name of document] includes [name of taxpayer]'s valid signature and the taxpayer intends to transmit the attached document to the IRS."

Federal Tax Update
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2023 Federal Tax Update

As are the Criminal Prosecutions!

The IRS is ramping up enforcement and prosecution...

Case 2:23-cr-00128-WSH Document 3 Filed 06/20/23 Page 1 of 8

B177

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

UNITED STATES OF AMERICA } Criminal No. 2:23-cr-128
v. } (18 U.S.C. §§ 1349 and 1344(1))
MATTHEW LLOYD PARKER JR. } [UNDER SEAL]
VIRGINIA R. HUMPHRIES }

FILED
JUN 20 2023
CLERK U.S. DISTRICT COURT
WEST. DIST. OF PENNSYLVANIA

INDICTMENT

The grand jury charges:

INTRODUCTION

At all times material to this Indictment:

1. Defendant MATTHEW LLOYD PARKER JR. (hereafter, "PARKER") was a certified public accountant licensed in the state of Michigan, and was a resident of Detroit, Michigan. PARKER also owned and operated a company located in Detroit, Michigan called "Apollos Management Group, LLC" (hereafter "Apollos").
2. Defendant VIRGINIA R. HUMPHRIES (hereafter, "HUMPHRIES") was a resident of Pittsburgh, Pennsylvania, in the Western District of Pennsylvania and was a small business owner offering credit repair services.
3. Both PARKER and HUMPHRIES solicited, prepared, and applied for pandemic related funds through the Paycheck Protection Program for themselves and for companies located primarily in Pittsburgh and Detroit.

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Employee Retention Credit

- ❖ The IRS is working on a special Withdrawal option for those who have filed a questionable ERC claim
- ❖ And a settlement program for businesses to return improper ERC payments



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2023 Federal Tax Update

Employee Retention Credit

The IRS is rolling out a process for reporting of abusive “ERC mills”

Form 14242 (October 2016)	Department of the Treasury - Internal Revenue Service Report Suspected Abusive Tax Promotions or Preparers	OMB Number 1545-2219
<small>Use Form 14242 to report a suspected abusive tax avoidance scheme and/or tax return preparers who promote such schemes. More information about tax avoidance schemes is available at www.irs.gov/scams. CLAIM FOR REWARD: To claim a reward for providing this information to the IRS, file Form 211, Application for Reward for Original Information.</small>		
<small>Answer the following questions as accurately as possible. Fields on this form have been designed to expand as additional information is entered.</small>		
1. Describe the suspected tax scheme being promoted		
2. How did you become aware of the promotion or promoter (e.g., seminar, internet, email, TV, flyer, newspaper, magazine, friend, relative, etc.)		
3. When did you first learn about the tax promotion (mm/dd/yyyy)		
4. Promoter/Preparer information (if more than one promoter/preparer is involved, provide information on all) Name of Promoter(s)/Tax Preparer(s)		

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\$1T Bipartisan Infrastructure

Infrastructure Investment and Jobs Act

NOT (really) a Tax Act !

- ❖ Employee Retention Credit
- ❖ **Crypto-asset Reporting**
- ❖ Disaster Relief
- ❖ Miscellaneous



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2023 Federal Tax Update

\$1T Bipartisan Infrastructure

Cryptocurrency Reporting

Currently, covered Securities Brokers must report customers names, addresses, adjusted basis and ST or LT gain or loss



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\$1T Bipartisan Infrastructure

Cryptocurrency Reporting



The Infrastructure Act extends the definition of **broker** to “any person who (for consideration) is responsible for regularly providing any service affecting transfers of **digital assets** on behalf of another person.”

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2023 Federal Tax Update

\$1T Bipartisan Infrastructure

Cryptocurrency Reporting

A **digital asset** is “any digital representation of value which is recorded on a cryptographically secured distributed ledger or any similar technology as specified by the” IRS.



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\$1T Bipartisan Infrastructure

Cryptocurrency Reporting



- ❖ The beginning date for basis tracking was ~~January 1, 2023~~
- ❖ 1099-B reporting would start for ~~2023~~
- Returns required to be filed after December 31, ~~2023~~
 - *Filed in 2024 for 2023 activity*

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2023 Federal Tax Update

\$1T Bipartisan Infrastructure

Cryptocurrency Reporting



In Announcement 2023-2 the IRS provided transitional guidance:

- It intends to publish regulations, accept public comments, and issue final regulations
- Brokers may report gross proceeds and basis as required under existing law and regulations as of December 23, 2022
- Brokers will not be required to report or file returns on dispositions of transfers of digital assets until final regulations are issued

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\$1T Bipartisan Infrastructure

Proposed Regs. Issued August 25

- ❖ The beginning date for basis tracking is January 1, **2025**
- ❖ 1099-B reporting would start for **calendar 2025**
 - *Filed in 2026 for 2025 activity*



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2023 Federal Tax Update

\$1T Bipartisan Infrastructure

Cryptocurrency Reporting

Digital assets will now be treated as **cash** for Code Section 60501(a) purposes

- Requiring reporting anytime you (a trade or business) receive more than \$10,000 in **cash/digital assets**
 - *Returns and statements filed after December 31, 2023*

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Form 8300 and Reporting Cash Payments of Over \$10,000

IRS Form 8300 (Rev. August 2014) Department of the Treasury Internal Revenue Service	Report of Cash Payments Over \$10,000 Received in a Trade or Business ▶ See instructions for definition of cash. ▶ Use this form for transactions occurring after August 29, 2014. Do not use prior versions after this date. For Privacy Act and Paperwork Reduction Act Notice, see the last page.	FinCEN Form 8300 (Rev. August 2014) OMB No. 1506-0018 Department of the Treasury Financial Crimes Enforcement Network
1 Check appropriate box(es) if: a <input type="checkbox"/> Amends prior report; b <input type="checkbox"/> Suspicious transaction.		
Part I Identity of Individual From Whom the Cash Was Received		
2 If more than one individual is involved, check here and see instructions <input type="checkbox"/>		
3 Last name	4 First name	5 M.I.
7 Address (number, street, and apt. or suite no.)		6 Taxpayer identification number
9 City	10 State	8 Date of birth (see instructions)
11 ZIP code	12 Country (if not U.S.)	13 Occupation, profession, or business
14 Identifying document (ID)	a Describe ID ▶	b Issued by ▶
	c Number ▶	
Part II Person on Whose Behalf This Transaction Was Conducted		
15 If this transaction was conducted on behalf of more than one person, check here and see instructions <input type="checkbox"/>		
16 Individual's last name or organization's name	17 First name	18 M.I.
20 Doing business as (DBA) name (see instructions)		19 Taxpayer identification number
		Employer identification number

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2023 Federal Tax Update

Form 8300 and Reporting Cash Payments of Over \$10,000

“Generally, if you're in a trade or business and receive more than \$10,000 in cash in a single transaction or in related transactions, you must file Form 8300.

The Form 8300, Report of Cash Payments Over \$10,000 in a Trade or Business, provides valuable information to the Internal Revenue Service and the Financial Crimes Enforcement Network (FinCEN) in their efforts to combat money laundering. Money is "laundered" to conceal illegal activity, including the crimes that generate the money itself, such as drug trafficking, tax evasion and terrorist financing.”

<https://www.irs.gov/businesses/small-businesses-self-employed/form-8300-and-reporting-cash-payments-of-over-10000>

Form 8300 and Reporting Cash Payments of Over \$10,000

When to File

You must file Form 8300 by the 15th day after the date the cash transaction occurred.

Besides filing Form 8300, you also need to provide a written statement to each party whose name you included on the Form 8300 by January 31 of the year following the reportable transaction. This statement must include the name, address, contact person and telephone number of your business and the aggregate amount of reportable cash. The statement must also indicate that you provided this information to the IRS.

Civil and criminal penalties may apply if you fail to file Form 8300 and provide a written statement to each person named on Form 8300. Penalty amounts are adjusted annually for inflation.

2023 Federal Tax Update

Form 8300 and Reporting Cash Payments of Over \$10,000

How to File

Electronic filing. E-filing is a free, quick, and secure method for filing Forms 8300. You may electronically file Forms 8300 using FinCEN's [BSA E-Filing System](#). You'll receive an electronic acknowledgement of each submission. For more information about Form 8300 e-filing, see the [FinCEN news release](#) announcing electronic filing.

Effective April 8, 2019, Form 8300 filers have the option to batch file their reports as opposed to discrete filing. Batch filing is for businesses that file a high number of Forms 8300 at a time. The BSA E-Filing System includes batch processing functionality in XML format. Find more information on batch filing in hot topics and quick links on the [BSA E-Filing System](#), including:

- FinCEN's announcement of XML batch processing for FinCEN Form 8300.
- 8300 XML batch processing technical webinar and
- FinCEN 8300 XML filing requirements.

File by mail. You may mail Form 8300 to the IRS at: Detroit Federal Building, P.O. Box 32621, Detroit, Michigan 48232.

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Form 8300 and Reporting Cash Payments of Over \$10,000

- ❖ On August 30 the IRS announced that Businesses **must e-file** Form 8300 beginning in 2024
- ❖ Applies to any business required to file at least 10 information returns
 - Of any type other than 8300s
- ❖ Set up an Account with FinCen's BSA E-Filing System

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2023 Federal Tax Update

Beware (Previously) Unreported Income!

The image shows a Form 1099-K, 'Payment Card and Third Party Network Transactions' (Rev. 1-2022). The form includes fields for the payee's TIN, gross amount of payment, merchant category code, federal income tax withheld, and a monthly breakdown of transactions. It also has checkboxes for reporting third-party networks and payment cards. A 'Copy B For Payee' section contains important tax information regarding the reporting threshold.

- ❖ Previously the threshold to report third party network transactions was \$20,000/200 transactions a year.
- ❖ Under the American Rescue Plan this was dropping down to **\$600** a year for 2022!
 - Regardless of the number of transactions

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1099-K Reporting

On December 23 the IRS announced a one-year delay



- ❖ Treating 2022 as a transition period
- ❖ Notice 2023-10

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2023 Federal Tax Update

1099-K Reporting

When (if?) this takes effect I suspect it is going to bring a lot of activity to light

- ❖ Gig work
- ❖ Side Hustles
- ❖ Vacation homes & condo rentals
- ❖ Air BNB
- ❖ Roommates
- ❖ Non taxable personal stuff.....

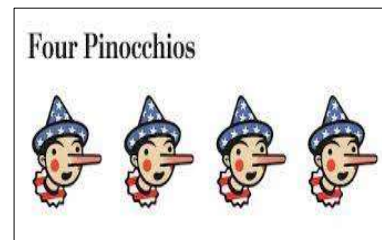


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BBB - Bank Account Reporting

The IRS was pushing (hard) to require financial institutions to report to the IRS the total amount of deposits and withdrawals over \$600/\$10,000

- ❖ Purportedly this would help the IRS focus on **wealthy** tax evaders
- ❖ **No**, This is all about targeting Schedule C, E and F filers



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BBB - Bank Account Reporting

The IRS was pushing (hard) to require financial institutions to report to the IRS the total amount of deposits and withdrawals over \$600/\$10,000

- Purportedly this will help the IRS focus on **wealthy** tax evaders
- *How in the heck do they think they're going to match up all the bank and other financial accounts of "rich" people?*



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FINANCIAL CRIMES



ENFORCEMENT NETWORK

Corporate Transparency Act

BENEFICIAL OWNERSHIP REPORTING

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Corporate Transparency Act



- Enacted as part of the National Defense Authorization Act for Fiscal 2021, it amends the Bank Secrecy Act to require reporting of **Beneficial Ownership**
- The CTA requires many (most) business entities to report their “Beneficial Owners” and “Company Applicants” to the US Treasury Financial Crimes Enforcement Network (“FinCEN”)

Inflation Reduction Act

Signed by President Biden on August 16, 2022



2023 Federal Tax Update

Inflation Reduction Act

Key provisions of the \$739 Billion Act include:

- New Corporate Taxes
- **Extended Premium Tax Credit**
- Prescription Drug Pricing Reform
- **Green Energy Tax Credits**
- IRS Funding



President Gerald R. Ford – Fall 1974

American Rescue Plan Act of 2021

Premium Assistance Tax Credit

The applicable percentage amounts were changed for 2021 and 2022.

- Under prior law you would needed to pay up to 9.83% of household income.
- Under ARPA your premium amount is capped at **8.5%**.



2023 Federal Tax Update

American Rescue Plan Act of 2021

Premium Assistance Tax Credit

- ❖ Previously anyone with income over 400% of the Federal Poverty Line (FPL) was not eligible for Premium Credits
- ❖ For 2021 and 2022 the Credit is available to taxpayers with household incomes in excess of 400% of the FPL

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Premium Tax Credit

Inflation Reduction Act

- Amends Section 36B to extend Premium Tax Credits to taxpayers with household incomes in excess of 400% of the FPL for three more years

2023 through 2025



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2023 Federal Tax Update

Premium Tax Credit



Inflation Reduction Act

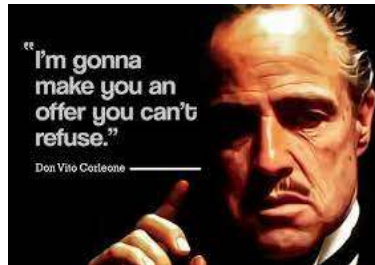
The ARPA 8.5% cap on premiums is also extended for three more years

2023 through 2025

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Drug Pricing

The Act imposes a new excise tax on drug manufacturers who fail to enter into drug pricing agreements



The excise tax ranges from 185.71% to 1,900% of the selected drug's price!

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2023 Federal Tax Update

Green Energy Credits

The Act includes @\$370 Billion in tax credits and other climate change provisions



Goal of reducing greenhouse gas emissions by @40% by the end of the decade

Green Energy Credits

The IRA introduces two new requirements to be eligible to receive the maximum amount for many of the tax credits

1) Compliance with Prevailing wage requirements

(Davis-Bacon Act)

- And Apprenticeship programs

- On November 30, 2022 the IRS issued **Notice 2022-61** provides initial guidance on meeting the Prevailing Wage and Apprenticeship Requirements
- Proposed Regs. were issued on August 30, 2023

Green Energy Credits

The IRA introduces two new requirements to be eligible to receive the maximum amount for many of the tax credits

- 1) Compliance with Prevailing wage requirements (**Davis-Bacon Act**)
 - And Apprenticeship programs
- 2) Domestic Content Requirements



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Home Energy Tax Credits

A promotional graphic for Home Energy Tax Credits. It features a green background with a white house icon on a keyboard, the IRS logo, the text "Home Energy Tax Credits", the URL "IRS.gov/homeenergy", and a QR code.

If you make energy improvements to your home, tax credits are available for a portion of qualifying expenses. The credit amounts and types of qualifying expenses were expanded by the Inflation Reduction Act of 2022.

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Home Energy Tax Credits

Energy Efficient Home Improvement Credit

Qualifying Credit Amounts and Expenses

These expenses may qualify if they meet requirements detailed on [energy.gov](https://www.energy.gov):

- Exterior doors, windows, skylights and insulation materials
- Central air conditioners, water heaters, furnaces, boilers and heat pumps
- Biomass stoves and boilers
- Home energy audits

The amount of the credit you can take is a percentage of the total improvement expenses in the year of installation:

- 2022: 30%, up to a lifetime maximum of \$500
- 2023 through 2032: 30%, up to a maximum of \$1,200 (water heaters, heat pumps, biomass stoves, and boilers have a separate annual credit limit of \$2,000), no lifetime limit

Get details on the [Energy Efficient Home Improvement Credit](#).

*For 2022, biomass stoves and boilers are treated as a Residential Clean Energy Credit with no lifetime maximum.

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Home Energy Tax Credits

Residential Clean Energy Credit

Qualifying Credit Amounts and Expenses

These expenses may qualify if they meet requirements detailed on [energy.gov](https://www.energy.gov):

- Solar, wind and geothermal power generation
- Solar water heaters
- Fuel cells
- Battery storage (beginning in 2023)

The amount of the credit you can take is a percentage of the total improvement expenses in the year of installation:

- 2022 to 2032: 30%, no annual maximum or lifetime limit
- 2033: 26%, no annual maximum or lifetime limit
- 2034: 22%, no annual maximum or lifetime limit

Get details on the [Residential Clean Energy Credit](#).

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Clean Vehicle Credits

Effective on the date of enactment, the tax credit is only available if the vehicle final assembly was in North America



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Clean Vehicle Credits

There is a two-step process to verify final assembly

- First check on the Department of Energy's website listing 2022 and 2023 vehicles that MAY be eligible



<https://afdc.energy.gov/laws/electric-vehicles-for-tax-credit>

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2023 Federal Tax Update

Clean Vehicle Credits



There is a two-step process to verify final assembly

- Second, enter the vehicle's 17 character VIN into the NTSA's VIN Decoder tool and view the "plant information" field

<https://www.nhtsa.gov/vin-decoder>

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Clean Vehicle Credits

Up to \$7,500 **Non-refundable** credit extended thru 2032

- **\$3,750** credit for meeting the battery component requirement
- **\$3,750** credit for meeting the critical minerals requirement



Vehicles placed in service
after **12/31/2022!**

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Clean Vehicle Credits

\$3,750 credit for meeting the battery component requirement

- Beginning in 2023 **50%** of the vehicle's battery must be manufactured or assembled in North America
 - Increasing by 10% per year
 - Hits 100% in 2029



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Clean Vehicle Credits

\$3,750 credit for meeting the critical minerals requirement

- ❖ The battery's critical mineral must be extracted or processed in the US or a country with a free-trade agreement
- ❖ Starts at 40% in 2023
- ❖ Hits 80% in 2027



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2023 Federal Tax Update

Clean Vehicle Credits

The Short List of Eligible EVs

Only 10 models qualify for the full \$7,500 US tax credit

Model	MSRP Limit	EV or Plug-In Hybrid
Chrysler Pacifica	\$80,000	Plug-In Hybrid
Ford F-150 Lightning	\$80,000	EV
Lincoln Aviator Grand Touring	\$80,000	Plug-In Hybrid
Chevrolet Bolt	\$55,000	EV
Cadillac Lyriq	\$80,000	EV
Chevrolet Blazer	\$80,000	EV
Chevrolet Silverado	\$80,000	EV
Chevrolet Equinox	\$80,000	EV
Tesla Model 3	\$55,000	EV
Tesla Model Y	\$80,000	EV

Source: US Treasury Department

Note: Chevrolet Blazer is available summer 2023, and Silverado and Equinox are available fall 2023. Tesla Model 3 Performance qualifies for full credit and Standard Range version is eligible for \$3,750 credit.

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Clean Vehicle Credits



Manufacturer's suggested retail price (MSRP) is limited to **\$55,000** for cars, **\$80,000** for Vans, SUVs & Pickups in 2023

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2023 Federal Tax Update

Clean Vehicle Credits

To claim the credit, the buyer's MAGI must be less than:

- **\$300,000 MFJ**
- **\$150,000 Single**



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Clean Vehicle Credits

Beginning in 2024, the credit can be transferred to the vehicle dealer.....



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2023 Federal Tax Update

Pre-owned Clean Vehicle Credits

There is also a new credit for previously owned clean vehicles:

- ❖ Applies to purchases from a dealer for a price of \$25,000 or less
- ❖ Must be at least 2 years old
- ❖ Credit lesser of \$4,000 or 30% of purchase price
- ❖ MAGI limited to \$150,000 MFJ, \$75,000 Single

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Green Energy Credits

Qualified Commercial Clean Vehicle Credit



**There is also a new credit
for commercial clean
vehicles**

**Vehicles placed in service
after 12/31/2022!**

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Green Energy Credits

Section 30C Alternative Fuel Refueling Credit

- ❖ Credit retroactively extended through 2032
- ❖ Includes bidirectional charging equipment and electric charging stations for 2 and 3 wheel vehicles intended for use on public roads
- ❖ 30% Tax Credit
- ❖ Limited to \$1,000 for residential installations

Green Energy Credits

Section 30C Alternative Fuel Refueling Credit

- ❖ Credit retroactively extended through 2032
- ❖ Beginning in 2023 the maximum credit is increased from \$30,000 to **\$100,000**
 - *Computed per unit, not per location*



2023 Federal Tax Update

IRS Funding

The Act provides an additional \$80 Billion in funding to the IRS

- ❖ Spread over 9 years
- ❖ The current IRS annual budget is @ \$12.7 Billion



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\$80 Billion IRS Funding

- ❖ **\$3.2 Billion** is allocated to improve taxpayer services
- ❖ **\$25.3 Billion** is dedicated to supporting internal IRS operations
- ❖ **\$4.75 Billion** is for modernizing IRS business systems



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2023 Federal Tax Update

IRS Funding

About \$46 Billion (57%) is allocated to tax enforcement!

Enabling the IRS to add approximately 87,000 FTEs
(The IRS currently has @93,000 employees)

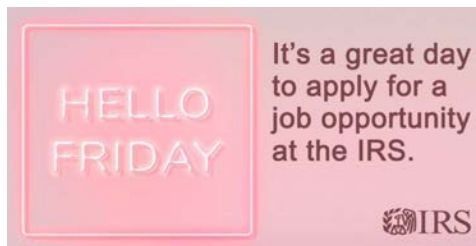
This stadium, at a capacity of 86,112, is not big enough to hold the 87,000 new IRS agents coming after you.



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\$80 Billion IRS Funding

About \$46 Billion (57%) is allocated to tax enforcement!



The increased IRS funding is estimated to bring in an additional **\$200 Billion** in revenue.

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2023 Federal Tax Update

IRS Funding

The Joint Committee on Taxation (JCT) says that 78% to 90% of the money will come from those making under \$200,000 a year

- Only 4-9% will come from those making over \$500,000



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IRS Funding

It's the Tax Accountant's Economic Relief Act!

How are we going to step up – and price – our taxpayer representation services?



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2023 Federal Tax Update

Consolidated Appropriations Act, 2023

The most important tax provision in the Act may be **DIVISION T—**

SECURE 2.0 ACT OF 2022

(Pages 2,000 – 2,349)

Containing a host of changes to retirement savings, RMDs and qualified plan rules - over the next five (5) years

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Secure 2.0 Act

New Saver's Match beginning in 2027

- ❖ 50% “matching contribution” up to \$2,000 for individuals making qualified retirement savings contributions
 - Claimed as a tax credit
 - Not a real match deposited in your account!
 - Phased out for AGI over \$20,500/\$41,000

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2023 Federal Tax Update

Secure 2.0 Act

- ❖ **The \$1,000 Catch-up contribution for IRAs is now indexed for inflation**
 - After 2023
- ❖ **Higher catch-up contributions for ages 60-63**
 - Increased to the greater of \$10,000 or 50% more than the regular catch up (\$5,000 for SIMPLE Plans)
 - *Beginning in 2025*

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Secure 2.0 Act

Permits employers to offer small/deferred financial incentives for employees making salary deferrals



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2023 Federal Tax Update

Secure 2.0 Act

New Pension-linked emergency savings accounts

- ❖ Plans may establish short-term employee savings accounts
- ❖ Roth Accounts of up to \$2,500
 - No minimum contribution or account balance required
 - Must allow for withdrawals at least once a month
 - **NOT** Subject to a 10% penalty!

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Secure 2.0 Act

New penalty exceptions for Qualified plan withdrawals beginning in 2024

- ❖ Personal and family emergencies
 - Up to \$1,000, option to repay within three years
- ❖ Domestic Abuse
 - Up to \$10,000. Self-certification
- ❖ Terminal illness
- ❖ Qualified disasters

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2023 Federal Tax Update

Secure 2.0 Act

New Department of Labor (DOL) lost-and-found database to search for retirement plan accounts



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Secure 2.0 Act

Will allow sole proprietors to make a retroactive first year 401K Plan elective deferral

- Up to the due date - without extension!



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2023 Federal Tax Update

Secure 2.0 Act

New limits on conservation easements

Charitable contributions by pass-through entities limited to 2.5 times sum of each partners/S Corp shareholders basis

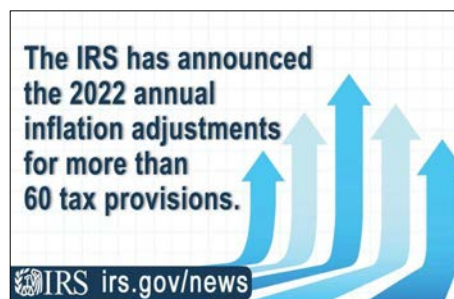


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Tax Cuts and Jobs Act

The Act adopted the **"Chained CPI"** for inflation adjustments.

- *C-CPI-U*



This is a **permanent** change!

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2023 Federal Tax Update

2023 Standard Deduction

Filing Status	Standard Deduction Amount
Single	\$13,850
Married Filing Joint & Surviving Spouse	\$27,700
Married Filing Separately	\$13,850
Head of Household	\$20,800

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2023 Standard Deduction

The TCJA ***keeps*** the additional standard deduction for elderly and blind taxpayers.

- \$1,850 or \$1,500 for 2023
 - *Up \$100 from 2022*



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2023 Federal Tax Update

2023 Tax Brackets

The 0%, 15% & 20% rates for LTCG and Qualified Dividends were retained:

- ❖ 0%
- ❖ 15% starts at \$44,625 / \$89,250
- ❖ 20% starts at \$492,300 / \$553,850



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American Rescue Plan Act of 2021

Child Tax Credit

- ❖ The Child Tax Credit was fully refundable for 2021 **(only)**
 - 17-year-olds were eligible
- ❖ This change was **not** extended by the Inflation Reduction Act!



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2023 Federal Tax Update

2023 Child Tax Credit

*For 2023 the child tax credit remains **\$2,000** per child*



Only \$1,600 is refundable

Up \$1,000 from 2022

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2023 Tax Brackets

Tax Rate	For Single Filers	For Married Individuals Filing Joint Returns	For Heads of Households
10%	\$0 to \$11,000	\$0 to \$22,000	\$0 to \$15,700
12%	\$11,000 to \$44,725	\$22,000 to \$89,450	\$15,700 to \$59,850
22%	\$44,725 to \$95,375	\$89,450 to \$190,750	\$59,850 to \$95,350
24%	\$95,375 to \$182,100	\$190,750 to \$364,200	\$95,350 to \$182,100
32%	\$182,100 to \$231,250	\$364,200 to \$462,500	\$182,100 to \$231,250
35%	\$231,250 to \$578,125	\$462,500 to \$693,750	\$231,250 to \$578,100
37%	\$578,125 or more	\$693,750 or more	\$578,100 or more

Source: Internal Revenue Service Rev. Proc. 2022-38

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2023 Federal Tax Update

Itemizing in 2023 ?

- ❖ You need more than **\$13,850/\$27,700** to itemize
- ❖ More for seniors!
 - *They need \$15,700/\$30,700*



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Itemizing in 2023?

*You need more than **\$13,850/\$27,700** to Itemize
(more for seniors!)*

But...

- ❖ State and Local Taxes capped at \$10,000
- ❖ NO home equity interest
- ❖ NO Miscellaneous Itemized deductions subject to the 2%

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2023 Federal Tax Update

2023 Itemized Deductions

You need more than **\$13,850/\$27,700** to Itemize (more for seniors!)

You need at least **\$3,850/\$17,700** of:

- ❖ Medical Expenses over **7.5% AGI**
- ❖ **Mortgage Interest** Expense (acquisition)
 - And PMI (extended thru 2021)
- ❖ Charitable Contributions

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2023 Itemized Deductions

- ❖ The Tax Foundation estimated that the number of taxpayers itemizing would drop by about 17% under the TCJA.
- ❖ From roughly 30% of all 1040s under prior law.
- ❖ To about 13% of all individual returns.



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2023 Federal Tax Update

§199A Pass-Through Income

There are two limitations on the 20% deduction that apply **only** when your **taxable income** exceeds a threshold amount:

- ~~—\$157,500 Single/\$315,000 MFJ~~
- **\$182,100 Single/\$364,200 MFJ for 2023**
- W2 wage/depreciable asset limit
- Exclusion of specified services

§199A Pass-Through Income

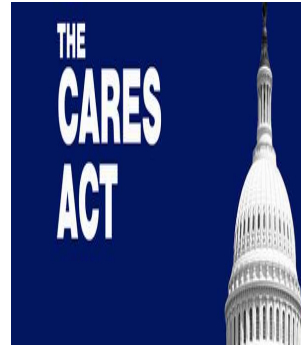
For **Year End Planning**, you should rough out the deduction and check to make sure that there are sufficient W-2 Wages and/or depreciable basis to support the deduction.



2023 Federal Tax Update

CARES Act

- ❖ The TCJA made a couple significant changes **adversely** impacting the tax laws affecting the deductibility of business expenses and losses.
- ❖ The CARES Act temporarily loosened **all three** of these onerous TCJA loss/deduction limitations
 - **Through 2020**



COVID-19 Business Losses

The CARES Act modifications to the TCJA loss limits were only for 2018, 2019 and 2020 tax years



2023 Federal Tax Update

COVID-19 Business Losses

Neither the December 2020 **COVID-Related Tax Relief Act of 2020** nor the March 2021 **American Rescue Plan Act of 2021** nor the August 2022 **Inflation Reduction Act** extended any of these modifications!



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COVID-19 Business Losses

*For 2021, 2022, **2023 and beyond** we're back to:*

- ❖ No NOL Carryback, Carryforward only subject to 80% limitation
- ❖ Section 461(l) cap on business losses
- ❖ Section 163(j) Interest Expense limitation

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2023 Federal Tax Update

TCJA Excess Business Losses

*The Section 461(l) limitation
on business losses returned
in 2021 on Form 461:*



- 2021 \$262,000 single / \$524,000 MFJ
- 2022 \$270,000 single / \$540,000 MFJ
- 2023 **\$289,000 single / \$578,000 MFJ**

101

Maximize IRA & 401K Contributions

- ❖ IRAs **\$6,500** in 2023 (up \$500)
 - Plus \$1,000 age 50 catch up (no change)



*However, Secure 2.0
will start CPI increases
for the catch-up*

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2023 Federal Tax Update

Maximize IRA & 401K Contributions

- ❖ 401(k) **\$22,500** in 2023 (Up \$2,000)
 - *Plus, Age 50 and older \$7,500 catch up (up \$1,000)*



Federal Tax Update

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Maximize IRA & 401K Contributions

SEP IRAs & Solo
401Ks **\$66,000**
(+\$6,000 from 2022)



Federal Tax Update

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2023 Federal Tax Update

2023 Form 1040

Federal Tax Update

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Phone and Email Address?

WHY? I thought the IRS NEVER initiated contact by phone or email....

Federal Tax Update

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Phone and Email Address?

The Form 1040 Instructions now state that entering the phone number and email is

OPTIONAL

(Page 61)

Phone Number and Email Address

You have the option of entering your phone number and email address in the spaces provided. There will be no effect on the processing of your return if you choose not to enter this information. Note that the IRS initiates most contacts through regular mail delivered by the United States Postal Service.

You can report a phone scam to the Treasury Inspector General for Tax Administration at [IRS Impersonation Scam](#)

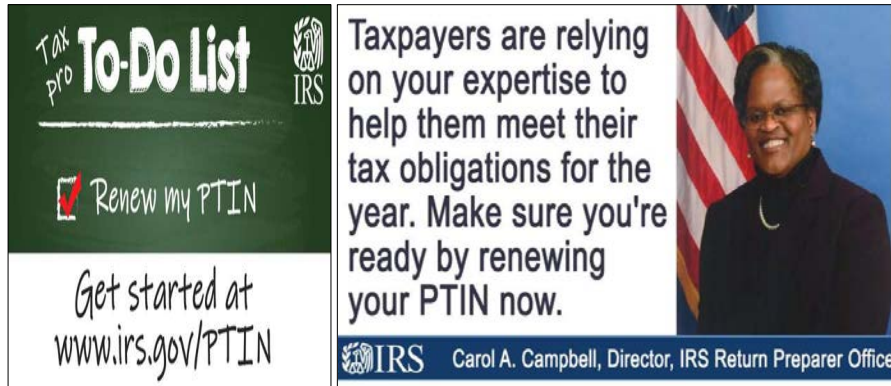
Filing Requirements - PTINs

A Preparer Tax Identification Number (PTIN) is required of **all** paid professionals who prepare or assist in preparing federal income tax returns.

- *Including Form 1041 for Estates & Trusts*



PTIN Renewal



The advertisement features a green chalkboard on the left with the text 'TAX PRO To-Do List' and 'Renew my PTIN' with a checkmark. Below the chalkboard, it says 'Get started at www.irs.gov/PTIN'. On the right, a woman, Carol A. Campbell, is shown in front of an American flag. Text next to her reads: 'Taxpayers are relying on your expertise to help them meet their tax obligations for the year. Make sure you're ready by renewing your PTIN now.' The IRS logo and her name and title are at the bottom.

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PTIN Renewal

- ❖ In October, the IRS announced it was reducing the PTIN Fees to \$19.75
 - \$11 user fee to the IRS
 - \$ 8.75 for the third-party contractor how administers the online process
- ❖ The IRS was forced to reduce its fees after the US District Court in *Steele* held in February that the fees were excessive

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2023 Federal Tax Update

Digital Assets?

The IRS has not revised the language of the 1040 Digital Asset question (yet):



If you checked the MFS box, enter the name of your spouse. If you checked the HOH or QSS box, enter the child's name if the qualifying person is a child but not your dependent: _____

Digital Assets	At any time during 2023, did you: (a) receive (as a reward, award, or payment for property or services); or (b) sell, exchange, or otherwise dispose of a digital asset (or a financial interest in a digital asset)? (See instructions.) . <input type="checkbox"/> Yes <input type="checkbox"/> No
Standard Deduction	Someone can claim: <input type="checkbox"/> You as a dependent <input type="checkbox"/> Your spouse as a dependent <input type="checkbox"/> Spouse itemizes on a separate return or you were a dual-status alien

111

Extenders Bill Failed to Launch



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2023 Federal Tax Update

Expired Tax Provisions

Expired at 12/31/2021:

- ❖ Refundability and enhancement of child and dependent tax credit
- ❖ Increased exclusion for employer-provided dependent care assistance



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Expired Tax Provisions



Expired at 12/31/2021:

- ❖ Charitable contributions by non-itemizers
- ❖ Treatment of PMI as tax-deductible mortgage interest expense

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Expired Tax Provisions

Expired at 12/31/2022:

- 100% deduction for food and beverages provided by a restaurant



100% Bonus Depreciation!

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§168(k) Bonus Depreciation

Then phases it out:

- ➔ ▪ **80% Bonus in 2023 !**
- 60% Bonus in 2024
- 40% Bonus in 2025
- 20% Bonus in 2026
- -0-% in 2027



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Delayed TCJA Provisions

In 2022 two critical changes in the TCJA finally kicked in and took effect:

- ❖ Research and Experimentation costs
- ❖ Interest Expense



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Research & Experimentation



In 2022 the TCJA change from immediate expensing to amortization of R&D costs hit our returns...



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Research & Experimentation

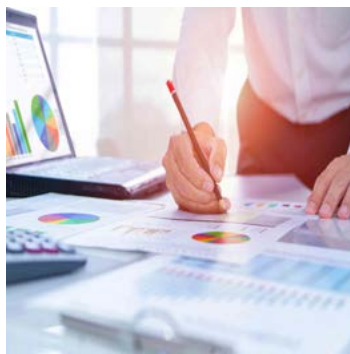
Beginning in 2022 Specified Research and Experimental (SRE) expenses are now to be amortized over:

- ❖ **5 years**
- ❖ 15 years for foreign research



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Research & Experimentation



The IRS issued Rev. Proc. 2023-08 to provide a simplified method to make the change to capitalize research costs

Using a mid-year convention

120

Research & Experimentation

In **Notice 2023-63** the IRS announced coming Proposed Regulations covering:

- ❖ **Capitalization and amortization of SRE Expenditures**
 - Labor, materials and supplies, depreciation or amortization, patent costs and some indirect costs must be capitalized and amortized
 - Some indirect costs such as support services, HR and Payroll do not.
- ❖ Scope of Section 174
- ❖ **Software Development**
 - **Any** amount paid or incurred in connection with the **development of any software** is treated as a research or experimentation expenditure
- ❖ Research provided under contract
- ❖ Disposition, retirement or abandonment of property

§163(j) Business Interest Expense



2023 Federal Tax Update

TCJA

§163(j) Business Interest Expense

Code Section 163(j) limits business interest expense to 30% of **adjusted taxable income**.

- **Tax EBIT**



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§163(j) Business Interest Expense

Until 2022 you were allowed to use:

Tax EBITDA

- ❖ Earnings before Interest, taxes, depreciation and amortization.
- ❖ A critical advantage when using 100% bonus!

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2023 Federal Tax Update

§163(j) Business Interest Expense

I think 2022 will be **brutal!**



- You will still have full 100% bonus
- But no addback under §163(j)!

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§163(j) Business Interest Expense

And it will get worse!

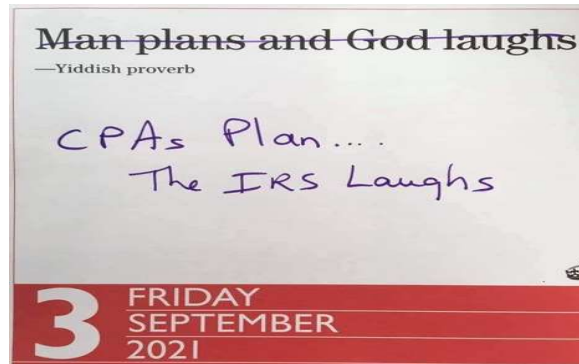


As the Federal Reserve raises interest rates to address inflation, your interest expense will increase

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2023 Federal Tax Update

2023 Year End Tax Planning



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2023 Year End Tax Planning



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2023 Federal Tax Update

2022 Year End Tax Planning

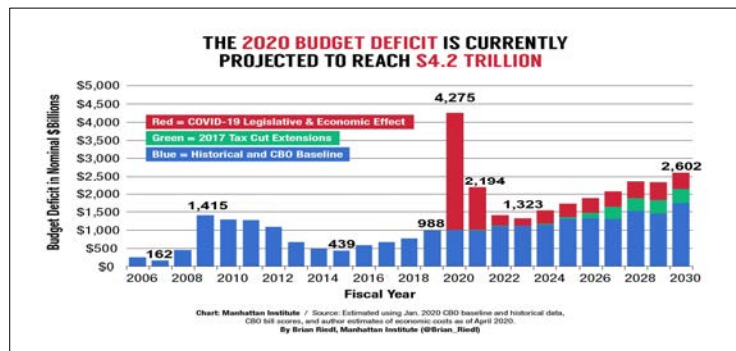
The TCJA has brought us relatively low tax rates for a **limited time** (2018-2025)



Revert back to old law rates in 2026

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2023 Year End Tax Planning



We have massive federal deficits for as far as the eye can see....

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2023 Federal Tax Update

2023 Year End Tax Planning

- ❖ How much exposure to rising tax rates are **you** and your clients willing to absorb?
- ❖ What discount rate are you using for your present value analysis?



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Concluding Thoughts



Doug Van Der Aa
www.vanderaataxed.com
Email: info@vanderaatax.com

Thank You

Follow Doug on Twitter and Facebook!

Twitter: [@AaTaxed](https://twitter.com/AaTaxed)

Facebook: <https://www.facebook.com/vanderaataxed/>

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12:45 – 1:45 p.m.

Charitable Contributions of Property

Robert Teuber, JD, *Shareholder, von Briesen & Roper, s.c.*

Charitable Contributions of Property

ROBERT B. TEUBER, VON BRIESEN & ROPER, S.C.



Robert B. Teuber

robert.teuber@vonbriesen.com

Rob Teuber is a shareholder with von Briesen & Roper, s.c. working out of the Milwaukee and Waukesha offices of the firm. His practice focuses on tax disputes and controversies nationally, regionally and locally with the Internal Revenue Service, Wisconsin Department of Revenue and municipal tax authorities.

In his federal practice, Rob assists clients in efficiently resolving IRS tax examinations of income and employment taxes, challenging Affordable Care Act penalty allegations and addressing international information reporting matters including FBARs and other disclosures. Where issues cannot be resolved in the examination division, Rob frequently works to resolve complicated issues with the IRS Independent Office of Appeals or before the Tax Court.

Rob's state tax practice involves working with the Wisconsin Department of Revenue on income, employment, sales & use and exposition tax audits and appeals through the Resolution Unit. He has successfully represented clients through the Wisconsin Tax Appeals Commission where a satisfactory resolution could not be achieved through the WDOR's administrative process. As with his federal practice, he assists clients in resolving any remaining liabilities in the collection division.

CHARITABLE CONTRIBUTIONS

The Basics

3

The Basics

- IRC §170
 - There shall be allowed as a deduction any charitable contribution payment which is made within the taxable year.

4

The Basics

Who may receive a charitable contribution?

- The United States or any state, the District of Columbia, a U.S. possession (including Puerto Rico), a political subdivision of a state or U.S. possession, or an Indian tribal government or any of its subdivisions that perform substantial government functions.
- Certain war veterans' organizations.
- Certain domestic fraternal societies.
- Certain nonprofit cemetery companies/corporations

5

The Basics

- A community chest, corporation, trust, fund, or foundation organized or created in or under the laws of the United States, any state, the District of Columbia, or any possession of the United States (including Puerto Rico). It must, however, be organized and operated only for charitable, religious, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals. Certain organizations that foster national or international amateur sports competition also qualify.

6

The Basics

- A transfer of money or property must occur.
 - Cash and cash equivalents
 - Stock
 - Real Estate
 - Tangible Personal Property
 - Intangible Property (i.e. patents, royalties)

7

CHARITABLE CONTRIBUTIONS Substantiation

8

Substantiation

Contribution Thresholds:

- Less than \$250
- \$250 or more, but not more than \$500
- \$500 or more, but not more than \$5,000
- \$5,001 but not more than \$500,000
- More than \$500,000
- \$250 or more, but not more than \$500

Contributions of art are subject to different thresholds.

9

Substantiation

Contemporaneous Written Acknowledgement:

- The amount of cash and a description (but not value) of any property other than cash contributed.
- Whether the donee organization provided any goods or services in consideration, in whole or in part, for any property described.
- A description and good faith estimate of the value of any goods or services referred to or, if such goods and services consist solely of intangible religious benefits, a statement to that effect.
- A CWA is contemporaneous if it is obtained on or before the earlier of the date on which the taxpayer files a return for the taxable year in which the contribution was made, or, the due dated (including extensions) for filing such return.
- See *Izen, Jr. v. Comm'r*, 38 F. 4th 459 (5th Cir. 2022)

10

Substantiation

Appraisal Summary

- For non-cash contributions of more than \$500, a Form 8283, Noncash Charitable Contributions, must be submitted with the filed tax return.
- Section A – Donated Property of \$5,000 or Less and Publicly Traded Securities.
- Section B – Donated Property Over \$5,000 (with exceptions).

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Substantiation

Qualified Appraisal

- In the case of contributions of property for which a deduction of more than \$5,000 is claimed, the donor must obtain a qualified appraisal.
- For contributions of more than \$500,000, the qualified appraisal must be attached to the filed tax return.
- Requirements:
 - Must be performed by a Qualified Appraiser.
 - Must include the information required under Treasury Regulation §1.170A-17(a)(3).
- Other issues – substantial compliance and reasonable cause

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Substantiation

Exceptions from Qualified Appraisal Requirements:

- Non-publicly traded stock of \$10,000 or less.
- A vehicle for which the deduction is limited to the gross proceeds of the sale.
- Qualified intellectual property.
- Certain Publicly traded securities.
- Inventory and other corporate donations that are “qualified contributions for the care of the ill, needy or infants.
- Stock in trade, inventory, or property held primarily for the sale to customers in the ordinary course of trade of business

13

CHARITABLE CONTRIBUTIONS Case Studies

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Cryptocurrencies

- A deduction for donated cryptocurrencies is allowed provided the substantiation requirements are satisfied.
 - Must obtain a contemporaneous written acknowledgment for gifts of \$250 or more.
 - Form 8283, Noncash Charitable Contributions must be signed by the charity if greater than \$5,000.
 - Qualified Appraisal. IRS guidance is clear that they consider cryptocurrencies to be property. Therefore, a qualified appraisal is required for contributions in excess of \$5,000.
 - Cryptocurrencies do not qualify for the publicly traded securities or any other exemption from the Qualified Appraisal requirements (at this time).

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Hoensheid v Comm'r, T.C. Memo. 2023-34

Facts:

- Donor contributed a portion of his stock holdings to Fidelity Charitable. Soon after, a 3rd party purchased his remaining stock and that held by Fidelity pursuant to a prearranged transaction.

The Tax Court held:

- The donor must recognize capital gain on the of the stock.
- No charitable contribution deduction is available for the failure to meet the qualified appraisal requirements.

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Hoensheid v Comm’r, **T.C. Memo. 2023-34**

- The donor must recognize capital gain on the of the stock.
 - Anticipatory Assignment of Income
 - “income is taxed to those who earn or otherwise create the right to receive it and that tax cannot be avoided by anticipatory arrangements and contracts however skillfully devised”
 - “A person with a fixed right to receive income from property thus cannot avoid taxation by arranging for another to gratuitously take title before the income is received”
 - The court looked to the substance, rather than form, of the underlying transaction.
 - A donor’s right to income from shares of stock is fixed if a transaction involving those shares has become “practically certain to occur” by the time of the gift despite the remote and hypothetical possibility of abandonment.

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Hoensheid v Comm’r, **T.C. Memo. 2023-34**

- The donor must recognize capital gain on the of the stock.
 - Anticipatory Assignment of Income
 - The record established that the donor’s charitable contribution would not have been made but for the impending sale of the company stock.
 - To avoid an anticipatory assignment of income on the contribution of appreciated shares of stock followed by a sale by the donee, a donor must bear at least some risk at the time of contribution that the sale will not close.
 - The *Hoensheid* case does not establish a bright line rule.

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Hoensheid v Comm’r, **T.C. Memo. 2023-34**

- No charitable contribution deduction is available for the failure to meet the qualified appraisal requirements.
 - The donor’s made a gift in the form of an assignment of income.
 - A charitable contribution is a gift of property to a charitable organization made with charitable intent and without the receipt or expectation of receipt of adequate consideration.”
 - The donor failed to obtain a qualified appraisal.
 - The appraiser was not a “Qualified Appraiser” under the regulations.
 - A sufficient description of the appraiser’s qualifications was not included in the appraisal.
 - The incorrect date of contribution was included in the appraisal.
 - The failure to properly substantiate the contribution was not excused by the doctrines of reasonable cause or substantial compliance.

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Other Challenges to Qualified Appraisals

- Insufficient description of donated property.
- Insufficient description of the condition of the donated property.
- The valuation effective date.
- The fair market value of the property on the valuation effective date.
- The terms of any agreement between donor and donee restricting the use of the property or reserving rights and earmarks for use.
- Information about the qualified appraiser and signature.

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Other Challenges to Qualified Appraisals

- The appraiser's declaration.
- A statement that the appraisal was prepared for income tax purposes.
- A statement that the appraisal was prepared for income tax purposes.
- The method of valuation (i.e. income approach, sales comparison approach, cost approach).
- The specific basis for the valuation.

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Challenges to Valuation

In addition to challenging whether a charitable contribution occurred and whether the substantiation requirements were satisfied, the IRS will often also challenge the valuation made by criticizing:

- the valuation methods relied upon,
- the weight given to a particular method,
- the sales comparisons chosen by the appraiser, or
- the market analysis conducted by the appraiser.

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QUESTIONS?



23

Thank You



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vonbriesen.com/email-sign-up



12:45 – 1:45 p.m.

Practice Management Panel

**Ryan Laughlin, CPA, JD, MST, AEP, Partner, Hawkins Ash
CPAs, LLP**

**Joshua TeBeest, CPA, Shareholder, Tax Service Line Leader,
Huberty**

WICPA Tax Conference

Practice Management Panel

Thursday, November 2, 2023

12:45 p.m. – 1:45 p.m.

quarles.com

Quarles

Presenters

Robert A. Mathers, JD, CPA, ABV, PFS
(Moderator)

Quarles

Joshua TeBeest, CPA
(Shareholder, Vesta CPAs)

Vesta
Accounting | Wealth | Advisory

Ryan Laughlin, JD, CPA, MST, AEP
(Partner, Hawkins Ash CPAs)

HAWKINS | ASH
Part of your business. Part of your life. CPAs

Dealing with IRS

How many IRS agents?



x 1,000!

Can I get just one?



3

Quarles

Dealing with IRS

What will 87,000 agents do?



4

Quarles

Dealing with IRS

Increased IRS Funding

Breakdown of \$80 billion:

- \$45.6 billion for enforcement, which includes examinations, collections, criminal investigations, legal and litigation support, and digital asset monitoring.
- \$25.3 billion for operations support, including legacy information technology systems and telecommunications.
- \$4.8 billion for business systems modernization, including technology to improve customer service.
- \$3.2 billion for taxpayer services, including pre-filing assistance and education, filing and account services, and funding for Taxpayer Advocate Service.



That'll buy you one heck of a pumpkin!

5

Quarles

Minimum Fees –
1040's

- Decrease Work
- Revenue Neutral
- Increase Quality
- Stratification
- But, does this work?



6

Quarles

Outsourcing

- Decrease Work
- Revenue Neutral
- Quality Neutral
- Stratification
- But, does this work?



7

Quarles

Quality Control

-  Inspection Program
-  Elements of Program
-  Artificial Intelligence
-  Other
-  What's Working?



8

Quarles

Tech Stack

- Document Management
- Workflow Management
- Auto Flow – OCI
- Integrations
- What’s Working?



9

Quarles

Text Area

Questions??

Practice Management Panel
Thursday, November 2, 2023
12:45 p.m. – 1:45 p.m.

10

Quarles

Thank You

Robert A. Mathers, JD, CPA, ABV, PFS
(Moderator)

Joshua TeBeest, CPA
(Shareholder, Vesta CPAs)

Ryan Laughlin, JD, CPA, MST, AEP
(Partner, Hawkins Ash CPAs)

quarles.com

The Quarles logo features the word "Quarles" in a white, sans-serif font. A small red square is positioned to the left of the letter "Q", partially overlapping it.

2 – 3 p.m.

IRS Update

Michael Smith, *Senior Stakeholder Liaison, Internal Revenue Service*



2023 IRS Updates for Tax Professionals

November 2023



Who we are:

- Team within IRS that establishes relationships with practitioner and industry organizations representing small business and self-employed taxpayers. We provide information about the policies, practices and procedures the IRS uses to ensure compliance with the tax laws.

What we do:

- Share IRS news and updates
- Education and outreach – (webinars, educational events, etc.)
- Issue Management Resolution System (IMRS) – tell us about IRS issues, we need your feedback!

Find us by searching “Stakeholder Liaison” on IRS.gov





What's New at the IRS in 2023

- Inflation Reduction Act
 - Tax return processing status (backlogs)
 - New clean vehicle and clean energy credits
 - Employee Retention Credit
 - Data Security for Tax Pros
 - Tax Pro Account and Online Account
 - IRS resources for tax professionals
 - Hiring initiatives
-
-



2022 Inflation Reduction Act

- August 16, 2022 – IRA was signed into law. This marked a transformational moment for the Internal Revenue Service – and an opportunity for the future of tax administration.
 - IRS will receive nearly \$80 billion of funding over next 10 years (reduced to ~\$60B)
 - Goals:
 - improve taxpayer service and technology,
 - increase staff,
 - and ensure that all taxpayers are paying their fair share.
-
-



Compliance / Service Transformation

Compliance Transformation:

\$45.6 billion for tax enforcement:

hiring more enforcement agents, providing legal support, and investing in “investigative technology”

Service Transformation:

\$3.2 billion for taxpayer services such as filing and account services, prefilling assistance, and education.





Information Technology Modernization

\$4.8 billion for Business Systems Modernization


- Improving customer service technology (automated callback systems)

The additional funding will enable the IRS to tackle the transformation of core tax systems and address some major pain points for taxpayers, businesses, tax professionals and others.






IRS Inflation Reduction Act Strategic Operating Plan

Internal Revenue Service
Inflation Reduction Act
Strategic Operating Plan
FY 2023-2031

IRS Operations: Status of Mission-Critical Functions – Favorite this IRS.gov Page!



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File Pay Refunds Credits & Deductions Forms & Instructions

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IRS Operations: Status of Mission-Critical Functions

English | [Español](#)

Topics in the News

- Coronavirus Tax Relief
- Economic Impact Payments

News Releases

Multimedia Center

Tax Relief in Disaster Situations

Inflation Reduction Act

Tax Reform

We're processing tax returns, payments, refunds and correspondence. However, we continue to experience delays. We are working hard to get through the inventory.

Our service delays include:

- Processing tax returns that need to be reviewed and corrected
- Answering mail from taxpayers

Check this page periodically for updates.

What You Can Expect

Look at the following list of actions – whether that's sending us your individual or business tax return or answering a letter from us. Then, open the action to see how long you may have to wait and what to do next.

[+ Filed a Tax Return in 2022 \(updated September 25, 2023\)](#)



**IRS Operations: Filed a Tax Return in 2022
(and later)**

Unprocessed Tax Returns	As of Sept. 2023	As of Sept. 2022
Form 1040	945,000	6,900,000
Form 1040-X	894,000	1,600,000
Form 941	9,000	4,000,000
Form 941-X	735,000	199,000



**IRS Operations: Filed a Tax Return in 2022
(and later)**

	As of Sept. 2023	As of Sept. 2022
Answered a letter or notice	20+ weeks	20+ weeks
Applied for an ITIN	1-2 months	N/A
ID Theft (Form 14039)	480 days	N/A





IRS Operations: Need Help

- Phones – 13 minute average wait
- IRS.gov
- Online Account
- IRS.gov/payments
- Interactive Tax Assistant
- Taxpayer Assistance Centers
- Taxpayer Advocate Service (TAS)



Clean Energy Credits





Energy Efficient Home Improvement Credit (§ 25C)

- Homeowners
- Renters
- Second home used as residence

Credits are available for homes that you use as a residence



Energy Efficient Home Improvement Credit (continued)

30% credit, with a \$1,200 annual credit limit for

1. qualified energy efficiency improvements – known as building envelope components
2. residential energy property expenditures made during the year, and
3. home energy audits conducted during the year (maximum of \$150)

30% credit, with a \$2,000 annual credit limit for

1. heat pumps and heat pump water heaters, and
2. biomass stoves and boilers.

The credit is allowed for qualifying property placed in service on or after January 1, 2023, and before January 1, 2033.





Credit for New Clean Vehicles Purchased in 2023 or After (Cont.)

Qualified Vehicles

To qualify, a vehicle must:

- Have a battery capacity of at least 7 kilowatt hours
- Have a gross vehicle weight rating of less than 14,000 pounds
- Be made by a qualified manufacturer.
- Undergo final assembly in North America

Fuel Cell Vehicles (FCVs) do not need to be made by a qualified manufacturer to be eligible. But qualified manufacturers of EVs must also report for their FCVs. See [Rev. Proc. 2022-42](#) for more detailed guidance.



Credit for New Clean Vehicles Purchased in 2023 or After (Cont.)

A list of eligible clean vehicles may be found at federal government's website:

<https://www.fueleconomy.gov/feg/tax2023.shtml>




Energy Efficient Commercial Building Credits





Energy Efficient Commercial Buildings Deduction

Building owners who place in service energy efficient commercial building property (EECBP) or energy efficient building retrofit property (EEBRP) may be able to claim a tax deduction. An increased deduction may be available for increased energy savings or meeting prevailing wage and apprenticeship requirements.

Who Is Eligible

Beginning January 1, 2023, the deduction is available to:

- Owners of qualified commercial buildings
- Designers of EECBP/EEBRP installed in buildings owned by specified tax-exempt

Amount of the Deduction for 2023 and After

For property placed in service in 2023 and after, the deduction for EECBP equals the **lesser** of:

- The cost of the installed property
- or**
- The savings per square foot calculated as:



Employee Retention Credit





Employee Retention Credit scam warning



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/ To protect taxpayers from scams, IRS orders immediate stop to new Employee Retention Credit processing amid surge of questionable claims; concerns from tax pros

To protect taxpayers from scams, IRS orders immediate stop to new Employee Retention Credit processing amid surge of questionable claims; concerns from tax pros

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Topics in the News

News Releases

Aggressive marketing to ineligible applicants highlights unacceptable risk to businesses and the tax system



Employee Retention Credit Information

Bookmark this page for ERC updates:

<https://www.irs.gov/coronavirus/employee-retention-credit>



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Employee Retention Credit

English | [Español](#)

Topics in the News

The Employee Retention Credit (ERC) – sometimes called the Employee Retention Tax Credit or ERTC – is a refundable tax credit for businesses and tax-exempt





Employee Retention Credit scam warning

To report tax-related illegal activities relating to ERC claims, submit by fax or mail a completed **Form 14242**, Report Suspected Abusive Tax Promotions or Preparers and any supporting materials to the IRS Lead Development Center in the Office of Promoter Investigations.



Tax Security Awareness



Signs of Client Data Theft

- Client e-filed returns begin to reject
- Clients who haven't filed tax returns begin to receive authentication letters (5071C, 4883C, 5747C) from the IRS
- Clients who haven't filed tax returns receive refunds



Data Compromise Action Items

Contact IRS and law enforcement

- Tax professionals contact IRS Stakeholder Liaisons immediately
 - Search “stakeholder liaison” on IRS.gov





Data Compromise Actions

Contact State Agencies:

- State revenue agencies – email Federation of Tax Administrators for state agency contacts at StateAlert@taxadmin.org
- State Attorneys General

Contact experts:

- Security expert
- **Insurance company**



Data Compromise Actions - continued

Contact Clients and Other Services

- FTC for guidance for businesses
 - Email: idt-brt@ftc.gov
- Credit Bureaus
- Clients

Review guidance at [IRS.gov/identitytheft](https://www.irs.gov/identitytheft)





Info for affected clients

- IRS Pub 5027, Identity Theft Information for Taxpayers
- Place a “fraud alert” or “credit freeze” with at least one of the three credit bureaus
- File a complaint with the Federal Trade Commission
- Review FTC’s www.identitytheft.gov for additional steps



Develop a Written Information Security Plan

The special plan, called a [Written Information Security Plan or WISP \(PDF\)](#), is outlined in a 29-page document that's been worked on by members of the Security Summit, including tax professionals, software and industry partners, representatives from state tax groups and the IRS.





Reporting phishing emails

Email: phishing@irs.gov

- Forward phishing emails with federal tax related contact to this address.
- Forward phishing text messages to: 202-552-1226

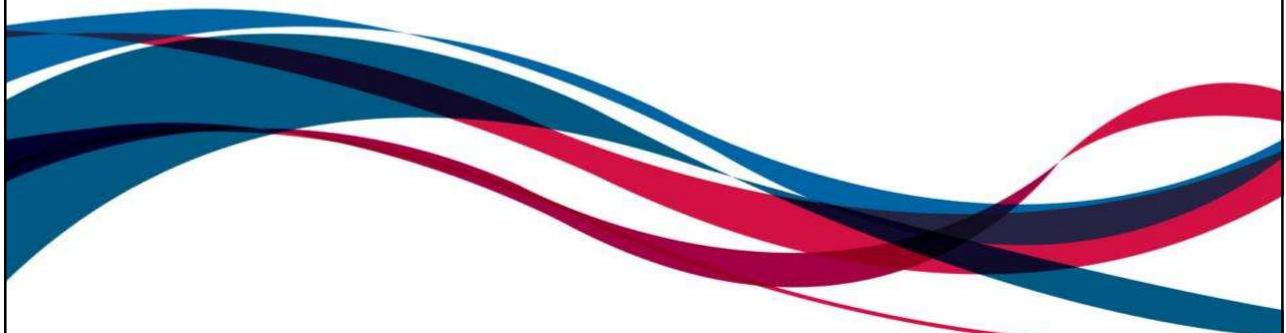
File a complaint with the FBI's IC3

- Search "IC3" or Internet Crime Complaint Center



Office of Online Services

Tax Pro Account





Expanding Services for Taxpayers

Expansion of Taxpayer Options for 3rd Party Authorizations launched in the summer of 2021

- Added “authorization” feature to individual Online Accounts.
- Launched Tax Pro Account on IRS.gov to allow tax professionals to initiate online POA or TIA requests.
 - Tax professional initiates a POA or TIA, uses checkbox as electronic signature for POAs.
 - POA or TIA requests automatically transfers to individual taxpayer’s Online Account.
 - Taxpayer accesses their Online Account and under the “Authorization” tab they can approve the request and use a checkbox as signature.
 - Upon approval, authorization is posted immediately to CAF.

Tax Pro Account



Individual Tax Pro Account Home Page

Notional



JOHN DOE | Profile [↗](#) | [Logout](#)

[Tax Pro Account Home](#) | [Request POA](#) | [Request TIA](#) | [Authorizations](#)

Welcome JOHN DOE

Important Message from the IRS

Tax Professional Account is now ready for you to use to initiate a Power of Attorney or Tax Information Authorization for the taxpayer. Please read the “Before You Start” information to make this process as easy as possible.

[Read less](#)

Request Authorization for an Individual Taxpayer

Submit a request online for power of attorney (POA) or tax information authorization (TIA) for an individual taxpayer. The taxpayer can log in to their IRS account to review and electronically sign the authorization request at www.irs.gov/account.

[REQUEST POA](#)

[REQUEST TIA](#)

Forms 2848 and 8821

You can also submit authorizations with forms: [Form 2848, Power of Attorney and Declaration of Representative](#) or [Form 8821, Tax Information Authorization](#).

Tax Pro Account



Taxpayer Approval of POA Request

Notional

Authorizations

Power of Attorney Approved



Request Approved

John Doe is authorized to represent you before the IRS and receive your confidential tax information for the matters described in this power of attorney.

Your Information

Name: Billy Baker
Address: 1000 Fountain Ave, Paris, GA, 38810

Representative Information

Name: John Doe
CAF Number: XXXX-XXXX
Address: 1111 Kings Ln, Danville, VA, 24541
Declaration of Representative: The representative signed that they are an Attorney who is not suspended or disbarred from practice before the IRS.
Signed by Representative: June 25, 2021

Tax Matters

Tax Matter: Form 1040 Income Tax
Tax Period(s): 2019 - 2019

Notices: The representative will not receive by mail copies of notices and communications the IRS sends you for these tax matters.

Electronic Signature

Signed By Taxpayer: June 23, 2021

Tax Pro Account



Tax Pro Account: Future State

- IRS will continue to expand Tax Pro Account capabilities to improve its features for authorization requests and to add functionality as resources allow.
- Here are just some of the features we are working, planning, or considering:
 - Notification to the taxpayer regarding action in their Online Account, to include pending authorization requests
 - Email alerts letting the tax professional know when taxpayer approves their authorization request
 - Taxpayer's ability to view their complete authorization history.
 - Tax professional's ability to view and manage all their active authorizations on CAF processed through all channels

Tax Pro Account



IRS Resources for Tax Professionals



e-News for Tax Professionals

Information about:

- IRS news releases and announcements
- Upcoming webinars
- Other information of interest to tax pros

Sign up at: www.irs.gov – search keyword “e-News”





IRS social media

Instagram – @IRSnews

Twitter:

[@IRSnews](#)

[@IRSenEspañol](#)

[@IRStaxsecurity](#)

YouTube: IRS Videos in English, Spanish and American Sign Language

Facebook: IRS, IRS en Español, IRS Tax Pros



IRS Webinars

IRS.gov – Search for keyword: **webinars**



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[File](#) | [Pay](#) | [Refunds](#) | [Credits & Deductions](#) | [Forms & Instructions](#)

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Webinars for Tax Practitioners

Individuals

Businesses and Self-Employed

[Small Business and Self-Employed](#)

[Employer ID Numbers](#)

[Business Taxes](#)

[Reporting Information](#)

Upcoming Webinars

- [Qualified Educational Assistance Programs](#) (September 14, 2023)
- [Preparation of Form 1040-NR, U.S. Nonresident Alien Income Tax Return](#) (September 26, 2023)
- [Mortgage & Other Interest Expense Allocation & Apportionment for Individuals with Partnership Interests Form 1116 and Schedule K-3](#) (September 28, 2023)
- [Beneficial Ownership Information](#) (October 4, 2023)

Qualified Educational Assistance Programs

Related Resources

- [Practitioner Local Liaison Meetings and Seminars](#)
- [Tax Practitioner Institute Classes](#)
- [Workshops and Other Events in Spanish for Small Businesses](#)





Stakeholder Liaison

IRS.gov – Search for keyword: **stakeholder liaison**

IRS logo | Search [input] | Help | News | Language | Charities & Nonprofits | Tax Pros

File | Pay | Refunds | Credits & Deductions | Forms & Instructions

Home > File > Businesses and Self-Employed > Small Business and Self-Employed > Stakeholder Liaison Local Contacts

Stakeholder Liaison Local Contacts

English

Individuals

International Taxpayers

Businesses and Self-Employed

Stakeholder Liaison establishes relationships with practitioner and industry organizations representing small business and self-employed taxpayers. We provide information about the policies, practices and procedures the IRS uses to ensure compliance with the tax laws. We also elevate issues that affect tax administration. To establish a relationship with us or report an issue, use this list to find a contact in your state.

Related Topics

- Partners and Stakeholders
- IRS Stakeholder Partners
- Headliners



We are hiring!





Current IRS Job openings

- 275 Job listings open to the public nationwide
- 251 of these are available in Wisconsin

September 20, 2023 announcement: IRS to establish new workgroup to focus on complex partnerships, other key areas

- 3,772 positions open
- \$98,496 - \$158,432 per year
- <https://www.usajobs.gov/job/748385600#>



Where to find job listings

www.jobs.irs.gov

- IRS Career fairs (most are virtual)
- Lists of positions and descriptions

www.usajobs.gov

- Where to apply for jobs





USAJobs.gov tips

- Search “IRS”
- Check “Open to the Public”



USAJOBS Sign in Help Search

Keywords: IRS Location or Remote: City, state, zip, country or type remote Search


Open to the public Remove all filters

Viewing 1 - 25 of 224 jobs Sort by Relevance

Save this search. We'll email you new jobs as they become available.

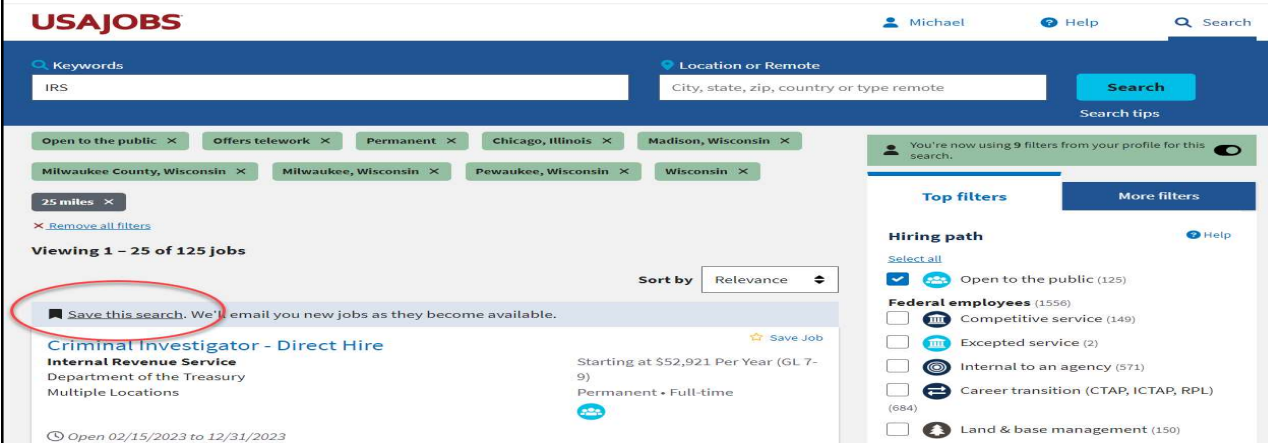
Senior Digital User Experience Analyst - 12 Month Register (Amended)
 Internal Revenue Service
 Department of the Treasury
 Starting at \$136,908 Per Year (GS 15)

Hiring path: Open to the public (224) Federal employees (2221) Competitive service (180)



USAJobs.gov tips

- Select “Save this search”
- You’ll receive e-mail job listings every day



USAJOBS Michael Help Search

Keywords: IRS Location or Remote: City, state, zip, country or type remote Search

Open to the public Offers telework Permanent Chicago, Illinois Madison, Wisconsin Milwaukee County, Wisconsin Milwaukee, Wisconsin Pewaukee, Wisconsin Wisconsin 25 miles Remove all filters

Viewing 1 - 25 of 125 jobs Sort by Relevance

Save this search. We'll email you new jobs as they become available.

Criminal Investigator - Direct Hire
 Internal Revenue Service
 Department of the Treasury
 Multiple Locations
 Starting at \$52,921 Per Year (GL 7-9)
 Permanent • Full-time

Hiring path: Open to the public (125) Federal employees (1,556) Competitive service (149) Excepted service (2) Internal to an agency (571) Career transition (CTAP, ICTAP, RPL) (684) Land & base management (150)



General IRS salaries

Experience levels:

- Recent college grad: GS 7-11 (\$47 - \$60K)
 - Mid-career: GS 11, 12, 13 (\$69 - \$128K)
 - Advanced/specialist: GS 14, 15 (\$116 – \$178K)
 - Management (add 10-20% to these ranges)
-



General IRS salaries

Benefits of federal service:

- 13 paid federal holidays
 - 13 days annual leave + 13 days sick leave
 - Regular annual increases + annual COLA
 - Federal pension upon retirement
 - Most positions qualify for telework
-



Contact information

Michael Smith

IRS Stakeholder Liaison - Wisconsin

211 W Wisconsin Ave, Milwaukee, WI 53203

(414) 231-2199

michael.smith6@irs.gov

- Report issues with IRS policies, practices, procedures
- Help navigating IRS processes
- Presentations/workshops on current IRS issues or tax topics



3:10 – 4 p.m.

Business Transactions & ESOPs

Kenneth Hoogstra, JD, *Shareholder, von Briesen & Roper, s.c.*



The Growing Popularity of ESOPs in Wisconsin

Kenneth A. Hoogstra, Shareholder
von Briesen & Roper, s.c.
kenneth.hoogstra@vonbriesen.com



kenneth.hoogstra@vonbriesen.com

414.287.1376

Ken Hoogstra is a Shareholder and chair of von Briesen's Compensation and Benefits/Executive Compensation Section. He maintains an extensive employee benefits practice including ERISA compliance for group health, welfare and pension plans, and the design and administration of qualified retirement plans and nonqualified deferred compensation plans. Ken places a particular focus on the implementation, design and administration of employee stock ownership plans ("ESOPs"). He also has significant experience working on executive compensation arrangements. Ken has helped defend employers, retirement plans and health care providers in numerous ERISA litigation cases, both at the federal district court and appellate court levels. He is recognized in *The Best Lawyers in America*® in Employee Benefits (ERISA) Law.



Agenda

1. ESOP Basics
2. Pros and Cons
3. Good ESOP Candidates
4. C Corp vs. S Corp
5. Setting Up an ESOP
6. Key ESOP Administration Issues
7. Legal and Ethical Considerations
8. Transactions Involving ESOP-Owned Companies

ESOP Basics

- Qualified retirement plan
 - Subject to qualification rules of Internal Revenue Code
 - Cannot discriminate in favor of highly compensated employees
 - Must be coordinated with other qualified retirement plans of the employer (such as 401(k) plans)
 - Example: Annual additions limits (Code section 415)

ESOP Basics

- Subject to Employee Retirement Income Security Act of 1974 ("ERISA")
 - ESOP usually borrows money to purchase shares from existing shareholders
 - Shares purchased with loan are held in suspense account; as loan is repaid, shares are released and allocated to participants
- Can provide a market for shareholders of privately held companies
 - This is a main reason Congress authorized ESOPs
 - If company is a C Corp, the selling shareholders may be eligible to defer taxes on gain associated with sale ("1042 Rollover"); will be partially available for S Corps in 2028



ESOP Basics

- ESOP may own 100% of company or a lesser percentage
 - ESOP needs to own at least 30% in order for selling shareholders to defer gain on sale of shares to ESOP in a 1042 rollover
 - Not uncommon for ESOP to engage in several purchases of company stock over time
 - Company sponsoring ESOP may decide to contribute shares to the ESOP over time instead of having ESOP borrow money to purchase large block of shares



ESOP Basics

- Subject to Employee Retirement Income Security Act of 1974 (“ERISA”)
 - ERISA’s fiduciary rules significantly impact ESOP transactions and administration
 - ESOP fiduciaries can be held personally liable for breaches of fiduciary duty (*e.g.*, if ESOP pays too much for employer stock)
 - Department of Labor has become increasingly active in challenging valuations for ESOP stock purchases; plaintiffs’ firms also active in bringing lawsuits
 - Following a proper process is critical – DOL has entered into several “process agreements” with ESOP trustees



ESOP Basics

- Some LLCs are not eligible to sponsor ESOPs
 - ESOPs must hold “employer securities”
 - Default tax treatment of an LLC is a tax partnership; ownership interests in tax partnership are not considered “employer securities”
 - LLCs that elect to be taxed as corporations (C Corp or S Corp) may sponsor an ESOP



Pros and Cons for Selling Shareholders

- Pros for Selling Shareholders
 - Ready buyer (often for up-front cash)
 - The business is not being sold to third parties that may alter or eliminate the legacy of the company
 - Can continue to be involved in operation of the business (via employment and board of directors)
 - Seller(s) of C Corp stock may reinvest sale cash in securities and defer tax obligations relating to the sale (§1042 transaction)



Pros and Cons for Selling Shareholders

- Cons for Selling Shareholders
 - ESOP cannot pay more than fair market value for shares
 - Currently no deferral of tax on gains of S Corporation shares (will be partially allowed beginning in 2028)
 - If seller notes are involved, seller(s) take risk of company insolvency; debt will be subordinated to bank debt



Pros and Cons for Company

- Pros for Company
 - Maintain control of the business
 - Long-term ownership succession planning
 - Contributions to the ESOP are tax-deductible (even if ESOP uses the contributions to repay securities acquisition loan)
 - For S Corps, no federal income taxes on corporate income or earnings on shares held by ESOP



Pros and Cons for Company

- Cons for Company
 - Transaction costs
 - Administrative costs and burdens
 - Selling shareholder holdouts
 - ERISA obligations
 - Obligation to pay cash to ESOP participants upon distribution (immediately or deferred)
 - Company debt for leveraged ESOP transaction



Pros and Cons for Employees

- Pros for Employees
 - Tax deferred retirement savings
 - If shares are distributed from ESOP, gains are taxed at capital gains rates (otherwise, ordinary income)
 - Cash distributions can be rolled over to plan or IRA
 - Exclusion of net unrealized appreciation on employer stock included in lump sum distributions
 - Sense of ownership/pride in the company



Pros and Cons for Employees

- Cons for Employees
 - Lack of diversification
 - Possible delayed distributions
 - Company may reduce contributions to other retirement plans in order to make payments on ESOP financing



Good ESOP Candidates

- Strong, stable cash flow and a history of increasing sales and profits
- Selling shareholders want to remain involved in the business
- Selling shareholders are willing to accept a conservative deal, possibly with deferred payments
- Selling shareholders desire to transition ownership of company to employees



Good ESOP Candidates

- Lack of buyers willing to pay significant premium for company
- More than 25 employees
- Transaction size exceeds \$1,000,000
- Senior management supports the ESOP formation
- Company has room to make deductible contributions sufficient to support ESOP debt service



C Corp vs. S Corp

- 1042 rollover
 - Selling shareholders of C Corp shares can defer taxation of gain on sale, provided certain conditions are met; not yet available for selling shareholders of S Corp
- Deduction limits
 - In general, contributions to a defined contribution plan are deductible up to 25% of participant compensation
 - For C Corp, a separate 25% of compensation limit applies for contributions used to pay principal on securities acquisition loan; contributions to pay interest are fully deductible



C Corp vs. S Corp

- Corporate taxation differences
 - S Corp that establishes ESOP not only avoids corporate tax, but ESOP trust does not pay tax on amounts contributed to it or on growth of investments
- Participants' right to demand employer stock in C Corp
- Annual additions (Code section 415 limits)
 - Participant's annual additions may not exceed lesser of 100% of compensation or a specific dollar amount (\$66,000 in 2023)
 - For C Corp, contributions to ESOP to pay interest on securities acquisition loan and certain forfeitures do not count



C Corp vs. S Corp

- Nonallocation rules
 - S Corp: if “disqualified persons” own more than 50% of the company’s stock, they may not receive an ESOP allocation or hold company stock or related assets in an ESOP (Code section 409(p))
 - “Disqualified person” is one who owns at least 10% of Company shares, or 20% with family members
 - In determining ownership, shares allocated to a participant’s ESOP account are counted, as are a proportionate number of unallocated shares and “synthetic equity”
 - Violation of 409(p) will cause ESOP loan to be a prohibited transaction and will cause company income received by ESOP to be taxable
 - No correction for 409(p) violation – prevention is critical
 - C Corp: No allocation to shareholders who elected 1042 rollover (or their family members)



Setting up an ESOP

- Overview of Major Steps
 - Initial valuation and feasibility study for company
 - Decide key transaction parameters
 - Company engages independent ESOP trustee
 - Trustee engages valuation firm and legal counsel
 - Trustee due diligence
 - Negotiate letter of intent



Setting up an ESOP

- Overview of Major Steps (*continued*)
 - Prepare transaction documentation (e.g., stock purchase agreement, stock pledge agreement, loan agreements with bank and/or selling shareholders)
 - Prepare plan documentation (e.g., ESOP plan document and trust agreement)
 - Prepare ancillary documents (e.g., employment agreements, non-compete agreements, revised related-party contracts, amendments to credit agreements)
 - Prepare corporate documents (e.g., stock split, recapitalization, revised Bylaws/Operating Agreement)
 - Closing
 - Post-closing tasks (e.g., summary plan description, IRS determination letter)



Setting up an ESOP

- Common ESOP Transaction Structures: Bank-Financed
 - Typically involves bank loan to company (“External Loan”) and company loan to ESOP (“Internal Loan”)
 - Terms of External Loan and Internal Loan need not be identical
 - Shares purchased by ESOP with Internal Loan are placed in suspense account in ESOP
 - ESOP’s repayment of Internal Loan triggers annual release of shares from suspense for allocation to participants



Setting up an ESOP

- Common ESOP Transaction Structures: Seller-Financed
 - Shareholder(s) sell shares to company in exchange for seller note(s) (External Loan(s))
 - Company simultaneously sells shares to ESOP in exchange for note from the ESOP (Internal Loan)
 - Terms of External Loan and Internal Loan need not be identical
 - Shares purchased with Internal Loan are placed in suspense account in ESOP
 - ESOP's repayment of Internal Loan triggers annual release of shares from suspense for allocation to participants



Setting up an ESOP

- Common ESOP Transaction Issues
 - Deal price is generally conservative
 - Indemnification from selling shareholders
 - Employment/non-compete agreements with key employees
 - Clawbacks
 - Implementation of independent board of directors



Key ESOP Administration Issues

- Internal loan repayment and share release/allocation
- Annual valuation
- Annual testing (coverage, discrimination, 409(p), etc.)
- Coordination with other retirement plans
- Diversification requirements
- Distributions – cash or stock; put rights
- Repurchase liability forecasting



Legal and Ethical Considerations

- ESOP Transactions
 - ERISA fiduciary considerations
 - Who represents the selling shareholders?
- After ESOP is Established
 - Corporate governance – relationship between ESOP trustee and company's board of directors
 - Corporate vs. ESOP counsel



Transactions Involving ESOP-Owned Companies

- Second-Stage ESOP Transactions
 - Redemption by company vs. sale to ESOP
 - Price protection for ESOP participants
- Acquisitions by ESOP-Owned Companies
 - Fiduciary duties of directors vs. ESOP trustee
 - Coverage of target's employees after closing



Transactions Involving ESOP-Owned Companies

- Sale of ESOP-Owned Companies
 - Stock sale vs. asset sale and role of ESOP trustee & participants
 - Treatment of unallocated shares
 - Status of ESOP after sale
- Unsolicited Offers
 - Duties of management, board, ESOP trustee
 - Adoption of unsolicited offer policy



QUESTIONS?



Thank You



Kenneth A. Hoogstra

kenneth.hoogstra@vonbriesen.com

414.287.1376

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von Briesen's
Law Updates by visiting:

vonbriesen.com/email-sign-up



3:10 – 4 p.m.

Qualified Appraisals (Valuations) for Tax Reporting Purposes

Mark Heroux, JD, Tax Partner, Baker Tilly

Bruce Hutler, CFA, ASA, CVA, Partner, Baker Tilly

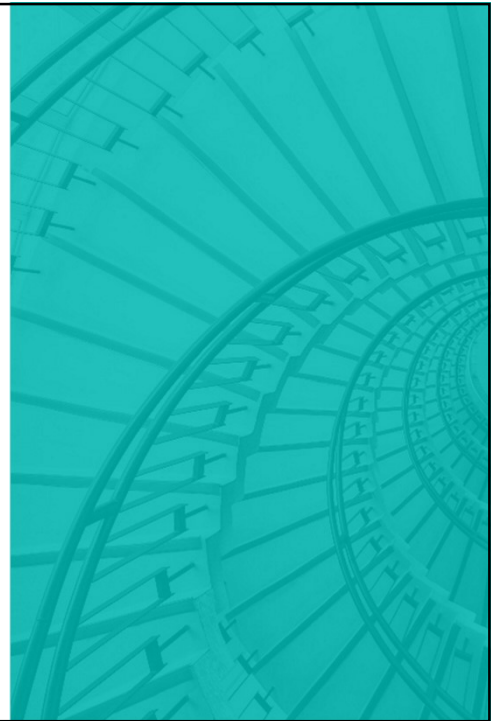


Qualified Appraisals (Valuations) for Tax Reporting Purposes

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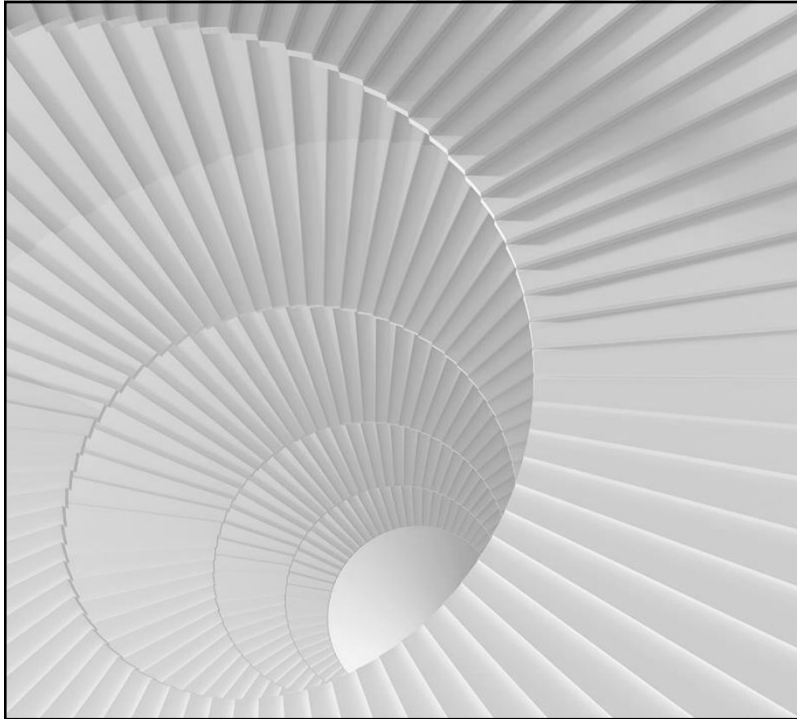
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Bruce Hutler, CFA, ASA, CVA

Mr. Hutler is a Partner at Baker Tilly US, LLP, and has been active in all aspects of business valuation and financial analysis on a full-time basis for over thirty years completing thousands of valuations. Mr. Hutler holds a Master of Business Administration degree with a major in Finance, Investment, and Banking from the University of Wisconsin - Madison and a Bachelor of Business Administration degree with majors in Finance and Real Estate from the University of Wisconsin - Milwaukee.





Mark Heroux, JD

Mr. Heroux has more than 35 years of tax litigation, technical and program management experience. Mark specializes in IRS procedures, controversy and dispute resolution. He began his career with the IRS Chief Counsel in 1985 where he litigated cases around the world for the IRS. When Mark left the IRS in 2000, he was a Department of Justice Special Assistant United States Attorney, industry counsel for the nation for the insurance industry, and a senior trial attorney who helped litigate the two largest transfer pricing cases in history. At Baker Tilly, he leads the IRS Practice and Procedures group and provides tax and business advisory services to middle-market and large companies and high-net-worth individuals.

3



Overview

- **What is required to be considered a qualified appraisal for tax reporting purposes**
- **Questions you should be asking the appraiser**
- **Reasons why a qualified appraisal would be necessary**
- **Situations in which your client would need a qualified appraisal**
- **What you and your clients should expect from a qualified appraisal**

4



Qualified Appraisals and Appraisers

Definition of Value

For estate and gift tax purposes, assets must be valued at *fair market value*. Section 20.2031-1(b) of the Estate Tax Regulations and Section 25.2512-1 of the Gift Tax Regulations define *fair market value* as follows:

“ . . . the price at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts.”

Qualified Appraisals and Appraisers

The IRS issued guidance relating to the definitions of *qualified appraiser* and *qualified appraisal* for charitable contributions of non-cash property.

- An appraisal should be conducted in accordance with generally accepted appraisal standards.
- The Uniform Standards of Professional Appraisal Practice (USPAP) is an example of accepted standards.



Qualified Appraisals: Valuation Standards

- The Appraisal Foundation: *Uniform Standards of Professional Appraisal Practice*
- American Institute of Certified Public Accountants: *Statement on Standards for Valuation Services*
- American Society of Appraisers: *Business Valuation Standards*
- National Association of Certified Valuation Analysts and Institute of Business Appraisers: *Professional Standards*
- Internal Revenue Service: *Business Valuation Guidelines*



Qualified Appraiser

The requirements will be treated as met if the appraiser:

- Earned an appraisal designation from a recognized professional appraiser organization;
- Regularly performs appraisals for which the individual receives compensation;
- Successfully completed college or professional-level coursework relevant to the appraised property
- Obtained at least two years of experience in the trade or business of buying, selling, or valuing the type of property under appraisal; and
- Included in the appraisal a full description of his or her education and experience that qualifies him or her to value the type of property being appraised.

IRC Sec. 170(f)(11)(E)(ii); Reg. 1.170A-13(c)(5); IRS Notice 2006-96



Questions To Ask the Appraiser

- What professional designations do you hold that relate to business valuation?
- What experience do you have that qualifies you to value the type of property being appraised?
- What adjustments did you make or consider making to the Company's financial information and why?
- What did you learn about the Company on your site visit and interviews?
- What industry information did you use and how did it impact your conclusion of value?
- What valuation methods did you consider/use and why?



Questions To Ask the Appraiser

- Did management provide you with cash flow projections and if so, did you use them?
- Did you consider historical earnings and if so, how did you use them?
- Were you able to find any comparable transactions? If so, how did you select the multiple to apply to the company?
- What discounts did you consider (e.g., lack of control, lack of marketability, lack of voting rights, trapped in capital gains).
- What sources of information did you use to support the discounts?
- What does your conclusion of value imply as a multiple of historical or future earnings? Is it reasonable and supportable?

Adequate Disclosure for Gifts

Adequate Disclosure for Gifts

The IRS's rules set forth in Treasury Regulations Section 301.6501(c)-1(f)(3), published December 3, 1999, apply to all gifts made after August 5, 1997

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Adequate Disclosure for Gifts

- The IRS is precluded from revaluing gifts if the gift was adequately disclosed on the gift tax return and the statute of limitations for the gift tax return has expired.
- This rule also prevents the IRS from revaluing gifts when reporting adjusted taxable gifts on estate tax returns.

Reg. 301.6501(c)-1(f)

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Adequate Disclosure for Gifts

For gift tax purposes, qualified appraisers and qualified appraisals are defined similarly in the regulations, but with additional requirements or restrictions.

Reg. 301.6501(c)-1(f)(3)

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Adequate Disclosure for Gifts

- To meet the adequately disclosed requirement, regulations require taxpayers to furnish extensive information with the gift tax return to cause the statute of limitations to begin.
- Instead of the information listed in the regulations, the donor may submit an appraisal of the transferred property prepared by a qualified appraiser.

Regs. 20.2001-1; 25.2504-2; and 301.6501(c)-1(e) and (f)

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Adequate Disclosure for Gifts

The appraiser must meet the following requirements:

- The appraiser is an individual who holds himself or herself out to the public as an appraiser or performs appraisals on a regular basis.
- The appraiser is qualified to make appraisals of the type of property being valued. This requirement is satisfied by a detailed description of the appraiser's background, experience, education, and membership, if any, in professional appraisal associations.
- The appraiser is not (a) the donor or donee of the property, (b) a family member of the donor or donee, or (c) any person employed by the donor, donee, or member of the family of either.

Reg. 301.6501(c)-1(f)(3)

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Adequate Disclosure for Gifts

The appraisal must contain the following:

- Date of the transfer
- Date on which the property was appraised (appraisal date)
- Purpose of the appraisal
- Description of the property
- Description of the appraisal process, including the valuation method(s) considered and/or used
- Description of the assumptions relied upon or any hypothetical conditions

Reg. 301.6501(c)-1(f)(3)

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Adequate Disclosure for Gifts

The appraisal must contain the following:

- Descriptions of any limiting conditions and restrictions on the transferred property that affect the analyses, opinions, and conclusions
- Information considered in determining the appraised value, including all financial information that was used in sufficient detail to allow another to replicate the appraisal process and arrive at the appraised value
- Appraisal procedures followed, and the reasoning that supports the analysis, opinions, and conclusions

Reg. 301.6501(c)-1(f)(3)

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Adequate Disclosure for Gifts

The appraisal must contain the following:

- Valuation method utilized, the rationale for the valuation method, and the procedure used in determining the fair market value of the asset transferred
- Specific basis for the valuation, such as specific comparable sales or transactions, sales of similar interests, asset-based approaches, merger-acquisition transactions, etc.

Reg. 301.6501(c)-1(f)(3)

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Appraiser Penalty

Appraiser Penalty

- The Pension Protection Act of 2006 granted the IRS powers to sanction individuals who perform valuations for any tax purposes, including estate, gift, and income taxation.
- If a person prepares a property appraisal, and knows (or reasonably should have known) that the appraisal would be used in connection with a return or a claim for refund, that person is subject to a penalty if the claimed property value results in a substantial estate or gift tax valuation misstatement under IRC Sec. 6662(g) or a gross estate or gift tax valuation misstatement under IRC Sec. 6662(h) for the property.



Appraiser Penalty

- Penalties for negligence
- Substantial valuation misstatement
- Substantial estate or gift tax valuation understatement (under Internal Revenue Code section 6662)
- Understatement of reportable transactions (under Internal Revenue Code section 6662A)

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Appraiser Penalty

The amount of the penalty equals the lesser of (IRC Sec. 6695A):

- the greater of: (a) 10% of the underpayment; or (b) \$1,000; or
- 125% of the gross income received by the appraiser for the appraisal services.

No penalty will be imposed if the appraiser establishes that the appraised value was “more likely than not” the proper value. Unless the appraiser can satisfy the “more likely than not” standard, the IRS must impose a penalty.

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IRS Issues

Burden of Proof

IRC Sec. 7491 provides that if a taxpayer presents credible evidence regarding any factual issue relevant to determining the estate, gift, or generation-skipping transfer taxes, the IRS will have the burden of proof with respect to such an issue.



Common Gift & Estate Audit Issues

- Standard of Value
 - ❖ Fair market value
 - ❖ Hypothetical buyer and seller
 - ❖ Consider both buyer and seller
- Discounts
 - ❖ Failure to support the discounts selected
- Tax-Affecting
 - ❖ Failure to address and support position
- Illogical Conclusion
 - ❖ Conclusion not supported based on the data
- Subsequent Events

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Important Recent Valuation Cases

- Cecil v. Commissioner
- Nelson v. Commissioner
- Warne v. Commissioner
- Grieve v. Commissioner
- Kress v. United States

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Questions?



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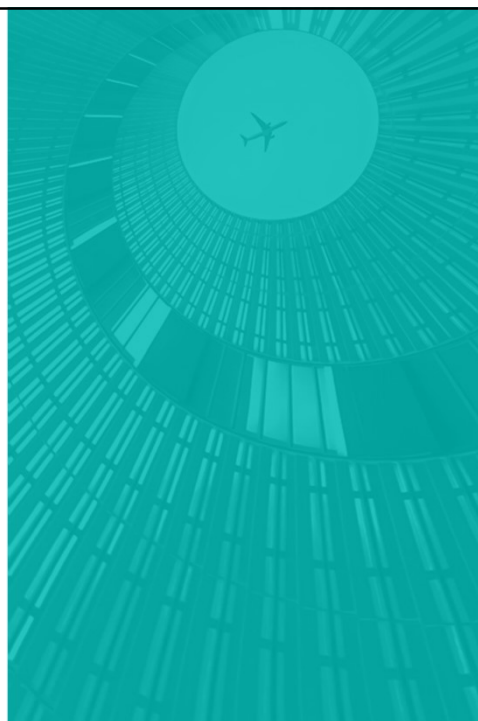


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3:10 – 4 p.m.

Sec. 83 Overview & Issues

Kieran Coe, JD, *Attorney, Godfrey & Kahn S.C.*

Timothy Smith, JD, *Tax Attorney, Godfrey & Kahn S.C.*

Code Section 83 – Equity Compensation Risks and Considerations

November 2, 2023

Kieran Coe & Tim Smith

GODFREY  KAHN_{SC}

MILWAUKEE | MADISON | GREEN BAY | APPLETON | WASHINGTON, D.C.

Code Section 83

- ▶ “If, ***in connection with the performance of services***, property is ***transferred*** to any person other than the person for whom such services are performed, the excess of— (1) the ***fair market value*** of such property . . . Over (2) the amount (if any) paid for such property, shall be included in the gross income of the person who performed such services in the first taxable year in which the rights of the person having the beneficial interest in such property . . . are not subject to a ***substantial risk of forfeiture***, whichever is applicable.”

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Section 83

- ▶ Types of common property—Stock (granted outright or purchased (e.g., exercise of option)), Restricted Stock, or Capital Interests in an LLC)
- ▶ When does it apply?
 - ▷ It applies when there is a *compensatory* transfer of property.
- ▶ What does it do?
 - ▷ Governs the taxation of such transfers.
 - ▶ Property transferred in connection with the performance of services is taxed when it has been transferred to the service provider and has become substantially vested (**no longer subject to a “substantial risk of forfeiture” (“SRF”)**). * See Treas. Reg. §1.83-1(a)(1).

*Assumes no Section 83(b) election.

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Section 83 SRF

- ▶ What is the significance of a SRF?
 - ▷ The presence of a SRF determines when an individual will be taxed in connection with the receipt of the property.
 - ▶ Example (Assumes no Section 83(b) election)
 - ▷ Facts
 - ▶ Assume restricted stock is transferred to an employee at no cost which will only vest if the employee remains employed with the company in year 3, or, if sooner, upon a change in control of the company.
 - ▷ Result
 - ▶ Employee will be taxed, at ordinary income rates, on the fair market value (“FMV”) of the shares in year 3, or, if earlier, a change in control.

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Section 83(b) Election

▶ What is it?

- ▷ A mechanism provided by the Internal Revenue Code and Treasury regulations to elect immediate taxation of transferred property (**30 days after transfer**).

▶ Benefits of an Election?

- ▷ The future appreciation in the property's value after the date of grant will be taxed at preferential capital gains rates.
- ▷ Especially beneficial with property that has a low (i.e., \$0.01 (e.g., start-ups)) FMV at time of transfer.

▶ Potential Downsides?

- ▷ No deduction above the amount paid for property that is forfeited prior to vesting, or depreciation in value of property.

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Section 83(b) Election and Pass-Throughs

▶ Other than attempting to capture appreciation as a capital gain, a Section 83(b) election is important to properly treat employees as owners/partners for allocation and distribution purposes.

- ▷ S-Corporations (Treas. Reg. Section 1.1361-1(b)(3)) (*Estate of Arthur E. Kechijian v. Commissioner*, No. 18-2277 (4th Cir. 2020)); and
- ▷ LLCs and Partnerships (*Crescent Holdings, LLC v. Commissioner*, 141 T.C. No. 15)

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Section 83- How it Works

Grant of Restricted Stock					
Date	Fair Market Value Per Share	Number of Shares	Total FMV	Regular Section 83 Taxation	Taxation With 83(b) Election
Grant (Year 1)	\$1	5,000	\$5,000	\$0	\$1,850 37% (\$5,000)
Vesting (Year 3)	\$20	5,000	\$100,000	\$37,000 37% (\$100,000)	\$0
Sale (Year 5)	\$25	5,000	\$125,000	\$5,000 20% (\$25,000)	\$24,000 20% (\$120,000)
Total Tax				\$42,000	\$25,850

37%-Ordinary Income Tax Rate; 20% Capital Gain Tax Rate; Grant at \$0 cost

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Section 83 SRF Definition

- ▶ When is there a SRF?
 - ▷ "...whether a risk of forfeiture is substantial or not depends upon the facts and circumstances." Treas. Reg. §1.83-3(c).
 - ▷ "a [SRF] exists only if rights in property that are transferred are conditioned, directly or indirectly, [1] upon the **future performance** (or refraining from performance) **of substantial services** by any person, or [2] upon the occurrence of a **condition related to a purpose of the transfer** if the possibility of forfeiture is substantial." Treas. Reg. §1.83-3(c).

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Substantial Future Services

- ▶ Regulations provide factors to determine whether future services are substantial:
 - ▷ Regularity of performance of services
 - ▷ Time spent in performing such services
 - ▷ Ability to decline performance without forfeiture
- ▶ Examples
 - ▷ Example 1 (Does Create a SRF)
 - ▶ Transferred Property vests in full in 3 years or vests 1/3 per year only if employee remains a full-time employee during the relevant period.
 - ▷ Example 2 (Does Not Create a SRF)
 - ▶ A company transfers property to independent contractor that vests in three years if independent contractor is "on call" to perform services for the company. Independent contractor can refuse to perform and not forfeit property.

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Condition Related To A Purpose Of The Transfer

- ▶ Example
 - ▷ A company valued at \$5 million transfers restricted stock to an employee that vests only on a change in control where the company is valued at \$10 million regardless of whether the employee remains employed with the company.
 - ▷ Recall, "upon the occurrence of a condition related to a purpose of the transfer **if the possibility of forfeiture is substantial.**" Treas. Reg. §1.83-3(c).

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SRF Does Not Exist

- ▶ A SRF does not exist (i.e., no delayed taxation) when:
 - ▷ Enforcement of forfeiture condition is unlikely,
 - ▷ Transferor must pay transferee the FMV of forfeited property upon forfeiture,
 - ▷ The only risk is that property value is subject to a risk of decrease in value,
 - ▷ Property is subject solely to a nonlapse restriction,
 - ▷ Property is subject solely to a transfer restriction, or
 - ▷ Property is only forfeited on termination for “Cause”

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Enforcement Is Unlikely

- ▶ “Property is not transferred subject to a [SRF] if at the time of transfer the **facts and circumstances demonstrate that the forfeiture condition is unlikely to be enforced.**” Treas. Reg. §1.83-3(c)(1).
- ▶ Practice Tip:
- ▶ A pattern of waiving vesting conditions is problematic because it tends to show a lack of enforceability at time of transfer.
- ▶ In addition, please note that regulations provide special rules for determining likelihood of enforcement when a transfer of property is made to an employee that owns a significant amount of the total combined voting or value of a corporation. See Treas. Reg. §1.83-3(c)(3)

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Payment For Forfeited Property

- ▶ “Further, property is not transferred subject to a [SRF] to the extent that the **employer is required to pay the fair market value** of a portion of such property to the employee **upon the return of such property.**” Treas. Reg. §1.83-3(c)(1).

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Nonlapse Restriction

- ▶ “A nonlapse restriction, standing by itself will not result in a [SRF].” Treas. Reg. §1.83-3(c)(1).
- ▶ Nonlapse Definition
 - ▷ “A restriction which **by its terms** will never lapse” and is “[a] permanent limitation on the transferability of property—(i) which will require the transferee to sell, or offer to sell, such property at a price determined by a formula, and (ii) which will continue to apply to and be enforced against the transferee or any subsequent holder (other than the transferor)”
 - ▶ Right of first refusal with a set price is a nonlapse restriction.

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Transfer Restrictions

- ▶ Restrictions on transfer of property generally do not create a SRF.
 - ▷ One Limited Exception to Transfer Restriction Rule:
 - ▶ Where transfer could subject individual to liability under §16(b) of the Securities Exchange Act of 1934

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Cause

- ▶ Risk of forfeiture upon termination for “Cause” does not create a SRF.
 - ▷ “On the other hand, requirements that the property be returned to the employer **if the employee is discharged for cause or for committing a crime** will **not be** considered to result in **a substantial risk of forfeiture**.” Treas. Reg. §1.83-3(c)(2).

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Cause (cont'd)

- ▶ Beware of the Meaning of “Cause” (Austin v. Commissioner, 141 T.C. 551 (2013))
- ▶ Cause under Section 83 really refers to serious misconduct that is unlikely to occur.
- ▶ The parties can't hide something that would be a SRF in the definition of Cause and say an SRF was not established.

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SRF-Less Common Circumstances

- ▶ A SRF may exist when forfeiture of transferred property is conditioned on:
 - ▷ A requirement that an employee not compete after termination
 - ▶ “An enforceable requirement that the property be returned to the employer if the employee accepts a job with a competing firm will not ordinarily be considered to result in a [SRF] unless the particular facts and circumstances indicate to the contrary.” Treas. Reg. §1.83-3(c)(2)
 - ▷ A retiring employee to continue to provide services to an employer through consulting
 - ▶ “Similarly, rights in property transferred to a retiring employee subject to the sole requirement that it be returned unless he renders consulting services upon the request of his former employer will not be considered subject to a substantial risk of forfeiture unless he is in fact expected to perform substantial services.” Treas. Reg. §1.83-3(c)(2)

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Section 83-Transfer Required

- ▶ Section 83 applies when there is a compensatory transfer of property.
 - ▷ There must be an actual transfer of property (i.e., employer issues an employee restricted stock and registers the shares as outstanding on company's books and records).
- ▶ Lack of a current transfer or a mere promise to transfer property in the future upon satisfaction of a condition takes us out of Section 83 and makes a Section 83(b) election inapplicable.

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Section 83-Transfer Required

Tip

- ▶ Beware of circumstances that threaten whether a transfer has occurred (e.g., guaranteed floor price or value cap, non-recourse loan to purchase property, etc.)

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Risk Alert #1: Stockholder / LLC Agreements

- ▶ Beware of stock restrictions housed in stockholder and LLC agreements.
- ▶ Such agreements can create an “unknowing” SRF.
 - ▷ More Obvious- Repurchase at a discount upon voluntary termination of employment.
 - ▷ Less Obvious- Repurchase at a formula value upon voluntary termination of employment.

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Risk Alert #1: Stockholder / LLC Agreements-Example

- ▶ Executive is granted stock in 2020 that cliff “vests” after three years of continued employment in 2023.
- ▶ Executive is required to be party to a Stockholder Agreement.
- ▶ Stockholder Agreement contains a provision that allows the Company to repurchase stock at a discount of 50% to FMV upon an employee’s voluntary termination of employment prior to age 65.
- ▶ This repurchase right at a discount creates a SRF.

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Risk Alert #1: Stockholder / LLC Agreements-Example Cont'd.

- ▶ Assume Executive's FMV of stock in 2023 was \$1,000,000 and Executive is 55. Executive paid tax at an ordinary income rate in 2023 thinking the stock had vested (i.e., \$370,000).
- ▶ In 2026, the Company is sold and the value of the stock had grown by 25% (meaning stock is worth \$1,250,000). This is the true time of the lapse of the SRF with respect to the stock.
- ▶ The Executive expects capital gain treatment on the full growth above \$1,000,000, but ordinary income treatment is applicable under Section 83 with respect to the growth above \$1,000,000.
- ▶ There is a difference in tax of \$42,500 ($[(\$250,000 \times 37\%) - (\$250,000 \times 20\%)])$)
- ▶ Note: Possible solution would have been 83(b) election at the time of transfer.
- ▶ Note: Company withholding at time of sale.
- ▶ Note: Implications of tax timing and tax rate changes.

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Risk Alert #2: Founders Stock

- ▶ Founders often subject their shares to repurchase rights if they leave the employment or service. Often, those repurchase rights are at a discount to FMV.
- ▶ If these restrictions are placed on the equity at the time the founder receives (i.e., *at the time of "transfer"*) the shares (even if the founder purchases such shares at full FMV), a Section 83(b) election should be made to avoid future ordinary income on the shares. If the restrictions are added after the original issuance, Section 83 may not apply.

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Risk Alert #2: Founders Stock – Example*

- 2 Founders establish startup company
- Each pays par value of \$0.00001 per share (\$40 each for 4 million shares)
- Repurchase restrictions lapse / shares become vested over a period of 4 years (1M shares per year).
- In year 1, based on seed round investment, the shares are worth \$0.35 per share (\$350K for 1M shares). Taxable income to each founder is \$349,900 (\$350K - \$10).
- In year 2, based on additional Company success, the shares are \$1.30 per share (\$1.3 M for 1M shares). Taxable income to each founder is \$1,299,990 (\$1.3M - \$10).
- And so on...
- If 83(b) election was made at the time of purchase, no additional taxable income would be recognized in Years 1, 2, etc.

*Example from "Founder Traps", Michael J. Gorbach, March 28, 2017

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Risk Alert #3: Rollover and Purchased Equity in M&A

- ▶ Consider 83(b) elections in M&A transactions when the management team is asked to rollover current equity interests or purchase new equity interests in target company post-closing.
- ▶ Both in post-tax investments and tax-free rollovers, there are situations where 83(b) elections are advisable if rolled or purchased equity is subject to a SRF, including repurchase restrictions.
- ▶ 83(b) election often involves no tax cost, as the management team has paid FMV for their new equity or has contributed property of equal value to receive the new equity.

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Risk Alert #3: Rollover and Purchased Equity in M&A

▶ Revenue Ruling 2007-49

- ▷ Situation 1: Imposition of SRF on already owned stock (e.g., new investor that requires condition for investment). [No Transfer]
- ▷ Situation 2: Exchange of vested stock for “substantially nonvested stock” in a rollover with respect to a Section 368(a) tax-free reorganization. [Transfer; exchanged basis; treated as paying FMV for Section 83(b) election]
- ▷ Situation 3: Exchange of vested stock for “substantially nonvested stock” in a rollover with respect to a taxable transaction [Transfer; FMV basis; treated as paying FMV for Section 83(b) election]
- ▷ Does Not address unvested for unvested. [IRC Section 83(g) facts and unsettled “second bite at the apple”]
- ▷ The revenue ruling does not address holding period or continuity of interest issues.

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Risk Alert #3: Rollover and Purchased Equity in M&A - Example

- ▶ M&A transaction – management team receives large payout of incentive equity at closing.
- ▶ Management is asked to roll over \$5 million of their after-tax proceeds from the sale and invest that amount into equity in the target company, with such equity to participate on terms similar to equity held by the purchaser.
- ▶ However, in the event of a voluntary termination of employment within 2 years of closing, target company has a repurchase right to buy back the management employee’s stock at the lesser of FMV or the price paid by the employee.
- ▶ The management team should make 83(b) elections at the time of investment to avoid paying future ordinary income on any appreciation in the stock between closing and the 2-year anniversary when the repurchase restrictions lapse.
- ▶ The management team would file an 83(b) election at closing, collectively reporting that \$5 million of equity was received in exchange for a purchase price of \$5 million, thus \$0 taxable income.

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Thank you!

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4:10 – 5 p.m.

Hot Tax & IRS Practice & Procedure Issues

Michael Goller, JD, *Shareholder, Reinhart Boerner Van Deuren s.c.*

HOT TAX AND IRS ETHICS PRACTICE AND PROCEDURE ISSUES 2023

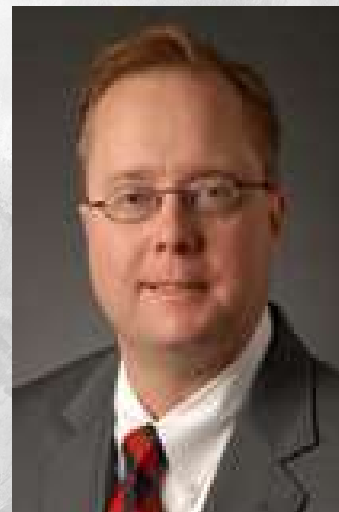
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Michael G. Goller is a shareholder in Reinhart's Tax, Litigation and Business practices. He focuses on tax controversy and tax litigation, as well as tax and estate planning. His clients range from large public corporations to midsized, privately held businesses and their owners. Michael works on behalf of his clients in disputes with the IRS, the Department of Justice and various other taxing authorities.



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- Part I - **Hot** Practice and Procedure Issues
- Part II - **Hot** Ethics Issues
- Part III - **Hot** High Net Work and Family Office Issues
- Part IV - **Hot** Employment Tax Issues

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PART I Hot Practice and Procedure Issues

- The IRS is going to receive a lot of money. They are starting to spend it.
- What are the hot audit issues?

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Hot Issues - Which Will Get Hotter

- Partnership Audits
- High Net Worth Audits
- Private Airplane Cases
- Estate and Gift - Valuation Issues
- Net Operating Loss and Basis Issues
- Passive Losses and the Real Estate Professional
- Cost Segregation Issues
- Section 183 - “Hobby” Loss Cases
- Refund Claim Traps
- Employment Tax Audits
- Penalty Issues

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PARTNERSHIP AUDITS

New Partnership Audit Program and related high net worth audit program are **HOT** in FY 2022, and beyond.

Source: Tax Notes (9/20/21)

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Overview

The BBA, among other things, eliminates the so-called TEFRA Unified Partnership Audit Procedures¹ and the Audit Procedures for Electing Large Partnerships.² It also creates a more streamlined partnership audit approach, thus making it easier for the IRS to audit a partnership.

1 These were first created in the Tax Equity and Responsibility Act of 1982.

2 Created as part of the Taxpayer Relief Act of 1997.

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Neutral Revenue Raiser

- The BBA was promoted as a “neutral” revenue raiser (*i.e.*, a revenue raiser in disguise); in that an increase in partnership audits will raise revenue without increasing taxes.
- It is expected that the new audit procedures and increased audits will yield \$9.3 billion of additional revenue over ten years. As such, the law gained quick approval in Congress.

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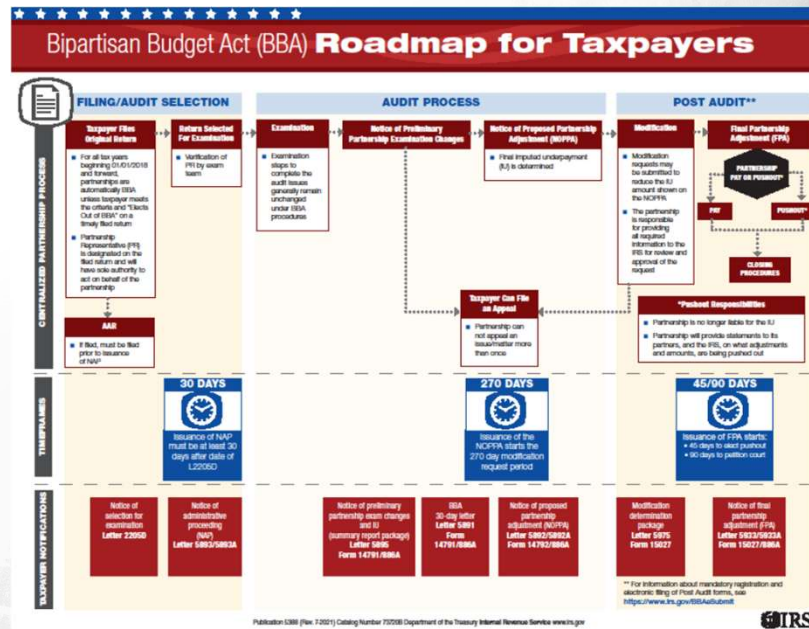
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Partnership Audit Road Map

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Current Status

- These audits seem to be off to a slow start
- IRS is asking for lengthy statute extensions

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Auditing Net Operating Losses

- What are the rules of the road
- Many traps - the statute of limitations is an issue

Comment: The five year net operating loss carry back has made this very relevant

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Statute of Limitations Issues

- A statute of limitations is a law that specifies the amount of time within which an act must be performed to be legally binding.
- Normally, the IRS must make any assessment of additional tax within three years of the time a return is filed.
- Assessment is nothing more than a bookkeeping entry made on the records of the Internal Revenue Service. Specifically, section 6203 provides that an "assessment shall be made by recording the liability of the taxpayer in the Office of the Secretary [of the Treasury]"
- A determination as to when the IRS made an assessment can be made by reviewing an IRS transcript of account.

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Statute of Limitations Issues (cont.)

There are a few significant intricacies about the statute of limitations on assessment

- A. A return filed prior to the due date is treated as filed on the due date
- B. If the return is filed after the due date, then the actual date of filing is used
- C. A return required to be filed return is deemed filed when it is postmarked, if the return is timely filed
- D. If the return is not filed when due, then the filing date, for limitations purposes, is the date it is actually received by the IRS. When a return is filed with the wrong Service Center, the statute does not begin to run until the redirected return is received by the correct Service Center

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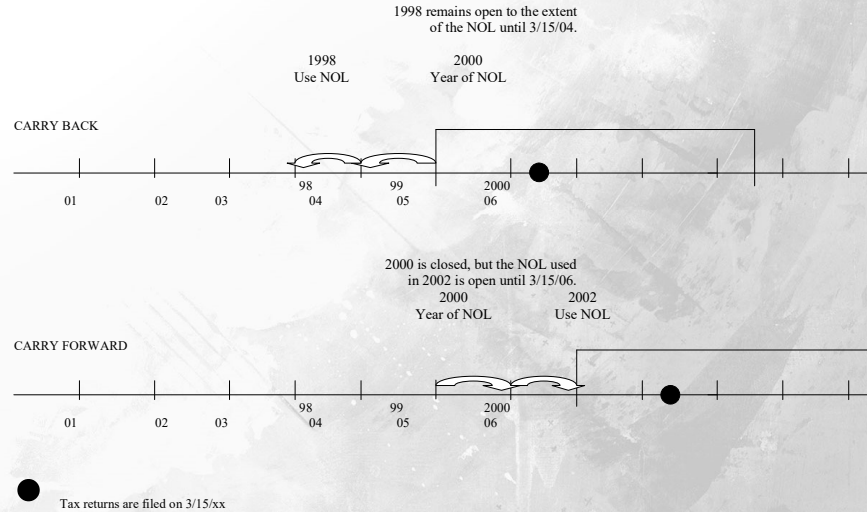
Statute of Limitations Issues (cont.)

- E. When calculating the 3-year period, the date that the return is actually filed is excluded
- F. When the due date falls on a Saturday, Sunday, or legal holiday, the return is considered timely filed if it is filed on the next business day. In such an instance, the statute of limitations begins to run on the actual date of filing.
- G. The statute of limitations on assessing estate tax cannot be extended. See § 6501(c)(4)(A)

Exception to Three-Year Rule for Items Carried Forward or Back

- A. A deficiency attributable to the carry-forward of a net operating loss, capital loss, or unused tax credit may be assessed within 3 years of the date of filing the return for the year the loss or credit is used, even though such date may be well beyond the normal statute of limitations for the year to which the loss or credit originally arose
- B. The statute of limitations on a carryback runs from the year of the loss, not the year in which the benefit of the loss is put to use

Net Operating Losses and The Statute of Limitations on Assessment § 6501



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IRS Attach on Cost Segregation Studies

- Publication 5653 (Rev. 6-2022) “Cost Segregation and Audit Technique Guide”
- Revisions were not large but whenever the IRS revises an audit manual, there will be audits

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Sample IDR

Form 4564	Department of the Treasury Internal Revenue Service Information Document Request	Request Number 006
To: [REDACTED]	Subject: Activity Log	
Submitted to: [REDACTED]		Dates of Previous Requests: N/A

Description of Documents Requested:

1. Please complete and sign the attached log forms (Exhibit A for calendar year 2019 and Exhibit B for calendar year 2020) for each real estate activity for which Taxpayer claims to have materially participated.
 - a. List all hours and services performed for the 2019 and 2020 calendar years. Provide detailed explanations of services or activities performed.
 - b. Provide documents to support hours claimed. This can include, but is not limited to, calendars, diaries, or other documents that reflect services provided and hours attributable to those services.

Where documents exist in electronic format, please provide in original electronic format.

Draft Date: 9/16/2022
Due Date: 11/7/2022

Information Due By 11/7/22 At Next Appointment Mail In

Name and Title of Requestor: Hwang, Yujin Internal Revenue Agent	Badge Number: 1003822997 Phones: 312-292-3152 Fax: 855-330-7359 Email: Yujin.hwang@irs.gov	Date: 9/16/2022
FROM: Office Location: Internal Revenue Service, Mail Stop 4171 LB&I/ECPA/1113, 230 S. Dearborn, Chicago, IL 60604	Page 1 of 1	

Form 4564

Section 183 “Hobby” Loss Cases

- Section 183
- Recent case - Walters v. Comm’r, T.C. Memo 2022-17 “Green Home” was a for profit venture

WDOR and I.R.C. Section 183

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Basis Issues, Passive Loss and At-Risk Rules - Lessons from the Trenches and Planning to Avoid IRS Attacks

- A taxpayer's ability to deduct a loss may be subject to three sets of limitations:
 - Basis
 - At-Risk
 - Passive
- Partnership allocation rules could also be considered a fourth limitation that impacts the ability of a taxpayer to deduct a loss

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At-Risk Rules

- Applies to:
 - Individuals (including partners, LLC members and S corporation shareholders). I.R.C. § 465(a)(1)(A).
 - C Corporations, if at any time during the last half of the taxable year more than 50% of the value of the corporation's outstanding stock is owned by five or fewer individuals. I.R.C. § 465(a)(1)(B).
- Generally, for purposes of the at-risk rules, each activity conducted by a taxpayer is treated as separate. I.R.C. § 465(c)(2)(A). May aggregate in certain cases.

At-Risk Rules (cont.)

- What is "at-risk"
 - Cash contributed
 - Amounts borrowed with respect to the activity, to the extent the taxpayer:
 - Is personally liable for repayment of such amounts. I.R.C. § 465(b)(2)(A).
 - There are two circumstances in which a partner is considered personally liable for debt:
 - » Partner borrows funds on a recourse basis and contributes those funds to the partnership for use in activity. Prop. Reg. § 1.465-7(a).
 - » Partnership incurs liability for which, under state law, partners may be held personally liable for repayment of the liability. Prop. Reg. § 1.465-24(a)(2)(i).

At-Risk Rules (cont.)

- Has pledged property (other than property used in the activity) as security for the borrowed amount. I.R.C. § 465(b)(2)(B).
 - Taxpayer is considered at risk only to the extent of the net fair market value of the pledged property securing the debt.
 - Property is not considered pledged property for purposes of this rule if the property is financed directly or indirectly by debt secured by the contributed property.
- A taxpayer is not considered at risk with respect to amounts protected against loss through nonrecourse financing, guarantees, stop-loss agreements or other similar arrangements. I.R.C. § 465(b)(4).
- Qualified nonrecourse financing is a big exception.

At-Risk Rules - Key Audit Issues

- A taxpayer is not considered at risk for amounts borrowed from any person who has an interest in the activity or from a person related to a person who has such an interest. I.R.C. § 465(b)(3)(A). Excludes direct borrowing by a partner. Other exceptions apply.
- Guarantees and Contribution Obligations
 - A guarantee does not increase a taxpayer's amount at risk unless the taxpayer has no right of reimbursement from the primary obligor of the liability. Prop. Reg. § 1.465-6(d).
 - An agreement that requires a taxpayer to make future contributions to capital does not increase the taxpayer's amount at risk until the contribution is actually made. Prop. Reg. § 1.465-22(a).
 - It is unclear whether a deficit restoration obligation ("DRO") increases a taxpayer's amount at risk.

Passive Losses and the Real Estate Professional

- Section 469
- Rental Real Estate
- Real Estate Professional
- Proving Material Participation
- Make a Grouping Election - watch limited partnership trap

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Passive Loss Rules

- Limit a taxpayer from deducting losses and excess credits from a passive activity against income from nonpassive activities. I.R.C. § 469(a).
- A passive activity is one that:
 - Involves the conduct of a trade or business in which the taxpayer does not materially participate. I.R.C. § 469(c)(1).
 - Is a rental activity. I.R.C. § 469(c)(2).

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Passive Loss Rules (cont.)

- Establishing Material Participation.
 - A taxpayer materially participates in an activity if, and only if, the taxpayer meets one of the following seven tests:
 - Work done in a taxpayer's capacity as an investor does not count toward the 500 Hour test, unless the taxpayer is directly involved in the day-to-day management or operations of the activity. Treas. Reg. § 1.469-5T(f)(2)(ii).

Passive Loss Rules (cont.)

- Investor activities include studying and reviewing financial statements or reports on an activity, preparing studies or analyses of the activity's finances or operations for the taxpayer's own use, and monitoring the activity's finances or operations in a nonmanagerial capacity

Passive Loss Rules (cont.)

- Facts and circumstances. Treas. Reg. § 1.469-5T(a)(7).
 - Taxpayer can establish material participation by regular, continuous and substantial involvement in an activity based on all the facts and circumstances
 - Must participate in activity for more than 100 hours. Treas. Reg. § 1.469-5T(b)(2)(iii).

Passive Loss Rules (cont.)

- Caution! Services performed in the management of an activity are disregarded unless:
 - » No other individual is compensated for performing management services in connection with such activity; and
 - » No other individual performs management services that exceed the hours spent by the taxpayer. Treas. Reg. § 1.469-5T(b)(2)(ii).

Passive Loss Rules (cont.)

- A taxpayer must establish hours of participation under the seven tests.
 - Any reasonable means of proof is sufficient to establish hours of participation. Treas. Reg. § 1.469-5T(f)(4).
 - Courts and the IRS are skeptical when a taxpayer makes extravagant claims on the number of hours of participation.
 - Courts generally do not accept "post-event ballpark guesstimate" of hours unless supported by credible testimony and other objective evidence
 - Taxpayers are recommended to keep careful records of participation
 - Practice Tip
 - Use an affidavit
 - A client interview

Passive Loss Rules (cont.)

- Special Rules for Real Estate Rental Activities.
 - Taxpayers who qualify as "real estate operators" may treat their real estate rental activities as nonpassive upon a showing of material participation. I.R.C. § 469(c)(7).
 - To qualify as a "real estate operator":
 - For CHCs:
 - More than 50% of the corporation's gross receipts for the year must be derived from real property trades or businesses in which the corporation materially participates. I.R.C. § 469(c)(7)(D)(i).

Passive Loss Rules (cont.)

- For individuals:
 - The taxpayer must satisfy the two following requirements:
 - » More than one half of all personal services performed in trades or businesses must be performed in the real property trades or businesses; and
 - » More than 750 hours of services must be performed in real property trades or businesses in which the taxpayer materially participates. I.R.C. § 469(c)(7)(B).

Passive Loss Rules (cont.)

- Personal services include any work performed by the individual in the connection with a trade or business, except for:
 - » Worked performed by an individual in the individual's capacity as an investor. Treas. Reg. § 1.469-9(d)(4).

Passive Loss Rules (cont.)

- » Services performed as an employee, unless the employee is a 5% owner of the employer. I.R.C. § 469(c)(7)(D)(ii).
 - » Practice Tip: When looking to purchase Real Estate (e.g., Apartment Buildings), document that the activity is not investment activity
- Services of the taxpayer's spouse cannot be combined to satisfy either of the two requirements. Treas. Reg. § 1.469-9(c)(4).

Passive Loss Rules (cont.)

- Caution! Rental activities held through a passthrough entity constitute a single interest if the entity grouped its real estate as a single activity. Treas. Reg. § 1.469-9(h). However, if a taxpayer owns directly or indirectly a 50% or greater interest in the passthrough entity, each interest in rental real estate is treated as a separate interest unless the taxpayer makes his or her own election to treat all interests in real estate as a single activity.

Airplane Cases

- Partnership or corporate structure
 - Personal Entertainment v. Non-Personal Entertainment
- SIFL or §274-10(e)
- Schedule C Structure - CCA 202117012 (4/30/21)
- Depreciation and the Section 280F trap
- Entertainment Facility trap

Examination of Returns— General

- Introduction
 - The possible audit of a taxpayer's return encourages voluntary compliance
 - The chances of examination vary depending on geographical location, type of return, and Adjusted Gross Income

Examination of Returns— General (cont.)

- IRS Field Audits
 - The field examination is used for most business returns and larger, more complex individual returns
 - Section 7602 of the Internal Revenue Code authorizes the Treasury Department to examine any books, papers, records, or other data that may be relevant or material to ascertaining the correctness of any return

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Examination of Returns— General (cont.)

- Other Types of Audits
 - Correspondence audit
 - Office examinations
 - Employment tax audits
- We have seen an increase in audits of Exempt Organizations. A key issue is control of the organization.

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Handling the Audit

- Examination of Tax Returns—Practical Strategies
 - Control the flow of information
 - Do the agent's job for him or her
 - Where the audit occurs
 - Do not give the IRS free access to the taxpayer's employees
 - How deep will the revenue agent dig?

Handling the Audit (cont.)

- Responding to Requests for IRS Information
- Tell Your Story
- Burden of Proof Issues
- Privilege Issues

Handling the Audit (cont.)

- The Concept of Assessment
 - What is assessment
 - Civil statute of limitations on assessment
 - Assessment as a civil concept
 - Generally, before assessment can occur, the normal deficiency procedures must be followed
- Summary of Important Terms
 - Thirty-Day Letter
 - Protest
 - Ninety-Day Letter

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IRS Acknowledgement IDR-- Happens at the end of the audit

- IRS issues to most larger taxpayers an IDR that attempts to box the taxpayer into certain facts
- How to respond to the IDR?
- Why noncompliance is not an option:
 - Burden of proof issues
 - Rule of evidence issues (must make info available to opponent)
 - Penalty issues--arguing reasonable cause
 - IRS appeals uses a nonresponse as a basis for not appealing
 - Qualified Offer issues

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Cooperation Issues

- Consider if you are eligible to switch the burden of proof to the IRS
 - Cooperation is important
 - Adequate records are important
- Noncooperation leads to admissions (e.g., statements or inferences that are later used against you)

Acknowledgement IDR

- Use the acknowledgement IDR to support your case

Getting to Appeals

- 30 day letter
- Protest - Skinny or fat - pros and cons
- Do an FOIA request
- Exam's "T-letter"

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Settling the Case at Appeals

- Hazards of litigation
- Does the IRS have uniform settlement guidelines?
- What to do if you hit a "brick wall"?

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Which Court to go to

- U.S. Tax Court
- Federal District Court (refund)
- U.S. Court of Federal Claims (refund)
- Issues to consider
 - Precedent
 - Discovery issues and cost
- IRS v. DOJ

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IRS Attorneys Requests for Information

- IRS attorneys have a set of standard questions
- Need to be able to address these questions in a cost-effective manner
- Trap - the failure to respond can lead to formal discovery or deemed admissions

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Penalty Issues

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Reasonable Cause and Penalty Avoidance

- How does Section 6662 work
- What is Reasonable Cause
- There is no "one free kick" rule
- Minimizing penalty risks

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Reasonable Cause and Penalty Avoidance

The Section 6662 Penalty

- Negligence or Disregard of Rules or Regulations
- Substantial Understatement of Income Tax
- Substantial Valuation Misstatement under Chapter 1 of the Code
- Substantial Overstatement of Pension Liabilities
- Substantial Estate or Gift Tax Valuation Understatement
- Disallowance of Tax Benefits Because a Transaction Lacks Economic Substance or any Similar Rule or Law
- Any Undisclosed Foreign Financial Asset Understatement

Section 6662 Penalty (20% or 40%)

- Generally, penalty is 20% and applies to any portion of an underpayment attributable to one or more violations
- In certain instances, penalty can rise as high as 40%

Interest

Computed from the date of the return



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What is an Understatement?

- Excess of the amount required to be shown on the return over the amount of tax shown on the return. Section 6662(d)(2)(A)

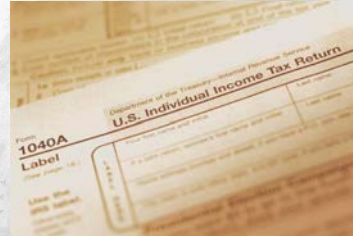
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Tax Return **MUST** Have Been Filed

Both the Accuracy-Related Penalty and the Fraud Penalty only apply where a return has been filed



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Qualified Amended Return Can Reduce the Amount of an Underpayment

Amount of tax shown on a tax return includes the amount shown as additional tax on a "qualified amended" return



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THE ACCURACY-RELATED PENALTY BASED UPON NEGLIGENCE . . .

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Negligence

- Only applies to that portion attributable to negligence, not the entire underpayment
- Negligence is defined as “any failure to make a reasonable attempt to comply with the provisions of [the Code]”

Comment: One way to settle a case is to apply the penalty to only a small part of a deficiency

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Disregard of Rules or Regulations

- Any "careless, reckless, or intentional disregard"
 - Section 6662(c)



THE ACCURACY RELATED PENALTY BASED UPON A SUBSTANTIAL UNDERSTATEMENT OF INCOME TAX. . .

What is a Substantial Understatement of Income Tax?

- Noncorporate taxpayer
 - Exceeds the greater of 10% of the tax required to be shown on the return or \$5,000
 - Corporation other than S Corporation or Personal Holding Company
 - Exceeds the lesser of one of the following:
 - 10% of the tax required to be shown on the return (or if greater, \$10,000); or
 - \$10 million
- Section 6662(d)(1)

Reasonable Basis

- Under Treasury Reg. § 1.6662-3(b)(3), negligence is negated if there is a reasonable basis for the return position
 - Determining what is Reasonable Basis
 - “A relatively high standard of tax reporting, that is significantly higher than not frivolous or not patently improper. The reasonable basis standard is not satisfied by a return position that is merely arguable or that is merely a colorable claim.”
 - What authorities can be cited to prove Reasonable Basis?

Reasonable Cause

- Defined as Ordinary Business Care and Prudence
- Section 6662 Penalty can be avoided by showing reasonable cause (in most-cases)
- Proof of Reasonable Cause, when arguing reliance on a professional - 3 part test
 - Advisor was competent and had significant expertise to justify reliance
 - Taxpayer gave advisor adequate and necessary information
 - Taxpayer relied in good faith upon the advisor

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Disclosure

- Penalty may often be avoided by a complete and adequate disclosure of the item or position at issue and there is:
 - Reasonable basis for position
 - Taxpayer keeps adequate books and records

Comment: Disclosure will not avoid the accuracy related penalty based on negligence.

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Substantial Authority

- See Treas. Regs. § 1.6662-4(d).
 - A Confidence Level of perhaps 40%?

Understatement Related to a Tax Shelter

- If related to a tax shelter, adequate disclosure of the item will not relieve the taxpayer from the penalty
 - Must meet elevated substantial authority test
 - Must show Substantial Authority and a reasonable belief that the treatment was MLTN correct tax
 - A tax shelter exists if a significant purpose of an entity, plan or arrangement is the avoidance of income tax

Raising Reasonable Cause Can Waive a Privilege

CAUTION:

Raising the assertion of reliance on professional advice constitutes reasonable cause probably waives the attorney/client privilege and the Section 7525 privilege.



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Raising Reasonable Cause Can Waive a Privilege (cont.)

- IRM 20.1.5.6.4 (January 24, 2013)
(If the taxpayer claims a tax memorandum or advice is privileged, the IRS will not abate the penalty)

Comment: Would the IRS assert a penalty to force a privilege waiver?

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Penalty Avoidance Matrix

	Reasonable Basis §1.6662-3(b)(3)	Reasonable Cause §6664 §1.6664-4(b)	Disclosure §6662(d)(2)(B) §1.6662-3(a)	Substantial Authority §1.6662-4(d)
Negligence	Yes	Yes	No ¹	Yes ²
Disregard of the Rules or Regulations	Yes ⁴	Yes	Yes ³	Yes ⁵
Substantial Understatement of Income Tax	No	Yes	Yes ⁶	Yes
Substantial Valuation Misstatement (Income)	No	Yes ⁷	No	No
Substantial Valuation Misstatement (E&G)	No	Yes	No	No
Gross Valuation Misstatement (Income)	No	No ⁷	No	No
Gross Valuation Misstatement (E&G)	No	Yes	No	No

1. § 1.6662-7(b).
 2. There must also be a reasonable basis for the position, adequate records must be kept and the position must be properly substantiated. § 1.6662-3(c). In a case where there is substantial authority for a position, since this standard is higher than the reasonable basis standard (which negates negligence), there is no negligence. § 1.6662-3(b)(3).
 3. There must be reasonable basis and the taxpayer must keep adequate books, records and substantiation. § 1.6662-3(c)(1).
 4. The disregard can be careless, reckless or intentional. § 1.6662-3(b)(2). The first two (careless and reckless) are for all practical purposes, the same as negligence, meaning reasonable basis would negate these two triggers. Further, however, if a position is intentionally contrary to a rule or regulation, reasonable basis would not be enough. However, see the disclosure election.
 5. A position that is contrary to a Revenue Ruling or Notice is not treated as disregarding the ruling or notice if the contrary position has a realistic possibility of being sustained (a standard that is lower than substantial authority § 1.6662-3(b)(2)). It is technically possible to have substantial authority that is contrary to a Treasury Regulation, which means the penalty could apply. In this case the taxpayer should be sure to make a disclosure.
 6. There must also be a reasonable basis for the tax treatment of the disclosed item. § 6662(d)(2)(B)(i).
 7. There is no reasonable cause exception for a gross valuation misstatement with respect to charitable deduction property and the exception only applies to a substantial valuation statement when there is a qualified appraisal and the taxpayer made a good faith investigation of the value of the property. § 6664(c)(3).

Income Tax Overstatement of Value e.g., a Charitable Contribution

- Substantial Valuation Misstatement
 - There is a 20% penalty applicable to any underpayment attributable to a Substantial Valuation Misstatement
 - Section 6662(b)(3)
 - A substantial valuation misstatement occurs if the value (or adjusted basis) of any property claimed on a return claimed income is 150% or more of the correct amount
 - Section 6662(e)
 - The penalty is not imposed unless the misstatement results in an underpayment of greater than \$5,000 (\$10,000 for a C-corporation)
 - Section 6662(b)(2)

Gross Valuation Misstatement

- There is a 40% penalty in the case of a Gross Valuation Misstatement.
- A Gross Valuation Misstatement occurs if the value of the property is 200% or more of the correct value section.
- The standard is automatically met if the correct value is zero.
 - Treas. Reg. Section 1.6662-5(g).
- Example
 - Donor claims a deduction under Section 170 for the donation of property to a qualified charity

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Reasonable Cause and the Income Tax Valuation Penalties

- A reasonable cause exception under Section 6664 can apply when the underpayment is attributable to a substantial (but not a Gross) understatement with regard to a charitable contribution if the following occurs:
 - The claimed value of the property is based upon a qualified appraisal by a qualified appraiser;
 - The taxpayer also made a good faith investigation of the value of the contributed property; and
 - The taxpayer acted with reasonable cause and in good faith
 - Section 6664(c)(3)

Comment: Review the definitions of a qualified appraiser and appraisal in Treas. Reg. Section 1.170A-13(c)(3) and (5)

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Penalty for Erroneous Refund Claims – Section 6676

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Penalty for Erroneous Refund Claims (Section 6676)

- Penalty equal to 20% of the excessive amount claimed unless:
 - It is shown that there is reasonable cause for the claim for the excessive amount.
 - Assume reasonable cause is the same as under Section 6664.

Comment: Reasonable cause is a defense.

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PART II

Ethics

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Ethical Obligation to Talk About Penalty Avoidance

- Under IRS Circular 230, practitioners must advise the client of any penalties that are reasonably likely to apply and the practitioner must discuss the possibility of penalty avoidance via disclosure.
§10.34(c)

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The Office of Professional Responsibility

- There is often a tendency to assume that the Department of the Treasury's Circular No. 230 (Circular 230) pertains solely to preparing tax returns, tax opinions or dealings with the IRS
- The conventional wisdom is that a violation Of Circular 230 must mean a practitioner has engaged in some sort of outrageous behavior
- The reach of this ethical code is far greater than one might think
- A violation can (and does) occur in many more situations than practitioners might otherwise expect

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A Violation of Circular 230 Is a Serious Matter

- Public discipline for violating Circular 230 usually involves obvious misconduct such as one's own failure to file or pay tax, or the conviction of a criminal offense
- We have been seeing more cases that pertain to alleged "bad tax practice," such as a lack of due diligence, failure to give sound tax advice, conflicts of interest or other issues that indicate a tax practitioner's lack of fitness to practice before the IRS

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Who Is Subject to Circular 230? Section 10.3 (Revised June 9, 2014)

- Circular 230 applies to those who “practice before the IRS”
- “Practice before the IRS” comprehends all matters connected with a practitioner’s presentation to the IRS with respect to a taxpayer’s rights, privileges or liabilities under the tax law, including
 - Preparing or filing documents, correspondence and communicating with the IRS
 - Rendering written advice with respect to an entity plan or arrangement that has a potential for tax avoidance or evasion
 - Representing a client at IRS conferences and hearings

Who Is Subject to Circular 230? Section 10.3 (Revised June 9, 2014)

- Attorneys and CPAs (including in-house practitioners) who are not under suspension or disbarment from practice before the IRS may file a Power of Attorney (POA) (Form 2848)
 - This permits them to and practice before the IRS and makes them subject to Circular 230
- One need not file a POA to provide written tax advice, however, providing written tax advice constitutes practice before the IRS
 - *i.e.*, makes the individual subject to Circular 230

When Is Conduct Sanctionable?

- Generally, a practitioner may be sanctioned if the practitioner:
 - Is incompetent or disreputable;
 - Intentionally misleads a client so as to defraud that client; or
 - Is acting with a specific mental state or competency standard (*i.e.*, willful, reckless or gross incompetence), fails to comply with key provisions of Circular 230

AICPA Rules

- Statements on Standards for Tax Services

Statement on Standards for Tax Services No. 1, *Tax Return Positions*

- Interpretation No. 1-1, Reporting and Disclosures
- Interpretation No. 1-2, Tax Planning

Statement on Standards for Tax Services No. 2, *Answers to Questions on Returns*

AICPA Rules

Statement on Standards for Tax Services
No. 3, *Certain Procedural Aspects of
Preparing Returns*

Statement on Standards for Tax Services
No. 4, *Use of Estimates*

Statement on Standards for Tax Services
No. 5, *Departure from a Position Previously
Concluded in an Administrative Proceeding
or Court Decision*

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AICPA Rules

Statement on Standards for Tax Services
No. 6, *Knowledge of Error: Return
Preparation and Administrative Proceedings*

Statement on Standards for Tax Services
No. 7, *Form and Content of Advice to
Taxpayers*

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ABA Model Rules of Professional Conduct

- Some Version of the MRPC has been adopted in almost all states.
- Rules are mandatory.
- Comments to the rules are aspirational (not mandatory).

How Aggressive Can (Should) The Practitioner Be?

- Standards With Respect to Tax Returns and Other Documents §10.34
 - The practitioner must inform a client to of any penalties that are reasonably likely to apply with respect to:
 - A return position the practitioner provided advice on;
 - A return the practitioner prepared or signed; and
 - Documents submitted to the IRS.
 - A practitioner may not advise a client to take a frivolous position in a document, affidavit or other paper submitted to the IRS
 - Further, a practitioner cannot advise a client to make a submission to the IRS if the submission is frivolous, intended to cause delay, or intentionally disregards IRS rules or regulations

Caution: An offer in compromise or a Collection Due Process appeal cannot be filed solely to delay collection activity

How Aggressive Can (Should) The Practitioner Be?

- The practitioner must also inform the client of the opportunity to avoid such penalties by disclosure and the requirements of adequate disclosure
- It is critical that the practitioner understand how Section 6662 works
- Do a memorandum to the file

AICPA Rule

AICPA Statement on Standards for Tax Services No. 1, Tax Return Positions, Section 6.

When recommending a tax return position or when preparing or signing a tax return on which a position is taken . . . [a CPA] should, when

relevant, advise the taxpayer regarding potential penalty consequences of such tax return position and the opportunity, if any, to avoid such penalties through disclosure.

Circular 230 Conflicts of Interest Section 10.29

- A major cause of malpractice claims, especially for Estate Planners



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A Conflict of Interest Exists If

- The representation of one client will be directly adverse to another client; or,
- There is a significant risk that the representation of one or more clients will be materially limited by the practitioner's responsibilities to another client, a former client or third person, or by the personal interest of the practitioner.

Comment: Rule is very similar to Model Rule 1.7

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Other Authority

- ACTEC Commentary to Model Rule 1.7

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Conflict Waivers - Circular 230 10.29



- The client must provide a written consent waiving the conflict within 30 days of giving verbal consent.
- The written waiver must be retained for at least three years after the conclusion of the representation of any affected client.

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Obtain a Waiver

- Where a conflict exists, a practitioner may still handle the matter if the practitioner reasonably believes that he/she will be able to provide competent and diligent representation to each affected client, the representation will not otherwise violate the law and each affected client waives the conflict in an informed consent at the time the conflict is discovered by the practitioner.

Traps for the Unwary

- Representing spouses
- Personal interest of the lawyers
 - penalty issues
 - lawyer as a fiduciary
- Lawyer paid by a third party
- Innocent spouse relief issues

Tax Court Rule 24(g)

- The Rule goes beyond the normal conflict definition and states that if Counsel of Record was involved in planning or promoting a transaction at issue before the Court, that attorney must either obtain a consent or withdraw from the case.
 - This is a trap for the unwary.

Comment: More cases are becoming docketed in Tax Court due to the IRS insistence that a year or more remain on the assessment statute. The estate tax statute on assessment cannot be extended. Thus, the application of Rule 24(g) will come up more often in estate tax cases.

Why are more and more estate planners finding it necessary to docket a case in Tax Court?

- Two reasons
 - IRS budget cuts
 - Section 6501(c)(4)(A) provides that the statute of limitations on assessment can be extended with regard to "any tax imposed by this title, except *the estate tax . . .*" (emphasis added)
 - Practical Comments

Additional Trap for the Unwary

- Tax Court Petition is due before an executor is appointed (presumably an income tax issue that pertains to a pre-death year).
- Petition is filed in the name of Joe Smith, Deceased.
- Under Rule 60, must ratify Petition or the case may be dismissed.
- Dismissal of your Tax Court Petition means the IRS assessment stands.

Comment: If the estate has multiple beneficiaries, does the estate and a surviving spouse have a conflict?

More Conflict Traps for the Unwary

The Practitioner's Own Interest

- A common conflict, which is often overlooked, is the situation where a practitioner prepares a tax return, either as a signing or nonsigning preparer, and then handles the subsequent tax audit or appeal.
- In this situation, there may be a conflict if the practitioner has a personal interest that conflicts with the client's interest.
- For example, if the IRS asserts an accuracy-related penalty, will the practitioner be hesitant to argue that the penalty should not apply because of the taxpayer's good-faith reliance on the practitioner's tax advice?
- What if the practitioner has a conflict because of an unreasonable fee?

Comment: The estate and gift tax valuation penalties are mathematical triggers. Thus, if value is too low the trigger (and thus a possible conflict) could arise without much warning.

More Conflict Traps for the Unwary (cont.)

Representing Both Spouses

- Another common conflict exists when the practitioner represents both a husband and wife, and the two spouses' interests become adverse.
- In such a situation, the practitioner may be unable to represent either spouse.
- Example – clients divorce and there is a pending Tax Court case. Does one spouse have a claim for relief under Section 6015 (i.e., innocent spouse and similar relief)?

Need both a PTIN and a Data Security Plan

Resources:
[IRS.gov](#)
[Frequently Asked Questions](#)
[Annual Filing Season Program](#)
[Enrolled Agent Information](#)
[Pay.gov System](#)
[Online PTIN System](#)
[Back to top](#)

Dear Tax Professional,

Summer is over, and it won't be long until you're sitting down at your computer to renew your preparer tax identification number (PTIN) for 2020. In mid-October when renewal season begins, you will notice a *data security responsibilities statement* has been added to the PTIN renewal process. It serves as a reminder of your legal responsibility to have a data security plan and to provide data and system security protections for all taxpayer information. When completing your PTIN renewal, a checkbox will be available to confirm your awareness of these data security responsibilities.

Data security continues to be a hot topic. That's because tax professionals remain a top target of identity thieves and data breaches continue to affect tax professionals at an alarming rate. Cybercriminals use sophisticated and ever evolving techniques to gain access to your systems. These criminals steal sensitive taxpayer data to file fraudulent tax returns and create financial havoc for your clients. There are simple steps you can incorporate in your daily operations to minimize your vulnerability and protect client data, including:

- Protect email accounts with strong passwords and two-factor authentication if available.
- Install an anti-phishing tool bar to help identify known phishing sites.
- Use anti-phishing tools that are included in security software products.
- Use security software to help protect systems from malware and scan emails for viruses.
- Never open or download attachments from unknown senders, including potential clients. They should instead make contact first by phone.
- Send only password-protected and encrypted documents when files must be shared with clients over email.
- Never respond to suspicious or unknown emails.
- Back up sensitive data to a safe and secure external source.
- Properly dispose of old computer hard drives that contain sensitive data.

You should also make sure to have a written data security plan in accordance with the Federal Trade Commission's *Safeguard Rule*. Remember, protecting your clients is not only good for business, it's also the law. While the hope is that you're never the victim of a data breach, preparation and education will go a long way in helping to protect your clients and yourself.

More information:
[Publication 4557, Safeguarding Taxpayer Data](#)



[Publication 5283, Data Security Resource Guide for Tax Professionals](#)
[Identity Theft Information for Tax Professionals](#)

[Back to top](#)

Firm Management Procedures to Ensure Circular 230 Compliance Section 10.36 (Revised June 10, 2014)

- The IRS appears to be attempting to create a “culture of compliance”
- Practitioners in a position of authority must do more than ensure their own compliance with Circular 230
- Supervising practitioners must ensure that all individuals they supervise comply with Circular 230 as it pertains to the preparation of returns, claims for refund or other documents submitted to the IRS

Section 10.36

- A practitioner responsible for implementation of Circular 230 compliance procedures will be subject to disciplinary action if:
 - 1(a) The responsible practitioner, through willfulness, recklessness or gross incompetence, does not take reasonable steps to ensure that the firm has adequate procedures to comply with Circular 230; and
 - 1(b) One or more individuals who are members of, associated with, or employed by the firm are, or have engaged in a practice in connection with their practice with the firm of failing to comply with Circular 230;

Section 10.36

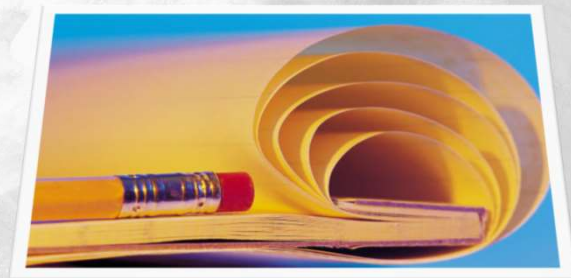
- 2(a) The responsible practitioner, through willfulness, recklessness or gross incompetence, does not take reasonable steps to ensure that firm procedures in effect are properly followed; and
- 2(b) One or more individuals who are members of, associate with, or are employed by the firm or have engaged in a pattern or practice, in connection with their practice with the firm of failing to comply with Circular 230; or

Section 10.36

- 3(a) The responsible practitioner knows or should know that one or more individuals who are a member of, associated with, or employed by the firm are, or have engaged in a pattern or practice in connection with their practice with the firm that does not comply with Circular 230, as applicable; and
- 3(b) The responsible practitioner, through willfulness, recklessness or gross incompetence, fails to take prompt action to correct the noncompliance.

Written Tax Advice Form Section 10.35 and Section 10.37(a) Revised June 9, 2012

- The Covered Opinion Rules (Former §10.35)
 - These have gone away – Proposed regulations were issued on September 14, 2012
 - Final regulations were issued June 9, 2014 and became effective on June 12, 2014



Old Rules

- Certain burdensome requirements existed if one issued one of the following:
 - A listed transaction opinion;
 - Principal purpose opinion is tax avoidance; or
 - Significant purpose to avoid tax opinion PLUS the opinion is one of the following opinions
 - Reliance Opinion
 - Marketed Opinion
 - Opinion subject to conditions of confidentiality
 - Opinion subject to contractual protection

Ramifications of the Withdrawal of the Covered Opinion Rules

- No more legends on our e-mails
- Issuing a tax opinion may be more complex than before
- It is clear under the new rules that government submissions on matters of general policy and continuing education presentations are not considered written tax advice

Requirements for Written Tax Advice Section 10.37(a) (Revised June 9, 2014)

- The Practitioner must
 - Base written advice on reasonable factual and legal assumption
 - Including assumptions as to future events
 - Reasonably consider all relevant facts and circumstances the practitioner knows or reasonably should know
 - Use reasonable efforts to identify and ascertain the facts relevant to written advice on each federal tax matter

Requirements for Written Tax Advice Section 10.37(a) (Revised June 9, 2014)

- Not rely upon representations, statements, findings or agreements (including projections, financial forecasts, or appraisals) of the taxpayer or any other person if reliance upon them would be unreasonable
- Relate applicable law and authorities to the facts; and not, in evaluating a federal tax matter, take into account the possibility that a tax return will not be audited or that a matter will not be raised on audit

Further, reliance upon a representation, statement, finding or agreement is specifically unreasonable if the practitioner knows or reasonably should know that one or more representations or assumptions on which any representation is based is incorrect, incomplete or inconsistent

Reliance on Others Section 10.37(b) Revised June 9, 2014

- The practitioner may only rely on the advice of another person if the advice was reasonable and the reliance is in good faith considering all the facts and circumstances
- Reliance is specifically not reasonable when
 - The practitioner knows or reasonably should know that the opinion of the other person should not be relied upon;
 - The practitioner knows or reasonably should know that the other person is not competent or lacks the necessary qualifications to provide the advice; or
 - The practitioner knows or reasonably should know that the other person has a conflict of interest in violation with Circular 230
 - e.g., the conflict has not been properly waived

Standard of Review Have I Complied with the Rule?

- In evaluating whether a practitioner's written tax advice complies with Section 10.37, the IRS will apply a "reasonable practitioner" standard, considering all facts and circumstances, including, but not limited to the scope of the engagement and the type and specificity of the advice sought by the client

Standard of Review

Have I Complied with the Rule?

- In the case of an opinion the practitioner knows or has reason to know will be used or referred to by a person other than the practitioner in promoting, marketing or recommending a transaction, a significant purpose of which is the avoidance or evasion of tax, the IRS will apply an elevated “reasonable practitioner” standard. Emphasis will be given to the additional risk, caused by the practitioner’s lack of knowledge of the specific taxpayer’s particular circumstances (*i.e.*, when tax advice is going to be used to promote a transaction to a third party, the IRS will apply an elevated standard of care).

Due Diligence

Section 10.22 (Revised June 9, 2014)

- Practitioner Must Exercise Due Diligence
 - Every practitioner must exercise due diligence when practicing before the IRS
 - This includes exercising diligence in preparing documents relating to IRS matters and verifying the correctness of oral and written presentations made to both the IRS and one’s client with regard to any matter administered by the IRS
 - A practitioner’s duty to be diligent is a very broad concept
 - A lack of diligence would seem to exist in most instances of deficient practice-related conduct

Due Diligence

Section 10.22 (Revised June 9, 2014)

- The concept of diligence seems to require more than the mere belief that a presentation is correct the moment it is submitted to the IRS or a client
 - The implied approval of past incorrect statements would seem to be a violation of Section 10.22
 - If a practitioner fails to correct an incorrect statement made to the IRS or a client, knowing full well that the recipient continues to rely on that statement
 - A failure to correct the error is inconsistent with the practitioner's obligation to be diligent

Reliance on Others



A practitioner will be presumed to have exercised due care if the practitioner relies on the work product of another person so long as the practitioner used reasonable care in engaging, supervising, training, and evaluating the person, **taking into account the nature of the relationship between the practitioner and the other person**

Diligence as to Accuracy §10.22

- Trap for the unwary – FBAR (FinCin 114) and foreign bank accounts



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IRS Circular 230 Issues (cont.)

Written Advice and a Conflict of Interest

A prior adviser, who may have advised the client to claim the ERC, has a conflict because of the amount of the fee the adviser charged for the advice, then the practitioner's reliance on that advice may not be reasonable?

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Use of Estimates

- AICPA Statement on Standards for Tax Services No. 4, Use of Estimates
 - Unless prohibited by statute or by some other rule, a CPA may use the taxpayer's estimates in the preparation of a tax return if it is not practical to obtain exact data and if the CPA determines that the estimates are reasonable based on the facts and circumstances known to the CPA
 - The taxpayer's estimate should be presented in a manner that does not imply greater accuracy than exists

Preparing a Tax Return

- The provisions of Circular 230 "piggy back" on I.R.C. Section 6694
 - Under Circular 230, practitioners may not willfully, recklessly or through gross incompetence sign (or advise a client to take a position on) a return or claim for refund if the practitioner knows or should know the return reports a position that lacks a reasonable basis, is an unreasonable position under I.R.C. Section 6694(a)(2), is a willful attempt to understate the tax liability, or is a reckless or intentional disregard of IRS rules or regulations

Preparer Penalty Standards Under I.R.C. Section 6694(a) and Circular 230 Section 10.34

Standard	Preparer Duty
Frivolous ¹	Cannot prepare tax return
Reasonable basis ²	Can prepare tax return with disclosure ³
Substantial authority ⁴	Need not disclose unless a tax shelter or a Section 6662A Reportable Transaction ⁵
Reasonably believe more likely than not (<u>i.e.</u> , more than 50%)	Need not disclose

¹ The percentage of comfort is perhaps 5% or less

² Reasonable basis is defined in Section 1.6662-3(b)(3); the percentage of comfort is perhaps 20%

³ Use Form 8275 or 8275R, or disclose pursuant to annual revenue procedure (e.g., Rev. Proc. 2015-16)

⁴ "Substantial authority" is defined in Section 1.6662-4(d). It is a comfort level of perhaps 40% or more

⁵ A tax shelter is an arrangement that has a significant purpose of avoidance or evasion of income tax. Section 6662(d)(2)(C)(iii). See Notice 2009-5 for how, in limited situations, to lower the standard to substantial authority for a tax shelter (basically educate the taxpayer about penalty exposure and document this fact)

Competence – Section 10.35 (Revised June 9, 2014)

- A practitioner must possess the necessary competence to engage in practice before the IRS
- Competent practice requires knowledge, skill, thoroughness and the preparation necessary for the matter at issue
- A practitioner may become competent through various methods such as consulting with experts or studying the relevant law

Comment: Sections 10.35 and 10.36 together mean that managers have a duty to ensure that their subordinates have the requisite knowledge and skill and that they appropriately use that knowledge and skill

AICPA Rules

- AICPA Code of Professional Conduct, Section 50, Article V, Due Care
- “... Members should be diligent in discharging responsibilities to clients, employers and the public. Diligence imposes the responsibility to render services promptly and carefully, to be thorough, and to observe applicable technical and ethical standards ...”

MRPC -1.3

- A lawyer shall act with reasonable diligence and promptness in representing a client

Prompt Disposition of Matters and Responses to Requests for Information §10.20 and §10.23

- If the IRS makes a proper request for records or information, a practitioner must promptly respond to the request unless the practitioner reasonably has the good-faith belief that the information is privileged
- A practitioner may not unreasonably delay the prompt disposition of any matter before the IRS



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Prompt Disposition of Matters and Responses to Requests for Information §10.20 and §10.23

- The practitioner must make a reasonable inquiry of the practitioner's client as to who has possession or control of the requested information
 - However, a practitioner need not make inquiry of any other persons or verify information provided by the client

Comment: Consider these rules when responding to a "wealth squad" IDR, a detailed LB&I IDR or a very broad discovery request.

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Prompt Disposition of Matters and Responses to Requests for Information §§10.20 and 10.23

- Where the documents or information requested by the IRS are not in the possession of the practitioner or client, the practitioner must promptly provide the IRS employee seeking the information with any information the practitioner has about who has possession or control of the requested information

Comment: This rule certainly seems to raise Section 7525 and attorney-client concerns

Professional Responsibility and the Employee Retention Credit

ERC - Circular 230 Issues

Purpose and Operation of the ERC

The ERC is a refundable tax credit. The ERC was enacted for employers who continued paying employees during a shutdown due to the COVID-19 pandemic or who experienced significant declines in gross receipts, from March 13, 2020, to December 31, 2021.

Eligible employers may claim the ERC on an original or amended Form 941.

ERC - Circular 230 Issues

To claim the ERC, employers must have:

- Sustained a full or partial suspension of their business operations due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings due to COVID-19 during 2020 or the first three quarters of 2021,
- Experienced a significant decline in gross receipts during 2020 or the first three quarters of 2021 because of COVID-19, or
- Qualified as a recovery startup business for the third or fourth quarters of 2021. (Only recovery startup businesses are eligible for the ERC in the fourth quarter of 2021.)

ERC - Circular 230 Issues

The amount of the ERC depends on various factors, including:

- the number of employees
- the amount of the employer's payroll and gross receipts
- and whether the employer paid any sick or family leave wages.

The amount of the ERC reduces the employer's allowable wage deduction on its income tax return. **Employers cannot claim the ERC for any quarter for which wages were reported as payroll costs in obtaining Payroll Protection Plan (PPP) loan forgiveness or were used to claim certain other tax credits.**

ERC - Circular 230 Issues

In its news releases, the IRS has noted that some advisers were urging employers to claim the ERC without appropriately informing them of the limitations on eligibility and the correct computation of the credit.

ERC - Circular 230 Issues

Tax Professionals' Role in ERC Compliance

The IRS's outreach efforts to employers about possible excessive ERC claims have prompted requests from tax practitioners for the IRS—and, in particular, the Office of Professional Responsibility (OPR)—to provide guidance on their obligations in connection with clients' ERC claims.

ERC - Circular 230 Issues (cont.)

Diligence as to Accuracy - Section 10.22(a)

Practitioners who prepare income, employment, and other tax returns for clients have a duty of due diligence to inquire of their clients with sufficient detail to ascertain the information necessary to determine clients' eligibility for the ERC and to claim the proper amount of the ERC on the clients' returns.



Professional Responsibility and the Employee Retention Credit

Internal Revenue Service (IRS) sent this bulletin at 03/07/2023 04:16 PM EST



Alerts from Office of Professional Responsibility (OPR)

03/07/2023

OPR Resources

[Circular 230 Tax Professionals](#)

[Circular No. 230 \(Rev. 6-2014\)](#)

[Frequently Asked Questions](#)

[Latest News and Guidance from OPR](#)

[Disciplinary Sanctions - IRB](#)

[OPR Webinars](#)

Issue Number: 2023-02

Inside This Issue

Professional Responsibility and the Employee Retention Credit

Since the Fall of 2022, the IRS has issued several warnings to employers to beware of third parties promoting improper Employee Retention Credit (ERC) claims. See IRS IR-2023-40 (Mar. 7, 2023); IRS IR-2022-183 (Oct. 19, 2022); COVID Tax Tip 2022-170 (Nov. 7, 2022). With tax filing season in full swing, tax professionals are requesting guidance to ensure they are meeting their Circular 230 professional responsibilities and the standards required to prepare and sign original tax returns, amended returns, or claims for refund relating to these credits.

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PART III

High Net Worth And Family Office Issues

- FY 2022 Audit Campaign Issue
- High-income taxpayers will continue to receive audit attention (the audit rate is approximately 9% for those reporting income of \$1 Million to \$5 Million)
 - These taxpayers often have income and losses from flow-through entities
 - Thus, the audit of an individual will often lead to the examination of various related entities

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High Net Worth Issues (cont.)

- The audit process involves a review of not only the taxpayer's personal income tax return, but also related partnership tax returns, fiduciary income tax returns, and estate and gift tax returns
- The audit is a complete review of the taxpayer(s) (*i.e.*, the IRS uses LB&I Audit Methods and Techniques)

LAW360 Tax Authority

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IRS Announces New Pass-Through Unit to Scrutinize Wealthy

By David van den Berg

Law360 (September 20, 2023, 6:33 PM EDT) - The Internal Revenue Service will launch a new group focused on scrutinizing pass-through organizations as part of its broader plan for beefing up enforcement work against the wealthy, according to an agency statement. . . [A] new unit scrutinizing pass-through organizations is part of a previously announced plan. . . to ramp up enforcement work against high-income earners, corporations and partnerships.

The agency said the initiative will drill down on large or complex pass-throughs. . . to ramp up enforcement work against high-income earners, corporations and partnerships. . .

The pass-through group will be housed in the IRS' Large Business & International Division, according to the agency. The pass-through entity's workforce will eventually also include current employees in both Large Business & International and the Small-Business & Self-Employed divisions, the agency said. The IRS' statement also said the pass-through group will include the more than 3,700 revenue agents it plans to hire for expanded enforcement work geared toward large corporations and complex partnerships. . .

IRS Announces New Pass-Through Unit to Scrutinize Wealthy (cont.)

The IRS' **strategic plan** for the funding increase provided by the Inflation Reduction Act called for expanded enforcement work against large partnerships and said the agency would hire specialized compliance workers and train others to help ensure pass-through entities comply with the law. . .

Greater resources are needed to evaluate the compliance of pass-through entities, especially large and complex ones, and pass-through audit rates dropped because of funding cuts, the agency said. . . [its] the strategic plan. The agency audited 4.4% of pass-throughs in 2010, and the rate dropped to 0.1% in 2017, the most recent year with nearly all audits closed, according to the plan, which was released in April.

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High Net Worth Issues (cont.)

- Responding to Information Document Requests can be very burdensome, with a number of practical and ethical concerns
- IRS Counsel is often involved through the audit
- Often if information is not produced by the IDR deadline the IRS will issue a pre-summons letter and then an IRS summons

High Net Worth Issues (cont.)

Some examples of the broad scope of high net worth audits include

- Estate and Gift tax issues
- **Valuation issues**
- Executive Compensation
- C corporation and S corporation issues
- Noncash charitable contributions
- **Partnership and LLC issues**
- Passive activity losses
- Foreign Trusts
- Foreign Bank Account reporting
- Basis and At-Risk issues
- Transfer Pricing Issues
- **Private airplane issues**

Department of the Treasury
Internal Revenue Service
LB&I/ECFA:NorthCentral:1721
230 South Dearborn M/S 4172
Chicago, IL 60604

Date:
10/09/2021
ID number (last 4 digits):
[REDACTED]
Form:
1040
Tax period:
201912
[REDACTED]
[REDACTED]
[REDACTED]

Dear Mr. [REDACTED] and Mrs. [REDACTED]:

Your federal return for the period(s) shown above was selected for examination.

What you need to do

Please call me on or before October 29, 2021. You may contact me from 8:00am to 3:00pm at the telephone number provided above.

During our telephone conversation, we'll talk about the items I'll be examining on your return, the types of documents I'll ask you to provide, the examination process, and any concerns or questions you may have. We'll also set the date, time, and agenda for our first meeting.

Someone may represent you

You may have someone represent you during any part of this examination. If you decide you want representation, the representative you authorize will need a completed Form(s) 2848, *Power of Attorney and Declaration of Representative*, before we can discuss any of your tax matters.

If you choose to have someone represent you, please provide a completed Form 2848 by our first appointment. You can mail or fax the form to me or have your representative provide it at the first appointment, if you won't be present. You can obtain Form 2848 from our office, from our web site, www.irs.gov or by calling (800) 829-3676.

If you filed a joint return, you and your spouse may attend the examination. If you and/or your spouse choose not to attend with your representative, you must provide completed Form(s) 2848. You should provide a separate Form 2848 for each spouse if you filed jointly even if you use the same representative.

Your rights as a taxpayer

We have enclosed Publication 1, *Your Rights as a Taxpayer* and Notice 609, *Privacy Act Notice*. The Declaration of Taxpayer Rights found in Publication 1 discusses general rules and procedures we follow in examinations. It explains what happens before, during, and after an examination, and provides additional sources of information.

A video presentation, "Your Guide to an IRS Audit," is available at <http://www.irs/videos.gov/audit>. The video explains the examination process and will assist you in preparing for your audit.
 Thank you for your cooperation and I look forward to hearing from you by [date]

Sincerely,

 Internal Revenue Agent

Enclosures:
 Publication 1
 Notice 609

Form 4564	Department of the Treasury Internal Revenue Service Information Document Request	Request Number 001
To: and	Subject: Initial IDR - Form 1040 - 201912	
	Submitted to:	
	Dates of Previous Requests:	N/A

Description of Documents Requested:

The purpose of this Information Document Request (IDR) is to obtain information relevant to your Form 1040 filed for the tax year ending December 31, 2019.

Please provide the following documentation:

1. Copies of any amended Forms 1040 (including all schedules/attachments) filed for the tax year ending December 31, 2018, December 31, 2019, and December 31, 2020.
2. Copies of any correspondence from the Internal Revenue Service concerning Form 1040 for the tax year ending December 31, 2019 excluding the Letter 2205 (initial contact letter) sent by _____.
3. Copies of all audit reports issued by any federal or state agency for tax year ending December 31, 2019.
4. Personal net worth and/or financial statement(s) as of December 31, 2019, if available. This should include the method of accounting used to compile them, net worth computations or other financial data regarding your assets, liabilities, net worth, income and losses, and cash flows from all sources within and without the United States, including all underlying documents and any applicable exhibits and/or footnotes associated therewith, and if not apparent, please identify the preparer of such documents. If not available, provide a negative written response.
5. A brief summary of your business and investment activities, including items reported on the Form 1040, Schedule E. For activities identified as non-passive, elaborate on your involvement and day-to-day role with each entity.
6. Provide a copy of the worldwide legal organization chart as of January 1, 2019 and December 31, 2019 including all domestic and foreign affiliates, places and dates of incorporation and their relationship to the reporting partnership/LLC for the entities you have greater than 50% control of through the rules of attribution. This chart should include all entities to which the Taxpayer is related within the meaning of Section 267.

Information Due By	11/05/21	At Next Appointment	<input type="checkbox"/>	Mail In	<input type="checkbox"/>
FROM	Name and Title of Requestor: Internal Revenue Agent	Badge Number: Phone: Fax: Email:	Date: 10/8/2021		
	Office Location: Internal Revenue Service; Mail Stop 4171 1, LB&L/ECFA-1113; 230 S. Dearborn; Chicago, IL 60604	Page 1 of 3			

Form 4564

Form 4564	Department of the Treasury Internal Revenue Service Information Document Request	Request Number 001
To: [redacted] and [redacted]	Subject: Initial IDR - Form 1040 - 201912	
	Submitted to:	
	Dates of Previous Requests:	N/A

Description of Documents Requested:

- The following should be included in the chart:
- Name of each entity,
 - Employer Identification Number,
 - Ownership percentage in each entity,
 - U.S. tax treatment of entity,
 - Country in which the entity was created or organized,
 - Country in which the entity operates, and
 - Business activity of the entity.

- If there is a difference in entities reported at January 1, 2019 and December 31, 2019, please provide an explanation.
- Tax return workpapers and reconciliation schedules used to prepare the Form 1040 (original and amended, if applicable) for the tax year ending December 31, 2019.
 - For all disregarded entities with activities reported on the Taxpayer's (each spouse) individual tax returns for the tax year ending December 31, 2019, please provide:
 - Detail General Ledger Transaction file (Lowest level transaction detail that can be reconciled to the Year-end Trial Balance amounts),
 - Year-end Trial Balance file showing beginning of the tax period balances and end of the tax period balances,
 - Chart of Accounts (GL Account Number, GL Account Name, Account Type),
 - LLC Operating Agreements,
 - Check-the-box elections (Form 8832), and
 - Reconciliation of the Profit and Loss records to the Form 1040 tax return.
 - Provide all Schedule K-1s issued to [redacted] and its disregarded entity/entities (flowing into Form 1040) for tax year ending December 31, 2019. Provide any Schedule K-1 workpapers and reconciliation to the 2019 tax return.

Information Due By	11/05/21	At Next Appointment	<input type="checkbox"/>	<input type="checkbox"/>
Name of Requestor:	Badge #:	Phone:	Fax:	Date: 10/8/2021
Internal Revenue Agent				
FROM	Office Location:	Internal Revenue Service; Mail Stop 4171 LB&I-ECPA-1113; 230 S. Dearborn; Chicago, IL 60604		

Form 4564	Department of the Treasury Internal Revenue Service Information Document Request	Request Number 001
To: [redacted] and [redacted]	Subject: Initial IDR - Form 1040 - 201912	
	Submitted to:	
	Dates of Previous Requests:	N/A

Description of Documents Requested:

- Any other tax returns filed for the tax years ending December 31, 2019, including Excise Tax, 1099, 1098, W-2, 940, 941, Schedule H, and Gift or Estate Tax returns.
- Copies of any gift or estate tax returns filed for the tax year ending December 31, 2019.
- Did you make gifts in excess of \$15,000 during the tax year ending December 31, 2019? If yes, specify the amount of the gift, when it was made, and the name(s) of the recipient(s).

When responding to this IDR, please identify each response to each item requested in this IDR by labeling each response with the corresponding number or letter listed in the IDR. This will help facilitate an efficient review of the information provided and decrease the likelihood of additional follow up questions. Where documents exist in electronic format, please provide in original electronic format.

Due Date: 11/05/2021

Information Due By	11/05/21	At Next Appointment	<input type="checkbox"/>	Mail To	<input type="checkbox"/>
Name of Requestor:	Badge #:	Phone:	Fax:	Date: 10/8/2021	
Internal Revenue Agent					
FROM	Office Location:	Internal Revenue Service; Mail Stop 4171 LB&I-ECPA-1113; 230 S. Dearborn; Chicago, IL 60604			

OBTAINING A "GOOD" VALUATION REPORT - The Do's and Don'ts Obtaining a "Good" Report

Privileges In a Tax Setting

- Federal Rules of Evidence - Rule 501- Privileges in General
 - Rule 501 provides that common law governs a claim of privilege unless provided otherwise by the Constitution, a federal statute, or rules prescribed by the Supreme Court. In a civil case, state law governs.
- There are a Number of Relevant Privileges
 - Attorney-Client
 - Accountant-client or practitioner privilege
 - Work Product Doctrine
 - Each can be waived
 - There are exceptions to each Recent case law
 - Spousal Privilege

Attorney-Client Privilege (cont.)

The Kovel Letter

- The Privilege Can Extend Communications with the Attorney's Agents
- So long as a client's communication is made to an agent of an attorney (*i.e.*, a CPA that has been retained by the attorney) in confidence, for the purpose of obtaining Legal Advice from the lawyer, it is privileged. *United States v. Schwimmer*, 892 F.2d 237, 243 (2d Cir. 1989).
- What is a *Kovel* Letter?
- This rule, generally known as the *Kovel* rule. The application of the *Kovel* rule can be difficult in situations where non-legal services, such as preparing a tax return, are provided with legal services because it is difficult to distinguish between communications made for the preparation of a tax return and those made for the provision of legal services. Because the *Kovel* rule rests on the attorney-client privilege, the protection of the *Kovel* rule is lost anytime the attorney-client privilege is lost.
- When to use a *Kovel* Letter.

Comment: The key is the facilitation of communication between the lawyer and client

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- How to retain an expert
 - Kovel letter
- Does my expert understand the tax law?
 - Section 2703
 - Tax affecting earnings
 - Use of a weighted average when there are multiple valuation methods
- Reliance
- Privilege waiver
- Tax Court Requirements - T.C. Rule 143(g)
- Ethically - What can I tell my experts?

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High Net Worth Issues

- Responding to Information Document Requests can be very burdensome, with a number of practical and ethical concerns
- IRS Counsel is often involved through the audit
- Often if information is not produced by the IDR deadline the IRS will issue a pre-summons letter and then an IRS summons

Qualified Appraisals

- See Goller Checklist

Lender Mgmt LLC V. Comm'r, T.C. Memo 2017-25

- Family office takes a profits interests in investments and is treated as a trade or business.

PART IV Employment Tax Issues

- New Audit Program
- Three Main Issues -
 - Employee/Independent Contractor
 - Fringe benefit issues
 - Deduction issues

October 1, 2021 - A very interesting day

Fringe Benefit Issues

- Executive compensation issues in general
- Vehicle and tool *per diem* issues
- IRS is looking at the issue of whether employees are attempting to turn “wages” into taxable *per diem* allowances
 - Carefully scrutinize what expenses can be included in a *per diem*
- Comment: Contractors who have a large amount of unreimbursed business expenses are asking for increased per diems due to the nondeductability of these expenses.

Section 530 of the Revenue Act of 1978



- Generally allows taxpayer to treat worker as not being an employee for employment tax, but not income tax or other purposes
- Must have reasonable basis and meet certain requirements

Section 530 of the Revenue Act of 1978 (cont.)

- *Reasonable basis* for treating a worker as an independent contractor exists if the taxpayer reasonably relied on
 1. Past IRS audit practice with respect to the taxpayer, or
 2. Published rulings or judicial precedent, or
 3. Long-standing recognized practice in the industry of which the taxpayer is a member, or
 4. If the taxpayer has any "other reasonable basis" for treating a worker as an independent contractor.

Section 530 of the Revenue Act of 1978 (cont.)

Comment: When section 530 relief is at issue, the IRS is supposed to consider the application of this relief before determining if an employment relationship existed.

Section 530 of the Revenue Act of 1978 (cont.)

Comment: When section 530 relief is at issue, the IRS is supposed to consider the application of this relief before determining if an employment relationship existed.

Section 530 of the Revenue Act of 1978 (cont.)

- Additional requirements
 1. The taxpayer must not have treated the worker as an employee for any period
 2. All federal tax returns, including information returns, must have been filed on a basis consistent with treating such worker as an independent contractor
 3. The taxpayer (or a predecessor) must treat all workers holding substantially similar positions consistently for purposes of employment taxes
 - The "similar worker consistency requirement"

Statute of Limitations in Employment Tax Cases

Section 6513 governs when a return is deemed to be filed for purposes of Section 6511 (i.e., for purposes of whether a claim for refund is timely filed). Subsection (c) pertains to Social Security Taxes and Income Tax Withholding (i.e., the taxes reported on a Form 941). Section 6513(c) provides that:

If a **return** for any period ending with or within a calendar year **is filed before April 15** of the succeeding calendar year, such return shall be considered filed on April 15 of such succeeding calendar year.

§ 6513(c)(1). (Emphasis added.)

Thus, when a Form 941 for a period is filed before April 15 of the following period, the tax return is considered filed on April 15 of that following year.

Interest-Free Adjustments

- Generally, for employment tax (i.e., Form 941 obligations), if the adjustment to the Form 941 (i.e., the tax deficiency) is
 - paid on or before the due date of the 941 for the period in which the error is "ascertained,"
 - the amount of the underpayment shall be paid without interest being charged.
- An error is ascertained when resolved at examination or with appeals.

Interest-Free Adjustments (cont.)

- If, however, the case is not resolved at Appeals and the taxpayer receives a notice and demand for payment from the IRS, the adjustment will not be interest free.
- In addition, the taxpayer will not be allowed an interest free adjustment where a prior audit found that additional tax was due with respect to the same issue.

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Make Sure During the Audit That the Burden of Proof Will Switch at Trial

- Burden to IRS
 - In most civil controversies, a rebuttable presumption existed that the IRS's determination of tax liability is correct
 - *i.e.*, the taxpayer has the burden of proving the IRS is wrong
 - Section 7491 switched the burden to the government in any non-criminal court proceedings, regarding a factual issue, if the taxpayer introduces credible evidence, which is relevant to determination of its liability.

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Switching the Burden of Proof to the IRS

- Burden of proof can be important in valuation cases.
- This is especially so if the IRS does not obtain a good valuation report.
- Thus, failure to shift the burden can be a significant malpractice issue.

Comment: Given IRS budget issues, it is more difficult for the IRS to obtain a solid valuation report.

Make Sure During the Audit That the Burden of Proof Will Switch at Trial (cont.)

- The requirement to prove credible evidence means that the burden technically starts out on the taxpayer, but shifts to the government unless the taxpayer produces evidence that would enable the court to find in favor of the taxpayer, absent any contrary evidence being produced by the IRS and ignoring the judicial presumption of IRS correctness.

Make Sure During the Audit That the Burden of Proof Will Switch at Trial (cont.)

- Finally, the shift in the burden of proof applies to all income, gift, estate, generation-skipping, taxes and all penalties in addition to tax
 - However, it does not apply to corporations, partnerships or trusts with the net worth exceeding \$7 million (book value)

CONCLUSION

8:15 – 9:20 a.m.

Wisconsin Tax Update

Kristina Somers, JD, *Shareholder, Reinhart Boerner Van Deuren s.c.*

Wisconsin Tax Update WICPA 2023 Tax Conference November 3, 2023

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Overview

- Sales/Use Tax
- Income/Franchise Tax and Pass-Through Withholding
- Property Taxes, Special Assessments, TIF Districts, Transportation Utility Fees
- Unclaimed Property
- Excise Taxes
- Miscellaneous

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Sales/Use Tax

Recent Laws, Cases, Other Guidance

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Exemptions / Exclusions / Deductions

Sales/Use Tax

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Trailer Type Vehicles - Do Not Qualify for Sales/Use Tax Exemption for "Truck Bodies"

- *William Becker v. Wisconsin Department of Revenue* (WTAC Dec. 29, 2020).
- **Wis. Stat. § 77.54. General Exemptions.** There are exempted from the taxes imposed by this subchapter:
 - (5)(a)4. Motor vehicles or **truck bodies** sold to persons who are not residents of this state and who will not use such motor vehicles or trucks for which the truck bodies were made in this state otherwise than in the removal of such motor vehicles or trucks from this state.

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Trailer Type Vehicles - Do Not Qualify for Sales/Use Tax Exemption for "Truck Bodies" (cont'd)

- **Wis. Admin. Code § Tax 11.83. Motor Vehicles.**
 - (4) PURCHASES BY NONRESIDENTS.
 - (a) The sales price for the sales of motor vehicles or **truck bodies** to nonresidents of Wisconsin, including members of the armed forces, who will not use the vehicles or trucks for which the truck bodies were made in Wisconsin other than their removal from Wisconsin is exempt. Truck bodies include semi-trailers. However, the separate sale of a "slide-in" camper to a nonresident is taxable if the sale is sourced to Wisconsin as provided in § 77.522.
- Trailer type vehicles sold:
 - Single Axle
 - Tandem Axle
 - Gooseneck

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Trailer Type Vehicles - Do Not Qualify for Sales/Use Tax Exemption for "Truck Bodies" (cont'd)

- Prior case (*Dep't of Revenue v. Trudell Trailer Sales, Inc.*, 104 Wis. 2d 39, 42, 310 N.W.2d 612 (1981)) held:
 - A semitrailer is built to and does carry the cargo. Without it or some other unit to carry the load, a tractor, which is the power unit, serves little or no purpose. When the two pieces of equipment are joined, the semitrailer is the "truck body," and it fits that definition and purpose when constructed and sold. No basis exists for distinguishing that type of truck body from one with a self-contained motor.
- All trailers designed to haul cargo ≠ "truck bodies."
- Must be a symbiotic relationship between (i) trailers sold and (ii) motor vehicles that power their movement.
- Here, automobiles and pickup trucks do not require "truck bodies."
- **Wisconsin Tax Appeals Commission** concluded: trailers did not qualify for exemption.

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Trailer Type Vehicles - Do Not Qualify for Sales/Use Tax Exemption for "Truck Bodies" (cont'd)

- Circuit Court (La Crosse Co. June 27, 2022):
 - Reviewed whether semitrailer definition extends to other trailers that require the support of a motor vehicle to hold cargo.
 - Concluded trailers = exempt "truck bodies"
 - Reversed the Wisconsin Tax Appeals Commission.
 - Appealed by the Wisconsin Department of Revenue to the Court of Appeals.

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Trailer Type Vehicles - Do Not Qualify for Sales/Use Tax Exemption for "Truck Bodies" (cont'd)

- Court of Appeals, 2022AP1349 (July 25, 2023) (unpublished):
 - Reversed the Circuit Court and affirmed the Wisconsin Tax Appeals Commission determination.
 - "As the DOR asserts, the language that 'trucks for which the truck bodies were made' requires that the truck body be a part of a complete truck. Becker's trailers are not made to be a part of a complete truck. Rather, they are pulled behind trucks or cars. Thus, they are not truck bodies under the plain language of the statute." 2022AP1349, ¶ 12.

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Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply

- *Citation Partners, LLC v. Wisconsin Department of Revenue* (WTAC Dec. 4, 2019).
- Citation Partners owns a Cessna Citation aircraft.
- 2013 Wis. Act 185 provided sales tax exemption for:
 - Parts used to modify or repair aircraft.
 - Aircraft maintenance services.

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Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Wisconsin Tax Appeals Commission found:
 - Lessor was obligated to arrange for and pay all repair and maintenance.
 - Lease payments were not partial reimbursement for repair and maintenance parts or services.
 - Exemption did not apply -> lease payments = fully taxable.

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Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Wisconsin Tax Appeals Commission did note that lessor's purchases of aircraft maintenance and repair services = exempt.
- Dodge County Circuit Court (Case No. 19-CV-612; August 20, 2020) - reversed in favor of the taxpayer.
 - Citation = agent of lessees.
 - Exemption applied, as it would apply to any direct purchaser of repairs, maintenance, or parts.

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Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Reversed by the Wisconsin Court of Appeals on November 23, 2021 (2020AP1683).
 - Lease payments subject to tax.
 - "Sales tax cannot be avoided by dividing up a lease price into categories or affixing labels."

Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Plain language of the statute (Wis. Stat. § 77.52(2)(a)10) exempts "the repair, service, alteration, fitting, cleaning, painting, coating, towing, inspection, and maintenance of any aircraft or aircraft parts"
- The plain language "does not exempt a lease from sales tax."
- Exemptions are strictly construed.

Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Affirmed by the Wisconsin Supreme Court on March 1, 2023 (2023 WI 16).
 - 4-3 decision
- Majority:
 - Looked to definitions of:
 - "Sales price" = "the total amount of consideration" - with no deduction for seller's or lessor's costs.

Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Found "[a]s part of the total amount the Lessees pay to lease the aircraft, Citation Partners charges per-flight-hour rates for aircraft repairs and engine maintenance."
- Acknowledged rates correspond to amount Citation spends on aircraft repairs and engine maintenance.
- But concluded per-flight-hour charges for aircraft repairs and engine maintenance = part of total consideration for lease of aircraft.

Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Deferred to Commission's findings of fact.
- Reviewed legal conclusions de novo.
 - Found that Citation Partners did not sell its Lessees "parts used to modify or repair aircraft" or "repair, service . . . and maintenance of any aircraft."
 - Rather, found that it is leasing an aircraft, not selling aircraft repairs or maintenance.
 - No agency relationship - Lessees had no right of control.

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Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Dissent:
 - Focused on the aircraft exemption provisions - and concluded that the "plain meaning of those statutes grants Citation Partners the sales tax exemption it seeks."
 - Found "the majority chooses to follow the error-strewn path of the Tax Appeals Commission (TAC), which contravenes the clear statutory direction to exempt the sale price of aircraft parts and aircraft maintenance from state sales taxes"

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Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Found "the legislature granted a broad exemption for the sales price of aircraft parts."
- Concluded "the TAC's material factual findings that underlie its legal conclusion are not supported by substantial evidence"
 - For example, the TAC found the Lessee's responsibilities did not include any maintenance related expenses - but the dissent read the relevant agreement to require Lessee to be responsible for maintenance.

Lease Payments - Aircraft Maintenance Services / Parts Exemption -> Does Not Apply (cont'd)

- Also found the TAC ignored the jointly-submitted Stipulation of Facts.
- Concluded TAC's material findings must be set aside.
- Found that "there is nothing in either statute that limits its use when obligations to pay for aircraft maintenance and parts are incurred pursuant to written documents rather than directly to the vendor."
- Focused on the more specific statutes.
- Noted that the majority did not review the TAC's decision.

Indirect Materials - Purchased for Resale to Federal Government

- *Oshkosh Corporation v. Wisconsin Department of Revenue* (WTAC Oct. 10, 2022).
- Contracts with federal government.
 - Direct materials (e.g., raw materials) purchased.
 - Indirect materials (e.g., office supplies and equipment, computer supplies and equipment, building repairs and supplies, repairs to security cameras, crane inspection, gas purchases, building prototypes, hand tools, cleaning supplies, vehicle leases, landscaping services and supplies, books, and training supplies) purchased.

Indirect Materials - Purchased for Resale to Federal Government (cont'd)

- Indirect materials:
 - Reimbursed by - but not physically transferred to federal government.
 - Federal Acquisition Regulations - provided for the transfer of title to indirect materials from a contracting party to the federal government.
- Refund claims

Indirect Materials - Purchased for Resale to Federal Government (cont'd)

- Wis. Stat. § 77.51:
 - (13m) "Retail sale" or "sale at retail" means any sale, lease, or rental for any purpose other than resale, sublease, or sub rent.
 - (14) "Sale" includes any of the following: the transfer of the ownership of, title to, possession of, or enjoyment of tangible personal property, or items, property, or goods under s. 77.52(1)(b), (c), or (d)"

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Indirect Materials - Purchased for Resale to Federal Government (cont'd)

- Wisconsin Tax Appeals Commission concluded that the statutory language straightforwardly includes the transfer of title to tangible personal property.
- Expressed concern that "businesses can evade paying taxes in the State of Wisconsin by creating what amounts to a fictional resale, but which satisfies the letter of the law."
- Asks "Does this mean that a furniture manufacturer can now contract with a large client to transfer the title of their office supplies and operating equipment, avoiding taxation?"

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Indirect Materials - Purchased for Resale to Federal Government (cont'd)

- Circuit Court (Dane Co. June 29, 2023).
- Affirmed WTAC ruling and order.
- When Oshkosh transferred title of indirect materials to the federal government as dictated by the model provisions of the Federal Acquisitions Regulations in their contract, this was sufficient to be a "sale" under the plain meaning of Wis. Stat. § 77.51(14).

Indirect Materials - Purchased for Resale to Federal Government (cont'd)

- Circuit Court reasoned the transfer of title was more than a "legal fiction" because the contract terms vest title and beneficial ownership in the federal government:
 - The indirect materials are limited to use in connection with federal contracts.
 - The federal government retains the right to access, inspect, and control the disposal of indirect materials.
 - The federal contracts define and allocate risk of loss for indirect materials.

Sales/Use Tax Exemption for Data Center Equipment and Materials

- 2023 Wis. Act 19 created sales/use tax exemption under Wis. Stat. § 77.54(70) for certain tangible personal property used at a data center.
- Effective October 1, 2023.

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 77.54(70)(a)
- The sales price of tangible personal property "used exclusively for the **development, construction, renovation, expansion, replacement, repair, or operation** of a **qualified data center**, as defined in s. 238.40(1)(b)"

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 77.54(70)(a)

". . . and **used solely** at the qualified data center including computer server equipment and the chassis for such equipment; networking equipment; switches; racks; fiber-optic cabling, copper cabling, and other cabling, including cabling used to connect one or more qualified data centers; trays; conduit; substations; uninterruptible energy equipment; supplies; fuel piping and storage; duct banks; switches; switchboards; batteries; testing equipment; backup generation equipment; modular data centers and preassembled components; monitoring equipment; security systems; and electricity."

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 77.54(70)(b)

- The sales price of tangible personal property "used in the **development, construction, renovation, expansion, replacement, or repair** of a **water cooling or conservation system used exclusively** to cool or conserve water for one or more qualified data centers"

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 77.54(70)(b)
". . . including chillers, mechanical equipment, refrigerant piping, fuel piping and storage, adiabatic and free cooling systems, cooling towers, water softeners, air handling units, indoor direct exchange units, fans, ducting, and filters."

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 77.54(70)(c)
- The sales price of tangible personal property "sold to a construction contractor that, in fulfillment of a real property construction activity, transfers the tangible personal property or property under § 77.52(1)(c) to a qualified data center, as defined in § 238.40(1)(b), if such tangible personal property or property under § 77.52(1)(c) becomes a component of the qualified data center."

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 238.40(1)(b):
- A "qualified data center" means one or more buildings owned, leased, or operated by the same business entity or its affiliate. The buildings must be used to centralize the processing, storage, management, retrieval, communication, or dissemination of data and information.

Sales/Use Tax Exemption for Data Center Equipment and Materials (cont'd)

- Wis. Stat. § 238.40:
- The Wisconsin Economic Development Corporation ("WEDC") is responsible for certifying a qualified data center for purposes of the exemption.
- The buildings must create a minimum qualified investment in the state within 5 years from the date WEDC certifies the data center (e.g., \$50,000,000 for buildings in a county having a population of not more than 50,000).

Increase in Retailer's Discount

- 2023 Wis. Act 19 amends Wis. Stat. § 77.61(4)(c).
- Increases retailer's collection discount deduction from 0.5% to 0.75% of the tax payable and the discount limit will increase from \$1,000 to \$8,000 maximum.
- Applies to sales and use taxes payable after October 1, 2023.

Increase in Retailer's Discount (cont'd)

- The retailer's discount is computed on the total sales tax as follows:
 - \$0 to \$10 - discount is equal to total sales tax
 - \$10 to \$1,333 - discount is \$10
 - Greater than \$1,333 - discount is the total sales tax amount x .0075, but cannot exceed \$8,000 per reporting period

Imposition

Sales/Use Tax

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City of Milwaukee and Milwaukee County - Higher Sales/Use Taxes

- 2023 Wis. Act 12 authorized the City of Milwaukee to impose a 2% sales/use tax under Wis. Stat. § 77.701 and Milwaukee County to impose a 0.4% sales/use tax under Wis. Stat. § 77.70. Effective June 22, 2023.
 - City of Milwaukee Common Council voted to impose the City sales/use tax of 2%, effective January 1, 2024.
 - Milwaukee County Board raised the county sales/use tax from 0.5% to 0.9%, effective January 1, 2024.

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City of Milwaukee and Milwaukee County - Higher Sales/Use Taxes (cont'd)

- Total sales/use tax rate in City of Milwaukee = 7.9%
- Total sales/use tax rate in Milwaukee County (outside City of Milwaukee) = 5.9%
- Total sales/use tax rate in other counties = 5.00 - 5.50%

Online Marketplace - Liable for Sales Tax on Admissions

- *StubHub, Inc. v. Wisconsin Department of Revenue* (WTAC Feb. 28, 2023).
- Sales of tickets/admissions - 2008 -> 2013
- What is being sold?
 - Ticket = Right to admission (represented by the ticket)
 - Tickets not separate from the admissions
 - "This novel argument is not persuasive to the Commission, and the Commission declines to upend years of precedent."

Online Marketplace - Liable for Sales Tax on Admissions

- Who is selling the tickets?
 - User Agreement - expressly disclaims agency relationship
 - Anonymity of ticketholder
- Does it matter who owns the property or services being transferred?

Online Marketplace - Taxable for Sales of Admissions (cont'd)

- What is StubHub selling/what services is it providing?
 - Similar to auctioneer?
 - FanProtect Guarantee - StubHub would find replacement tickets or offer a refund.
 - More than a passive marketplace - "no open-air market with which the Commission is familiar offers, on behalf of a stall holder in the market, replacement products or refunds for items which prove unsatisfactory to consumers."

Online Marketplace - Taxable for Sales of Admissions (cont'd)

- Final sales price
 - StubHub sets its fees -> added to the price set by the ticketholder = StubHub determined the final sales price.
 - "StubHub's complete control over the ultimate purchase price paid by the ticket buyer, as well as StubHub's control over the receipt and accounting of payment made by the ticket buyer"

Online Marketplace - Taxable for Sales of Admissions (cont'd)

- Retailer?
 - "[T]he statute does not require that a person making a sale at retail be or be deemed to be a retailer in order for its sales to be subject to tax."
- Nexus
- Penalties
 - Not applicable - Tax Bulletins 114 and 172 applied only to "ticket brokers"

Administrative Rules - Marketplace Providers and Sellers

- Changes published in Administrative Register 810B, CR 22-017. Effective July 1, 2023.
- Wis. Admin. Code § Tax 11.55 is renamed from "Agents, consignees, lienors, and brokers" to "Repossessions and sales of property to enforce liens."
- Wis. Admin. Code § Tax 11.55(1) and (2), relating to disclosed and undisclosed principals - repealed.

Administrative Rules - Marketplace Providers and Sellers (cont'd)

- Persons selling products and services on behalf of others are retailers and must collect tax regardless of whether the person they are selling on behalf of is disclosed to the purchaser.
- These agents, consignors, and brokers are often "marketplace providers" under the provisions created in 2019 Wis. Act 10, effective January 1, 2020.

Administrative Rules - Marketplace Providers and Sellers (cont'd)

- Wis. Admin. Code § Tax 11.555 "Marketplace providers and sellers" explains the various requirements by all types of sellers that facilitate sales of taxable products and services on behalf of other sellers.

Administrative Rules - Marketplace Providers and Sellers (cont'd)

- Wis. Admin. Code § Tax 11.555 provides information about:
 - Marketplace provider's requirement to notify the seller they are collecting and remitting tax
 - Who can be audited and held liable for tax
 - Requests for waiver from marketplace provider responsibilities
 - When the Department of Revenue may regard the seller as a retailer

Administrative Rules - Marketplace Providers and Sellers (cont'd)

- Wis. Admin. Code § Tax 11.555 provides information about:
 - Marketplace provisions applying to both online and physical marketplaces
 - Reporting and recordkeeping requirements
 - A marketplace being required to collect and remit tax on taxable sales it facilitates on behalf of a nonprofit organization, even if the nonprofit organization would qualify for the occasional sales exemption.

Administrative Rules - Marketplace Providers and Sellers (cont'd)

- Wis. Admin. Code § Tax 11.88(6), "Consignment sales," was repealed and recreated to explain that a recreational vehicle dealer that advertises and sells a recreational vehicle on behalf of another person is a marketplace provider and required to collect and remit the tax.

Classification of Property

Sales/Use Tax

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Definition of "Real Property Construction Activities"

- 2023 Wis. Act 12, amends Wis. Stat. § 77.51(12t):

"Real property construction activities" means "activities that occur at a site where tangible personal property or items or goods under s. 77.52(1) (b) or (d) that are applied or adapted to the use or purpose to which real property is devoted are permanently affixed to that real property."

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Definition of "Real Property Construction Activities" (cont'd)

- Wis. Stat. § 77.51(12t):
- "Real property construction activities" does "not include affixing property subject to tax under s. 77.52(1)(c) to real property or affixing to real property tangible personal property that remains tangible personal property after it is affixed."

Definition of "Real Property Construction Activities" (cont'd)

- Wis. Stat. § 77.51(12t):

"The department may promulgate rules to determine whether activities that occur at a site where tangible personal property or items or goods under s. 77.52(1)(b) or (d) are affixed to real property are real property construction activities for purposes of this subchapter."

Changes to Definition of "Real Property Construction Activities" (cont'd)

- Wis. Stat. § 77.51(12t):

"If the classification of property or an activity is not identified by rule, the department's determination of whether personal property becomes part of real property shall be made by considering the following criteria:

- (a) Actual physical annexation to the real property.
- (b) Application or adaptation to the use or purpose to which the real property is devoted.
- (c) An intention on the part of the person making the annexation to make a permanent accession to the real property."

Proposed Legislation

Sales/Use Tax

Expanding Electricity and Natural Gas Exemption

- 2023 Senate Bill 22 and 2023 Assembly Bill 20 proposed expanding the exemption for electricity and natural gas to all months of the year.
- The exemption currently only applies to electricity and natural gas sold from November through April for residential use.

Income/Franchise Tax and Pass-Through Withholding

Recent Laws, Cases, and Other Guidance

Deductions / Refund Claims

Income/Franchise Tax

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Royalty Deduction - Disallowed

- *Skechers USA, Inc. v. Wisconsin Department of Revenue* (WTAC Feb. 24, 2023).
- Entities:
 - Skechers USA, Inc. ("Skechers") = Corporation headquartered in California
 - Skechers USA Inc. II ("SKII") = Delaware corporation (subsidiary)
 - Corporate franchise tax assessments of Skechers USA, Inc. - tax years 2000 and 2001-2003

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Royalty Deduction - Disallowed (cont'd)

- Skechers contributed its domestic intellectual property to SKII
- Licensing agreement
 - Skechers required to pay operating margin (in excess of 2%) to SKII as royalty
 - Skechers claimed Wisconsin franchise tax deduction for royalties paid
- Wisconsin Department of Revenue disallowed deductions claimed by Skechers

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Royalty Deduction - Disallowed (cont'd)

- Wis. Stat. § 71.30(2):

ALLOCATION OF GROSS INCOME, DEDUCTIONS, CREDITS BETWEEN 2 OR MORE BUSINESSES. In any case of 2 or more organizations, trades or businesses (whether or not incorporated, whether or not organized in the United States and whether or not affiliated) owned or controlled directly or indirectly by the same interests, the secretary or his or her delegate may distribute, apportion or allocate gross income, deductions, credits or allowances between or among such organizations, trades or businesses, if he or she determines that such distribution, apportionment or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades or businesses
- *Hormel Foods Corp. v. Wisconsin Dep't of Revenue* (WTAC Mar. 29, 2010)

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Royalty Deduction - Disallowed (cont'd)

- Non-tax intellectual property benefits & economic substance?
 - Identify and protect existing intellectual property
 - Number of SKII employees increased
 - Larger office space needed
 - Third party licensing revenue grew
- Sham transaction?
 - KPMG - State Tax Minimization Project
 - No changes in operations or management of the intellectual property

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Refund Claim for Manufacturing Credit - Barred

- *General Mills, Inc. v. Wisconsin Department of Revenue* (WTAC Oct. 26, 2022).
- 2013 tax year:
 - Originally filed return - manufacturing credit not claimed.
 - Field audit.
 - Subsequent to the field audit, amended 2013 return filed - on July 21, 2017 (before the end of the four-year statute of limitations, which expired August 15, 2018).
 - Second amended 2013 return filed on August 15, 2018.

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Refund Claim for Manufacturing Credit - Barred (cont'd)

- Wis. Stat. § 71.75:

* * *

(2) With respect to income taxes and franchise taxes, except as otherwise provided in subs. (5) and (9) . . . refunds may be made **if the claim therefor is filed within 4 years of the unextended date** under this section on which the tax return was due.

* * *

(4) Except as provided in subs. (5) and (5m), no refund shall be made . . . for any year that has been the subject of a field audit if the audit resulted . . . in an assessment that is final . . . and if the department of revenue notifies the taxpayer that unless the taxpayer appeals the result of the field audit . . . the field audit is final."

Refund Claim for Manufacturing Credit - Barred (cont'd)

- Wis. Stat. § 71.75:

* * *

(5) A claim for refund may be made within 4 years after the assessment of a tax . . . including penalties and interest, under this chapter, assessed by office audit or field audit and paid if the assessment was not protested by the filing of a petition for redetermination. . . . If a claim is filed under this subsection, the department of revenue may make an additional assessment in respect to any item of income or deduction that was a subject of the prior assessment. No claim for refund may be made in respect to items that were not adjusted in the notice of assessment or of refund."

Refund Claim for Manufacturing Credit - Barred (cont'd)

- Wisconsin Department of Revenue - argued refund claim barred (under Section 71.75(5)) because the manufacturing credit was not a subject of the audit and assessment.
- Taxpayer - argued it followed the permitted time period (under Section 71.75(2)) to file a refund claim.
- Wisconsin Tax Appeals Commission - concluded "Section 71.75(5) Wis. Stat. bars a claim for refund in respect to items *not adjusted in the notice of assessment or refund.*"

Imposition

Income/Franchise Tax

Pass-Through Withholding Filings Required - Based on Wisconsin Income

- *RADS Partnership et al. v. Wisconsin Department of Revenue* (WTAC Aug. 16, 2022).
- Watermark Wisconsin LP = California limited partnership with principal offices in California.
 - Invested in Watermark Montclair Wisconsin Hotels LLC - which invested in real estate in Wisconsin.
- Taxpayers (CA/DE limited partnerships, partnership, and trust with principal location in California) = limited partners in Watermark Wisconsin LP.
 - All partners of the partnerships and beneficiaries of the trust = California residents.

Pass-Through Withholding Filings Required - Based on Wisconsin Income (cont'd)

- Mostly ordinary losses for tax years 2006-2013.
- Income (section 1231 gain) for 2013.
- Wisconsin Department of Revenue assessed:
 - Pass-through withholding tax (plus interest, underpayment interest, penalties, and late filing fees) for the pass-through entities.
 - Fiduciary tax (plus interest, penalties, and late filing fees) for the trust.

Pass-Through Withholding Filings Required - Based on Wisconsin Income (cont'd)

- Wis. Stat. § 71.775(2)(a):

For the privilege of **doing business in this state** or **deriving income from property located in this state**, a **pass-through entity** that has **Wisconsin income** for the taxable year that is **allocable to a nonresident partner, member, shareholder, or beneficiary** shall pay a **withholding tax**.

- Wis. Stat. § 71.775(1)(b):

"Pass-through entity" means a **partnership**, a limited liability company, a tax-option corporation, an estate, or a **trust** that is treated as a pass-through entity for federal income tax purposes.

Pass-Through Withholding Filings Required - Based on Wisconsin Income (cont'd)

- Wis. Stat. § 71.775(3):

(3) EXEMPTIONS

- (a) A nonresident partner's, member's, shareholder's, or beneficiary's share of **income** from the pass-through entity that is attributable to this state shall not be included in determining the withholding under sub. (2) if any of the following applies:

* *

2. The partner's, member's, shareholder's, or beneficiary's share of **income** from the pass-through entity that is attributable to this state is less than \$1,000.

Pass-Through Withholding Filings Required - Based on Wisconsin Income (cont'd)

- Wis. Stat. § 71.80(25):
 - (25) Net operating and business loss carry-forward and carry-back.
 - (a) No offset of Wisconsin income may be made under s. 71.05(8)(b)1., 71.26(4)(a), or 71.45(4)(a) unless the incurred loss was computed on a return that was filed within 4 years of the unextended due date for filing the original return for the taxable year in which the loss was incurred.

Pass-Through Withholding Filings Required - Based on Wisconsin Income (cont'd)

- Wisconsin Tax Appeals Commission concluded:
 - Income triggered pass-through withholding and obligation/trust (fiduciary tax) filing and payment obligation
 - Failure to submit required forms within 4 years of the unextended due date of the 2013 return (April 15, 2018) resulted in obligation to pay pass-through withholding/fiduciary tax.

Income Taxable for Online Sales Platform?

- *ASAP Cruises, Inc. v. Wisconsin Department of Revenue* (WTAC May 23, 2022).
- ASAP Cruises provides online platform through which independent travel agents book travel for their customers.
- Tax Years 2012-2017.

Income Taxable for Online Sales Platform? (cont'd)

- Wisconsin Tax Appeals Commission concluded that:
 - ASAP Cruises sold travel services.
 - ASAP Cruises used the services of Independent Travel Consultants (who were paid commissions).
 - ASAP Cruises was doing business in Wisconsin.
 - Travel services are not tangible personal property.
 - Travel services are not protected by Public Law 86-272.

Income Taxable for Online Sales Platform? (cont'd)

- Circuit Court (Dane Co. May 31, 2023):
 - Found that the Wisconsin Tax Appeals Commission improperly granted summary judgment.
 - Regarding the affidavit provided by ASAP Cruises, the Circuit Court found: "in the light most favorable to ASAP, a reasonable person could infer . . . that ASAP's business activity was not to sell services but was instead to sell the software contained on its online platform."

Income Taxable for Online Sales Platform? (cont'd)

- The material dispute created by the affidavit testimony is genuine.
- The standard is not whether the affidavit testimony is "self-serving" or other "evidence in the record . . . corroborates [the] statement."
- Wisconsin Tax Appeals Commission "committed a procedural error when it granted summary judgment."

Early Withdrawal from 401(k) - Penalty

- *Scott Cech v. Wisconsin Department of Revenue* (WTAC June 5, 2023).
- Taxpayer took an early distribution from his 401(k) plan and used most of the funds on a first home purchase.
- Taxpayer included the amount of the distribution in his federal and Wisconsin tax returns as taxable income, but did not report an early withdrawal penalty on either return.

Early Withdrawal from 401(k) - Penalty (cont'd)

- I.R.C. § 72(t)(1) imposes additional tax on early distributions from a "qualified retirement plan."
- I.R.C. § 4974 defines "qualified retirement plan."
- Pursuant to Wis. Stat. § 71.83(1)(a)(6), "[a]ny natural person who is liable for a penalty for federal income tax purposes under . . . § 4974 . . . of the Internal Revenue Code is liable for 33 percent of the federal penalty"

Early Withdrawal from 401(k) - Penalty (cont'd)

- The I.R.C. § 72(t)(2)(F) exception to the early withdrawal penalty for first time homebuyers applies to distributions from an "individual retirement plan" and only up to \$10,000.
- Central issue was whether a 401(k) is an "individual retirement plan" within the meaning of the first time homebuyer exception to either the Wisconsin or federal early distribution penalties.

Early Withdrawal from 401(k) - Penalty (cont'd)

- The *pro se* taxpayer made no legal arguments addressing the main issue and did not prove his entitlement to the exemption.
- The Wisconsin Tax Appeals Commission cited an IRS webpage "Retirement Topics - Exceptions to Tax on Early Distributions" as the most helpful source in assessing the issue.

Early Withdrawal from 401(k) - Penalty (cont'd)

"Retirement Topics - Exceptions to Tax on Early Distributions"

Exception	The distribution will NOT be subject to the 10% additional early distribution tax in the following circumstances:	Qualified Plans (401(k), etc.)	IRA, SEP, SIMPLE IRA* and SARSEP Plans	Internal Revenue Code Section(s)
Homebuyers	qualified first-time homebuyers, up to \$10,000	no	yes	72(t)(2)(F)

<https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-tax-on-early-distributions>

Retirement Plan Distributions - Taxed

- *Edward Lewis v. Wisconsin Department of Revenue* (WTAC Dec. 6, 2022).
- Tax years 2016, 2017, 2018, and 2019
 - IRS audited 2016
 - On audit, Wisconsin taxed distributions from retirement plans and assessed early withdrawal penalties.
 - Wisconsin Department of Revenue filed motion for summary judgment.
 - Taxpayer did not file any responsive pleadings.

Individual Income Tax Rate - Decrease

- 2023 Wis. Act 19 reduced tax rate for first and second brackets. Effective for taxable years beginning after December 2022.
- Individual income tax rate for the first bracket reduced from **3.54% to 3.5%**. Applies to (a) fiduciaries, single individuals and heads of household on the first \$13,810 of taxable income; (b) married persons filing jointly on the first \$18,420 of taxable income; and (c) married persons filing separately on the first \$9,210 of taxable income.

Individual Income Tax Rate - Decrease (cont'd)

- Individual income tax rate for the second tax bracket reduced from **4.65% to 4.40%**.
- The second bracket applies to (a) fiduciaries, single individuals and heads of household on taxable income exceeding \$13,810 but not exceeding \$27,630; (b) married persons filing jointly on taxable income exceeding \$18,420 but not exceeding \$36,840; and (c) married persons filing separately on taxable income exceeding \$9,210 but not exceeding \$18,420.

Apportionment of Income of Interstate Brokers-Dealers, Investment Advisers, Investment Companies, and Underwriters

- 2023 Wis. Act 19 revises the apportionment rule (Tax 2.495) regarding brokerage houses, investment advisers, investment companies, and underwriters.
- Applies retroactively to taxable years beginning on January 1, 2022.

Apportionment of Income (cont'd)

- Department of Revenue's authority to substitute net gains (net of commissions) from sales of trading assets does not apply to any taxpayer who:
 - before January 1, 2023, elected to use the customer billing address method and has not revoked that election and;
 - for any taxable year beginning on or after January 1, 2022, determines its receipts factor by using the average of the receipts factors determined using gross receipts, net of commissions, and net gain, net of commissions, from sales of trading assets for the taxable year, with all other components of the receipts factor remaining the same.

Apportionment of Income (cont'd)

- Any such taxpayer may compute its receipts factor using that averaging method.
- The Department of Revenue cannot require any taxpayer who elected before January 1, 2023, to use the customer billing address method, and who has not revoked that election, to use any other method of determining its receipts factor.

Credits

Income/Franchise Tax

Manufacturing and Agricultural Credit

- 2023 Wis. Act 12 made changes to the manufacturing tax credit to limit any effect on the ability of taxpayers who only have personal property assessed as manufacturing property to claim the manufacturing credit.
- Effective for taxable years beginning after December 31, 2023.

Manufacturing and Agricultural Credit (cont'd)

- Any establishment classified as manufacturing prior to January 1, 2024, is presumed to be engaged in manufacturing and does not need to submit an application.

Manufacturing and Agricultural Credit (cont'd)

Manufacturing Classification

- A person wishing to classify their establishment as manufacturing must file an application no later than July 1 of the taxable year to claim the credit.
- The Department of Revenue must make a determination and provide written notice by December 31.
- A determination regarding classification may be appealed to the State Board of Assessors.

Manufacturing and Agricultural Credit (cont'd)

- Changes to Wis. Stat. § 71.07(5n) definition of "Manufacturing Property Factor"
- The term "real and personal property assess under s. 70.995" is replaced by "land and depreciable property" in both the numerator and denominator.

Manufacturing and Agricultural Credit (cont'd)

Qualified Production Property

- 2023 Wis. Act 12 expanded the definition of "qualified production property" for purposes of claiming the manufacturing credit to include tangible personal property manufactured in whole or in part by the claimant at an establishment located in Wisconsin and classified as manufacturing under Wis. Stat. § 70.995(5n).

Manufacturing and Agricultural Credit (cont'd)

- "Qualified production property" includes tangible personal property manufactured on property located in Wisconsin and assessed as manufacturing property or approved to be classified as manufacturing real property under Wis. Stat. § 70.995, even if it is not eligible to be listed on the manufacturing roll until January 1 of the following year.

Manufacturing and Agricultural Credit (cont'd)

Eligible Qualified Production Activities Income

- If the claimant's entire qualified production activities income results from the sale of tangible personal property that was manufactured, produced, grown, or extracted entirely in Wisconsin by the claimant, it is not necessary to multiply the qualified production activities income by the manufacturing or agricultural property factor.

Research Credit

- 2023 Wis. Act 19 increased the refundable portion of the research credit.
 - For taxable years beginning after December 31, 2023.
 - Lesser of (i) 25% of the current research credit or (ii) the unused amount after subtracting the current year research credit used to offset any tax liability.

Research Credit (cont'd)

- Wisconsin Department of Revenue issued Publication 131 in August 2023, updating its guidance on tax incentives for conducting qualified research in the state, including:
 - What constitutes qualified research
 - How to claim the research credit and sales/use tax exemption
 - What records the taxpayer must keep to document qualified research

Research Credit (cont'd)

Wisconsin Department of Revenue Publication 131

- The updated publication notes that Wisconsin laws define which expenses are eligible to be used in the calculation of the credit by referencing the definition of "qualified research" found at IRC Sec. 41 and the related federal regulations.
- However, because Wisconsin has not adopted Sec. 13206 of the Tax Cuts and Jobs Act (P.L. 115-97), the pre-2022 rules apply for Wisconsin purposes.

Miscellaneous

Disclosure to Wisconsin Economic Development Corporation

- 2023 Wis. Act 19 expands the Wisconsin Economic Development Corporation ("WEDC") authority to examine tax returns to the extent necessary to administer tax benefit programs, including review of tax benefit applications, compliance with tax benefit certifications, and the confirmation of the amount of tax benefits used. WEDC was also given authority to receive copies of returns and claims for the same purposes.
- Effective October 1, 2023.

Proposed Legislation

Income/Franchise Tax

Proposed Legislation

- Flat Income Tax - 2023 Senate Bill 1 and 2023 Assembly Bill 1
 - Propose 3.25% flat income tax rate achieved by reductions each year until flat rate imposed in 2026.
- Reduce Income Tax for Third Bracket - 2023 Senate Bill 435 and 2023 Assembly Bill 386
 - Propose reduction of income tax rate from 5.3% to 4.40% for third bracket.

Proposed Legislation (cont'd)

- Increase annual cap of Wisconsin Housing and Economic Development Authority Low-Income Housing Tax Credit Program - 2023 Senate Bill 40 and 2023 Assembly Bill 39
 - Increase annual amount of tax credits WHEDA certifies from \$42 million to \$100 million.
 - Adds requirement that at least 35% of credits are allocated to rural areas.

Proposed Legislation (cont'd)

- Farmland Preservation Agreements and Tax Credits - 2023 Senate Bill 134 and 2023 Assembly Bill 133
 - Proposed increases in farmland preservation tax credit to minimum \$10 per qualifying acre.
 - Adds new category of farmland that qualifies for the tax credit to the extent covered by an agricultural conservation easement.

Proposed Legislation (cont'd)

- Income/Franchise Exemption for Broadband Expansion Grants - 2023 Senate Bill 266 and 2023 Assembly Bill 272
 - Exempts income received from state or federal grant for broadband expansion in Wisconsin.
 - Prohibits claiming the exemption under the bill and the exemption under current law for the same grant.

Property Taxes

Recent Laws & Cases

Assessment / Valuation

Property Tax

Not All Vacant Stores Are Dark Stores

- *Lowe's Home Centers, LLC v. City of Delavan*, 2023 WI 8 (Feb. 16, 2023).
- 2016 and 2017 property tax assessments
 - Lowe's Home Improvement store = 134,574 sq. ft.
 - 14.525 acres
 - \$8,922,300
 - Taxpayer opinion = \$4.6 million

Not All Vacant Stores Are Dark Stores (cont'd)

- Presumption of correctness
 - Applies with the filing of the assessment along with the assessor's affidavit.
 - Taxpayer must provide significant contrary evidence
- Taxpayer valuation
 - Sales comparison approach
 - Three former American TV locations (two sold to Steinhafel's, one sold and converted to go-kart racing track)
 - Former K-Mart store

Not All Vacant Stores Are Dark Stores (cont'd)

- Former Lowe's store
- Former Target store
- City valuation
 - Sales comparison approach (different properties)
 - All properties occupied at time of sale
- Can a vacant property sale be a comparable sale? **YES**
 - "A vacant store is considered dark when it is vacant beyond the normal time period for that commercial real estate marketplace and can vary from one municipality to another." WPAM 9-12 (2016).

Not All Vacant Stores Are Dark Stores (cont'd)

- "Vacant" and "dark" are not synonymous
- All dark stores are vacant but not all vacant stores are dark (dark = subset of vacant).
- "Comparable" properties
 - "Comparable sales refer to properties that are similar to the subject property in age, condition, use, type of construction, location, design, physical features and economic characteristics." WPAM 7-24.
 - If property is occupied = demand for the use.
 - "A property in receivership is often sold under vastly different economic conditions and subject to vastly different incentives from a property that is not in receivership."

Not All Vacant Stores Are Dark Stores (cont'd)

- Exposure time
- Multi-tenant shopping centers (used by City)
 - Less than ideal
 - Adjustments made that were "reasonable, sufficient, and credible"
- Circuit court's factual findings, including credibility determinations:
 - Not clearly erroneous
 - Not "against the great weight and clear preponderance of the evidence."

Not All Vacant Stores Are Dark Stores (cont'd)

- Concurrence (3 justices)
 - Deference to circuit court
 - Should not be given on a circuit court's "general-comparability analysis deference"
 - "If the power to tax is the power to destroy, taxpayers must have access to meaningful appeal when challenging property tax assessments."
 - "If appellate courts defer to circuit courts' legal conclusions in property tax assessment cases, taxpayers will lose any avenue for meaningful appeal."

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met

- *Kerry Inc. v. Wisconsin Department of Revenue* (WTAC Nov. 21, 2022)
- Kerry Inc. = Dairy production business in Owen, Wisconsin.
 - 22.13 acres of land
 - 121,279 sq. ft. improvement - used as dried and liquid food ingredient processing plant.
 - Tax years 2017 and 2018
 - Assessed value = \$3,690,000 (2017) and \$3,735,000 (2018)
 - Kerry Inc.'s opinion of value = \$975,000

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Taxpayer:
 - "bears a heavy burden to show error in the assessments"
 - To overcome the presumption of correctness
 - "Should the taxpayer overcome that burden, the taxpayer continues to carry the burden of persuasion; that is, the taxpayer must show that its opinions of value are more credible than those asserted by the Department."

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Building residual method (used by Wisconsin Department of Revenue)
 - Comparable sales - value for land
 - Compares the residual, "the improvement sale price" to the subject property improvements
 - Although found to be inherently unreliable, use of the building residual method - by and of itself - not enough to overcome the presumption of correctness.
 - In a prior case, use of the building residual method combined with problematic comparable sales = sufficient to overcome the presumption of correctness.

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Wisconsin Department of Revenue methodology:
 - Did not take unique land/parcel factors in account
 - Numerous steps, "each one producing more opportunity for estimation error"
 - Relied on dated sales at trial (2011 sale for the 2017 and 2018 assessments)
 - None of the sales are food-processing plants
 - WDOR did not include even one of 5 possible sales of computer-generated list of candidates with higher correlations to the property
 - Location should not have been 100%

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Taxpayer methodology:
 - More direct - and potentially more reliable.
 - Most of sales were not comparable, had issues affecting the sales price, or both.
 - Occurred after assessment dates
 - Not food grade facilities
 - Vacant for at least six months prior to sale
 - Changed use after sale to non-food grade use
 - Below market rent

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Sales chart contained mathematical errors, which did result (or should have resulted) in material differences to opinion of value.
- Inconsistent adjustments, e.g., to site coverage
- Some sales not adjusted for larger size.
- None of the non-food-processing sales adjusted up for inferior cleanliness standards.
- "These types of errors were extremely damaging to the credibility of Petitioner's value."

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Wisconsin appraiser's license.
- Concerned about familiarity of taxpayer's appraiser with valuing manufacturing property - e.g., "the Wisconsin Property Assessment Manual . . . requires that comps should not be vacant."
- At trial, described property as below average.
 - In post-trial brief, agreed with the WDOR that the building is in fair condition.

Presumption of Correctness Overcome -> But Burden of Persuasion Not Met (cont'd)

- Wisconsin Tax Appeals Commission said it "suspect[ed] that the true fair market value of the Property lies somewhere between the Department's assessed value and the Petitioner's appraised value" - but no authority to split the difference.
- Although overcame presumption of correctness, taxpayer's valuation not more credible -> Did not meet burden of persuasion.

Fifth Amendment Takings Clause

- *Tyler v. Hennepin County, Minnesota*, 598 U.S. 631 (2023).
- Geraldine Tyler owned a condominium that Hennepin County seized and sold for \$40,000 to pay an accumulated \$2,300 in property taxes and \$13,000 in interest and penalties.
- The County kept the excess sale proceeds (of \$25,000) pursuant to Minnesota law. Tyler had no ability to recover the excess sale proceeds under Minnesota law.

Fifth Amendment Takings Clause (cont'd)

- Tyler filed a class action against the County. The District Court granted the County's motion to dismiss.
- On appeal, the Eighth Circuit held that "[w]here state law recognizes no property interest in surplus proceeds from a tax-foreclosure sale conducted after adequate notice to the owner, there is no unconstitutional taking." 26 F.4th 789, 793 (8th Cir. 2022).

Fifth Amendment Takings Clause (cont'd)

- In a unanimous opinion, the Supreme Court overruled the Eighth Circuit and District Court, determining that Tyler plausibly alleged that Hennepin County unconstitutionally retained the excess value of her home above her tax debt in violation of the Takings Clause.
- The County "could not use the toehold of the tax debt to confiscate more property than was due."

Exemption

Property Tax

"CIP" Equipment Does Not Qualify for Manufacturing Property Tax Exemption

- *Saputo Cheese USA, Inc. v. Wisconsin Department of Revenue*, No. 2022AP195 (Wis. Ct. App. May 24, 2023).
- Saputo manufactures and distributes cheese. After each batch of cheese is complete, Saputo uses clean-in-place ("CIP") equipment to rinse and clean cheese production vats. No raw materials used to produce cheese ever pass through the CIP equipment and the CIP equipment does not operate while the cheese is being manufactured.

"CIP" Equipment Does Not Qualify for Manufacturing Property Tax Exemption (cont'd)

- Saputo appealed a Circuit Court order that affirmed a Wisconsin Tax Appeals Commission ruling denying that the CIP equipment qualifies for tax exemption under Wis. Stat. § 70.11(27).
- Wis. Stat. § 70.11(27)(b) allows tax exemption for "[m]achinery and specific processing equipment . . . that are used exclusively and directly in the production process in manufacturing tangible personal property"

"CIP" Equipment Does Not Qualify for Manufacturing Property Tax Exemption (cont'd)

- Court of Appeals determined that the CIP equipment is neither "used directly" in production of cheese nor is it used in the "production process" as those terms are defined in the statute.
- The CIP equipment does not process any raw materials and it is not used until after the production process is complete.

"CIP" Equipment Does Not Qualify for Manufacturing Property Tax Exemption (cont'd)

- "To be exempt, the statute requires that the equipment be used before the finished product is conveyed to the first point of storage. Wis. Stat. § 70.11(27)(a)5. This means that the CIP equipment cannot be involved with the manufacturing process because, as Saputo has admitted, the cleaning cycle occurs only after the cheese has been manufactured and cleared from the production equipment." 2022AP195, ¶ 11.

Imposition

Personal Property Tax
Manufacturing
Special Assessments
TIF Districts
Transportation Utility Fees

Personal Property Tax

Personal Property Tax - Repealed

- 2023 Wis. Act 12, beginning with property tax assessments as of January 1, 2024, repeals Wisconsin's tax on tangible personal property.
- Wis. Stat. § 70.015: "Beginning with the property tax assessments as of January 1, 2024, no tax shall be levied under this chapter on personal property."
- Wis. Stat. § 70.02: Definition of "general property" removes reference to personal property.
- Wis. Stat. § 70.111(28): Exemption for business and manufacturing personal property.

Personal Property Tax - Repealed (cont'd)

- References to personal property taxes removed from definition of property taxes eligible for various types of credits effective for taxable years beginning after December 31, 2023:
 - Veterans and Surviving Spouse Property Tax Credit - Wis. Stat. § 71.07(6e)(a)5.
 - School Property Tax Credit - Wis. Stat. § 71.07(9)(a)3.
 - Homestead Credit - Wis. Stat. § 71.52(7).

Personal Property Tax - Repealed (cont'd)

- Classification Changes (Wis. Stat. § 70.17):
 - Manufactured and mobile homes (if not exempt)
 - Buildings, improvements, and fixtures on leased lands, exempt lands, forest croplands, and managed forest lands.
 - Leasehold improvements?

Personal Property Tax - Repealed (cont'd)

- 2023 taxes
 - Property tax bill in December 2023, payable by January 31, 2024.
- Omitted property
- Manufacturing real property returns

Manufacturing

Manufacturing

- Excluded from Wisconsin Department of Revenue assessment: ". . . property not contiguous with or located within 1,000 feet of the parcel on which the production process . . . occurs" Wis. Stat. § 70.995(5).
- New manufacturing classification request required?
 - Ownership or name - NO
 - **Location** - YES

Manufacturing (cont'd)

- Revocation - not retroactive. Wis. Stat. § 70.995(5n)(b).
- Personal property used in manufacturing - if manufacturing activity terminates, the Wisconsin Department of Revenue must be notified within 60 days. Wis. Stat. § 70.995(5n)(b).

Special Assessments

Special Assessment - Service of Appeal

- *Greenwald Family Limited Partnership v. Village of Mukwonago*, 2023 WI 53.
- Greenwald Family Limited Partnership ("Greenwald") owns properties in the village of Mukwonago.
- In 2019, the village created a special assessment district and levied special assessments against properties in the district, including one owned by Greenwald.

Special Assessment - Service of Appeal (cont'd)

- Greenwald filed an action in Circuit Court challenging the special assessment pursuant to Wis. Stat. § 66.0703.
- Greenwald served the summons and complaint on the Mukwonago **village attorney**.

Special Assessment - Service of Appeal(cont'd)

- Wis. Stat. § 66.0703(12)(a) "The person appealing shall **serve a written notice of appeal upon the clerk of the city, town or village** and execute a bond to the city, town or village in the sum of \$150 with 2 sureties or a bonding company to be approved by the city, town or village clerk, conditioned for the faithful prosecution of the appeal and the payment of all costs that may be adjudged against that person"

Special Assessment - Service of Appeal (cont'd)

- The Village moved to dismiss the complaint, arguing that the Circuit Court lacked subject matter jurisdiction or competency to proceed because Greenwald did not serve a written notice of appeal on the village clerk. The Circuit Court granted the motion and dismissed the action.
- Court of Appeals affirmed - the Circuit Court dismissal.

Special Assessment - Service of Appeal (cont'd)

- In a 4-3 opinion, the Wisconsin Supreme Court affirmed the Court of Appeals, finding the meaning of Wis. Stat. § 66.0703(12)(a) unambiguous.
- "The statute's plain meaning mandates service of written notice on the Village clerk, which Greenwald did not accomplish. Therefore, Greenwald's failure to comply with § 66.0703(12)(a) requires dismissal of the action." 2023 WI 53, ¶ 3.

Special Assessment - Service of Appeal (cont'd)

- Wis. Stat. § 801.14(2), which provides for service on the attorney of a party to the proceeding, did not apply in this case because the Village clerk was not a "party" to the action. 2023 WI 53, ¶ 47.

Special Assessment - Service of Appeal (cont'd)

- Dissent: Service was proper under several alternatives.
- The Village attorney was a proper party to receive service under Wis. Stat. § 801.14(2) and had either (i) held himself out as a person "apparently" able to receive process, under Wis. Stat. § 801.11(4)(b) or (ii) had consented to accept service in an email, representing consent on behalf of the Village of accept service in the manner it was received, under Wis. Stat. § 801.18(5)(d). 2023 WI 53, ¶ 50.

TIF Districts

Exceptions for Pleasant Prairie Tax Incremental District Removed

- 2023 Wis. Act 8 eliminates an exception to the Wisconsin Statutes governing the establishment and operation of tax incremental districts (TID).
- The exception related to TID Number 2 in the Village of Pleasant Prairie, which terminated in 2022. TID Number 2 was not subject to the generally applicable "12% limit" relating to creation of the TID, nor was it subject to the generally applicable limits on modification of TID boundaries.

Developer-Financed Tax Incremental Districts

- 2023 Assembly Bill 96 and 2023 Senate Bill 103 would allow cities, villages, and certain towns to create developer-financed tax incremental districts (TID), which are excepted from the general rule that the equalized value of taxable property of a TID plus the value increment of all existing TIDs in a city or village may not exceed 12% of the total equalized value of taxable property in the city or village and the requirement that all areas of a TID be contiguous.

Transportation Utility Fees

Transportation Utility Fees Subject to Municipal Levy Limits

- *Wisconsin Property Taxpayers, Inc. v. Town of Buchanan*, 2023 WI 58.
- Town of Buchanan needed money in excess of its current property tax levy limit to fund reconstruction of as much as 44% of its roads over the next 10 years.
- Town residents passed a referendum to raise funds through a transportation utility fee ("TUF").

Transportation Utility Fees Subject to Municipal Levy Limits (cont'd)

- Wis. Stat. § 66.0827 authorizes municipalities to establish utility districts to fund highways, sewers, and other public improvements in the district. The funding for a utility district must be provided through taxation of property in the district.

Transportation Utility Fees Subject to Municipal Levy Limits (cont'd)

- Under the Town's funding scheme, all residential properties pay the same TUF amount annually, but commercial properties must pay a variable fee based on the size and type of business and the number of estimated "trips" on municipal roads the business is expected to generate.
- Result was a net increase in municipal tax revenue of approximately 34% above the property tax levy limit.

Transportation Utility Fees Subject to Municipal Levy Limits (cont'd)

- Wisconsin Property Taxpayers, Inc. brought an action against the Town, alleging the TUF is a property tax subject to municipal levy limits under Wis. Stat. § 66.0602. The Circuit Court granted summary judgment in favor of the Town.
- Parties filed a joint petition for bypass of the Court of Appeals, which the Wisconsin Supreme Court granted.

Transportation Utility Fees Subject to Municipal Levy Limits (cont'd)

- In a unanimous opinion, the Wisconsin Supreme Court held the TUF is a property tax because the utility district is funded by taxation of property in the district.
- Because the Town referendum did not authorize an increase in the levy limit, the taxation of property funding the utility district had unlawfully exceeded the municipal property tax levy limits.

Transportation Utility Fees Subject to Municipal Levy Limits (cont'd)

- "In calculating estimated use of roads, the Town bases the TUF on the class of the property and its commercial characteristics, not the value of the property. Because Wis. Stat. § 66.0827 does not authorize 'taxation of property' to be based on anything other than property value, the TUF's assessment methodology is unlawful." 2023 WI 58, ¶ 18.

Unclaimed Property

Recent Cases

Unclaimed Property - *MoneyGram* Case

- *Delaware v. Pennsylvania et al.*, 598 U.S. 115 (2023).
- "Official checks" issued by MoneyGram
 - Retail Money Orders
 - Agent Check Money Orders
 - **Agent Checks**
 - **Teller's Checks** (last two, collectively "Disputed Instruments")

Unclaimed Property - *MoneyGram* Case

- Purchaser pays face value of the check to the selling bank plus fees. Bank sends the funds to MoneyGram. Purchaser gives the check to the payee, who can cash the check at a bank, which will then be reimbursed by MoneyGram.
- "Third party bank checks"?
 - Common law applies
 - Escheat to state where company is incorporated.
 - MoneyGram = incorporated in Delaware.

Unclaimed Property - *MoneyGram* Case (cont'd)

- Or "money order, traveler's check, or other **similar** written instrument (other than a third party bank check) on which a banking or financial organization or a business association is directly liable"?
 - If so, the Disposition of Abandoned Money Orders and Traveler's Checks Act - or Federal Disposition Act ("FDA") - applies.
 - Primary escheatment rule = place-of-purchase rule

Unclaimed Property - *MoneyGram* Case (cont'd)

- Special Master appointed
 - First Interim Report - Found Disputed Instruments covered by the FDA
 - Briefs and oral argument
 - Second Interim Report - Concluded many of the Disputed Instruments were or could be "third party bank checks"

Unclaimed Property - *MoneyGram* Case (cont'd)

- U.S. Supreme Court:
 - Disputed Instruments = Prepayment of a specified amount of money to be transmitted to a named payee
 - Similar to money orders
 - Because MoneyGram does not keep records of creditor addresses as a matter of business practice, would otherwise escheat inequitably under common law

Unclaimed Property - *MoneyGram* Case (cont'd)

- No definition for "third party bank check"
 - Special Master "valiantly attempted to bring clarity to this term, adopting three different definitions of 'third party bank check' over the course of this litigation."
 - "Ultimately, between the parties and the Special Master, we have been offered at least six disparate definitions of the term."

Unclaimed Property - *MoneyGram* Case (cont'd)

- Delaware - "'third party bank check' means a check signed by a bank officer and paid through a third party. Not surprisingly, that definition fits the Disputed Instruments like a glove, given that they are signed by bank employees and then ultimately paid through MoneyGram, a nonbank third party when presented."
- No support whatsoever.
- Own expert disagreed.

Excise Taxes

Cigarette Tax

Increase in Cigarette Tax Stamp Discount

- 2023 Wis. Act 19 amends Wis. Stat. § 139.32(5).
- The discount on cigarette tax stamps purchased by cigarette manufacturers, bonded direct marketers, and distributors is increased from 0.8% to 1.25%.
- Effective for cigarette tax stamps purchased on or after October 1, 2023.

Miscellaneous

Streaming Companies - Not Subject to Tax Under Illinois' Cable and Video Competition Law

- East St. Louis filed lawsuit against video streaming services.
 - Claimed owed fees, up to 5% of gross revenue.
- Court dismissed the action
 - Found only the Illinois attorney general had enforcement authority under the Cable and Video Competition Law of 2007 (requires video and cable service providers to register with the state).
 - East St. Louis also argued claims of trespassing, unjust enrichment and ordinance violations.

Streaming Companies - Not Subject to Tax Under Illinois' Cable and Video Competition Law

- Seventh Circuit affirmed (October 13, 2023).
 - Not "cable service or video service."
 - No "use" of the public way for communication; no trespass.
 - No "resale" of "cable television service."

No More Free Cheese

- 2023 Wis. Act 7 repealed Wis. Stat. § 41.11(5) "Cheese Distribution".
- The Department of Tourism is no longer required to distribute free cheese to the public at tourist information centers from May to September.
 - Department of Tourism no longer operates tourist information centers (based on statutory change in 2009).

Questions?

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Thank You!

This presentation provides information of a general nature. None of the information contained herein is intended as legal advice or opinion relative to specific matters, facts, situations or issues. Additional facts and information or future developments may affect the subjects addressed in this presentation. You should consult with a lawyer about your particular circumstances before acting on any of this information because it may not be applicable to you or your situation.

9:40 – 10:40 a.m.

Wisconsin Department of Revenue Update

Nate Weber, CPA, *Director, Office of Technical Services Division
of Income, Sales & Excise Tax, Wisconsin Department of Revenue*



Wisconsin Tax Update

WI Dept of Revenue | Division of Income, Sales & Excise Tax
Fall 2023

Updated 10-20-2023



Mission

Strengthen Wisconsin through fair tax and lottery administration, while educating and serving the public, our customers and communities.

Vision

To be the premier agency in providing innovative, accessible resources, and exceptional customer service built on a foundation of trust, inclusivity and creativity.

Values

- Integrity
- Innovation
- Inclusivity
- Knowledge
- Empathy
- Security



Topics

- ▷ Income/Franchise Tax Update
- ▷ Sales/Use Tax Update
- ▷ Unclaimed Property Update
- ▷ Personal Property Tax
- ▷ Other Updates
- ▷ My Tax Account (MTA) Updates
- ▷ Statistics
- ▷ Contact Us



Internal Revenue Code Update



Internal Revenue Code (IRC) Update

Tax Year 2023

- ▷ Wisconsin follows the IRC as of December 31, 2020, with certain exceptions
- ▷ Wisconsin computes depreciation and amortization using IRC in effect on January 1, 2014, with certain exceptions
- ▷ Wisconsin has not adopted federal bonus depreciation provisions
- ▷ Wisconsin follows changes to IRC section 179 expensing



5

IRC Update

Federal laws that have passed since December 31, 2020:

- Public Law 117-2 – American Rescue Plan Act of 2021
- Public Law 117-6 – PPP Extension Act of 2021
- Public Law 117-44 – Surface Transportation Extension Act of 2021
- Public Law 117-52 – Further Surface Transportation Extension Act of 2021
- Public Law 117-58 – Infrastructure Investment and Jobs Act
- Public Law 117-103 – Consolidated Appropriations Act, 2022
- Public Law 117-167 – Supreme Court Security Funding Act of 2022
- Public Law 117-169 – Inflation Reduction Act of 2022
- Public Law 117-263 – James M. Inhofe National Defense Authorization Act – 2023
- Public Law 117-286 – HR 5961
- Public Law 117-328 – Consolidated Appropriations Act, 2023



6

IRC Update – Potentially Adopted

WI Senate Bill 389 and Assembly Bill 406

- ▷ Updates Wisconsin's definition of Internal Revenue Code to December 31, 2022
- ▷ Adopts most federal IRC provisions, with exceptions
- ▷ Does not adopt depreciation changes – WI follows IRC as of 1/1/14



7

IRC Update – Potentially Adopted

▷ Public Law 117-2 (American Rescue Plan Act)

- **IRC 32: Earned income credit** – Allows married filing separate individual who lives apart from spouse the last 6 months of the year or has a divorce or separation instrument by the end of the tax year to claim EIC
- **IRC 32: Earned income credit** – Raises investment income limit to \$11,000
- **IRC 864: Election to allocate interest on a worldwide basis** – Repeals retroactively to 2021 taxable year
- **Numerous retirement provisions** - Automatically apply for Wisconsin under secs. 71.01(7n), 71.22(5m)(a), 71.34(1m)(a), and 71.42(2m), Wis. Stats.



8

IRC Update – Potentially Adopted

▷ Public Law 117-58 (Infrastructure Investment and Jobs Act)

- **IRC 7508A: Extensions** – retroactive to taxable years after December 31, 2020
 - Treats multiple declarations of federally declared disasters as a separate incident period allowing for a 60-day extension for each incident period. Previously, if a subsequent federally declared disaster occurred during a current disaster period, the extension would extend 60 days beyond the first day of the incident period for the subsequent disaster.
 - Adds "significant fires" to the list of reasons certain deadlines may be extended.
- **IRC 118: Contributions to the capital of a corporation** - Certain contributions received by a regulated public utility are excluded from gross income of a corporation.



IRC Update – Potentially Adopted

▷ Public Law 117-58 (Infrastructure Investment and Jobs Act)

- **IRC 142 & 146: Exempt facility bonds** – Added qualified broadband projects and carbon dioxide capture facilities to the list of federally exempt interest (Note: interest not included in federal adjusted gross income is added back to Wisconsin income – sec. 71.05(6)(a), Wis. Stats.)



IRC Update – Potentially Adopted

▷ Public Law 117-169 (Inflation Reduction Act of 2022)

- **IRC 40A, 6426, & 6427: Sustainable aviation fuel credit** – Amount of credit is included in gross income
- **IRC 179D & 312: Energy efficient commercial buildings deduction & effects on earnings and profits** – Expanded eligibility. Efficiency requirements updated. Deduction decreased. For purposes of determining E&P for real estate investment trust corporations, the deduction is allowed in the year placed in service as opposed to over a period of five taxable years.
- **IRC 6418, 50, 39: Transfers of certain credits** - Certain taxpayers (not tax-exempt entities) are allowed a one-time transfer of certain tax credits. Any payments received in exchange for the transfer of credits are excluded from income, and any amounts paid to obtain a transferred credit cannot be deducted from income.



11

IRC Update – Potentially Adopted

▷ Public Law 117-328 (Consolidated Appropriations Act 2023)

- **IRC 45E: Small employer pension plan startup costs-**
 - Federal** - If the employer claims the credit under sec. 45E(a) or 45E(f), IRC, they may not deduct the startup costs used to compute those credits
 - Wisconsin** – Employer may make a different election and deduct the startup costs
- **Sections 529 & 408: Qualified tuition programs & individual retirement accounts** - Certain distributions from a qualified tuition program that have been maintained for a 15-year period are excluded from gross income of the distributee. The distributions may be transferred to a Roth IRA and treated as a "qualified rollover contribution".
- **Section 529A: Qualified ABLÉ programs** – Changes the age requirement from 26 to 46



12

IRC Update – Potentially Adopted

▷ Public Law 117-328 (Consolidated Appropriations Act 2023)

- **Section 1042: Sales of stock to employee stock ownership plans or certain cooperatives** – Allows the deferral of tax for certain sales of employer stock to employee stock ownership plan sponsored by S corporation
- **Sections 170 & 6662-6664: Charitable contributions and gifts, accuracy and fraud penalties** – Qualified conservation contributions by a pass-through entity are not treated as qualified conservation contributions if the amount of contribution exceeds 2.5 times the sum of each owner's basis in the pass-through entity.



13

IRC Update – Potentially Adopted

▷ IRC 1202: Small business stock gain exclusion

- Continuous conformity to IRC 1202
- Retroactive adoption to taxable years beginning after December 31, 2018 (amended WI returns allowed if passed)
- Federal exclusion is 100% for stock acquired after 9/27/2010
- WI exclusion (if not passed) is 50% for stock acquired after 12/31/13



14

IRC Update – Potentially Adopted

- ▷ **WI Senate Bill and Assembly Bill 364**
 - **IRC 223: Health savings accounts** - Extends health savings account safe harbor for the absence of telehealth deductible for plan years before January 1, 2025
 - Continuous conformity and retroactive to taxable year 2022



15

IRC Update – Not Adopted

- ▷ **IRC 461: Excess business loss limitation**
 - Excess loss limitation extended through December 31, 2026 (Public Law 117-2)
 - Excess loss limitation extended through December 31, 2028 (Public Law 117-169)
 - Wisconsin has not adopted federal excess business loss limitation
- ▷ **IRC 108: Student loan forgiveness**
 - IRC 108(f)(5) - most student loans discharged after December 31, 2020, and before January 1, 2026, are not included in federal gross income (Public Law 117-2)
 - Wisconsin follows the old sec. 108(f)(5), IRC (as of 12/31/20), which excludes student loan discharges on account of death or total and permanent disability
 - Wisconsin allows exclusion under sec. 108(f)(1) for individuals who work for a certain period of time in certain professions (e.g., Public Service Loan Forgiveness program)



16

IRC Update – Not Adopted

▷ IRC 162(m): Excessive employee remuneration

- **Federal** - A publicly-held corporation may not deduct more than \$1,000,000 of compensation paid to any covered employee for the performance of services. The law expands the definition of "covered employee" to CEO, CFO, and the next 5 highest paid employees for purposes of limiting publicly held corporations from deducting certain excessive employee remuneration. Excludes commission and performance-based pay.
- **Wisconsin** - The changes to the definition of "covered employee" by Public Laws 115-97 and 117-2 do not apply for Wisconsin



17

Wisconsin Income/Franchise Tax Law Changes



18

Tax Rate Reduction

2023 Wis. Act 19

- ▷ Effective for tax year 2023 and thereafter
- ▷ Affects individual taxpayers and fiduciaries
- ▷ Tax rate for first income bracket reduced from 3.54% to 3.5%
- ▷ Tax rate for second income bracket reduced from 4.65% to 4.4%
- ▷ See [Wisconsin Tax Bulletin 222](#), page 3 for details on the income ranges for these brackets



19

Capital Loss Deduction

2021 Wisconsin Act 157

- ▷ Capital loss deduction increased from \$500/year to \$3,000/year (\$1,500 for married persons filing a separate return)
- ▷ Applies to individuals, and partnerships and tax-option (S) corporations making the entity-level tax election
- ▷ Effective for taxable years beginning **after December 31, 2022**



20

Commercial Loan exemption

2023 Wis. Act 19

- ▷ Created 71.05(1)(i) and 71.26(1)(i), Wis. Stats.
- ▷ Effective for taxable years beginning January 1, 2023
- ▷ Income from a corporation or a tax option (S) corporation that is a financial institution, including interest, fees, and penalties, derived from a commercial loan is exempt from Wisconsin corporate and individual income tax.
- ▷ The loan must be for five million dollars or less
- ▷ The loan must be provided to a person residing or located in Wisconsin and used primarily for a business or agricultural purpose.



21

Interstate Broker Dealers Apportionment

2023 Wisconsin Act 19

- ▷ A brokerage house, investment adviser, investment company, or underwriter that is engaged in business both in and outside this state must apportion its apportionable income according to sec. Tax 2.495, Wis. Adm. Code.
- ▷ The Act revises sec. Tax 2.495(4), Wis. Adm. Code, to provide that in certain instances DOR cannot order or permit the substitution of net gains for gross receipts in the receipts factor if the use of gross receipts results in substantial distortion of the taxpayer's receipts factor.



22

Interstate Broker Dealers Apportionment

Specifically, DOR cannot substitute net gains for sales of trading assets if:

- ▷ The taxpayer, before January 1, 2023, elected to source its sales of trading assets using the customer billing address method; and
- ▷ The taxpayer has not revoked that election; and
- ▷ The taxpayer, for any taxable year beginning after December 31, 2021, determines its receipts factor under sec. Tax 2.495(4), Wis. Adm. Code, by using the average of the receipts factor determined by using (a) gross receipts, net of commissions, and (b) net gain, net of commissions, from sales of trading assets for the taxable year, with all other components of the receipts factor remaining the same.



23

Refundable Research Credit Increase

2023 Wisconsin Act 19

- ▷ Up to 15% of the research credit computed/claimed on eligible expenses for the taxable year may be refunded, if not used to offset tax due for that taxable year (starting in taxable years beginning after December 31, 2020)
- ▷ The Act increases the refundable portion from 15% to 25% effective for taxable years beginning on or after January 1, 2024



24

Manufacturing and Agriculture Credit

2023 Wis. Act 12

- ▷ Repeals personal property taxes in Wisconsin starting with assessment year 2024 and makes changes to the manufacturing and agriculture credit
- ▷ Qualified Production Property
 - Persons must sell qualified production property to be eligible
 - Qualified production property includes tangible personal property manufactured in whole or in part by the claimant on property that is located in this state and assessed as manufacturing property under sec. 70.995, Wis. Stats. [Real property]
 - The Act expands the definition of "qualified production property" to include tangible personal property manufactured in whole or in part by the claimant with an establishment that is located in this state and **classified** as manufacturing under sec. 70.995(5n), Wis. Stats. [Important for those who don't have real property assessed as manufacturing property]



25

Manufacturing and Agriculture Credit

- ▷ Classifying Personal Property as Manufacturing Property
 - An application must be filed with DOR no later than July 1 of the taxable year.
 - DOR must make a determination and provide notice by December 31 of the year in which the application is filed.
 - An establishment classified as manufacturing prior to January 1, 2024, is presumed to be engaged in manufacturing and does not need to submit an application.



26

Manufacturing and Agriculture Credit

- ▷ Manufacturing Property Factor
 - The Act amended the definition of "manufacturing property factor"
 - Real and personal property assessed under sec. 70.995, Wis. Stats., was replaced with the term "land and depreciable property" for the numerator and denominator.
- ▷ If all qualified production activities income results from sale of tangible personal property that was manufactured, produced, grown, or extracted entirely in Wisconsin, it is not necessary to multiply the qualified production activities income by the property factor.



27

Pass-Through Entity Representative



28

Pass-Through Entity Representative

- ▷ Under sec. 71.80(26)(a), Wis. Stats., each pass-through entity (PTE) must designate a pass-through member or other person with substantial presence in the United States as the pass-through entity representative (PTR).
- ▷ PTR may be different than federal representative.
- ▷ If PTE did not designate a PTR, the department will send a written request for a PTR.
- ▷ If PTE does not designate a PTR within 60 days of the department's request, the department may designate a PTR and notify, in writing, the PTE.
 - PTE may at any time provide a written statement to the department designating a new PTR.



29

Pass-Through Entity Representative

- ▷ Form 2 (fiduciary, estates, trusts), Form 3 (partnerships), and Form 5S (tax-option (S) corporations) have a section for the PTE to designate a PTR.
- ▷ PTE may also designate a PTR by submitting a Form PT-R, *Pass-Through Entity Representative*, or a separate statement, that includes all the information requested on Form PT-R, signed by an authorized agent of the PTE.
- ▷ **The department will treat the most recently appointed PTR as the sole active PTR under sec. 71.80(26), Wis. Stats.**



30

Pass-Through Entity Representative

- ▶ PTR powers and duties vs. POA authority for audit determinations at the entity level under sec. 71.745, Wis. Stats.

Authority for Pass-Through Entity Audit Determination	Power of Attorney	Pass-through Entity Representative
Enter into an agreement to extend the limitation period to make an audit determination	No	Yes
Enter into settlement agreements and bind pass-through members to adjustments in audit determination	No	Yes
File an appeal of the audit determination	No	Yes
Elect to reduce an audit assessment under sec. 71.745(8), Wis. Stats.	No	Yes
Elect to have an audit assessment assessed to the pass-through members under sec. 71.745(9), Wis. Stats.	No	Yes



Pass-Through Entity Representative

- ▶ Form PT-R or a written statement designating a PTR are sent to:
 - DORAuditPassThrough@wisconsin.gov, or
 - MS 6-81
Wisconsin Department of Revenue
Pass-Through Audit Unit
PO Box 8906
Madison, WI 53708-8906



Entity-Level Tax Election



33

Entity-Level Tax Elections

- ▷ 2017 Wisconsin Act 368 created an election for partnerships and tax-option (S) corporations to pay tax at the entity level on behalf of their pass-through members.
- ▷ **Reminder:** The election or subsequent revocation of the election under sec. 71.21(6)(a) or 71.365(4m)(a), Wis. Stats., **must** be made by the extended due date of the entity's income or franchise tax return.
 - Calendar year partnership extended due date: 9/15
 - Calendar year tax-option (S) corporation extended due date: 10/15



34

Pass-Through ELT Election Overview

2021 Tax Year (Statistics as of July 15, 2023)	
Tax-Option (S) Corporations (Form 5S) Filing Stats	
Tax-Option (S) Corporation returns filed	86,789
Tax-Option (S) Corporation entity-level tax elections filed	6,048
Percent of entity-level tax elections filed	6.97%
Partnership (Form 3) Filing Stats	
Partnership returns filed	85,382
Partnership entity-level tax elections filed	3,009
Percent of entity-level tax elections filed	3.52%
Pass-Through Entity Filing Stats - TOTAL	
Pass-Through entity returns filed	172,171
Entity-level tax elections filed	9,057
Percent of entity-level tax elections filed	5.26%



35

Claiming the Other State Tax Credit with the Pass-Through ELT Election

▷ **Five scenarios to consider when claiming the Wisconsin other state tax credit:**

1. ELT election made in Wisconsin only
2. ELT election made in other state only (non-refundable credit for members)
3. ELT election made in other state only (refundable credit for members)
4. ELT election made in other state only (income excludable for members)
5. ELT election made in Wisconsin and in other state



36

Claiming the Other State Tax Credit with the Pass-Through ELT Election

▷ ELT election made in Wisconsin only

- Only the pass-through entity may claim the credit (sec. 71.07(7)(b)2., Wis. Stats.)
- Entity's credit is based on net income or franchise tax **paid by the entity** to another state on that income and the net income tax on that income **paid by the entity** on behalf of its shareholders, partners, and members that are residents of this state on a composite return filed with the other state against the net income or franchise tax otherwise payable to this state on income of the same year (sec. 71.07(7)(b)3., Wis. Stats.)
- Use Schedule ET-OS, *Credit for Net Tax Paid to Another State*, to claim the credit



37

Claiming the Other State Tax Credit with the Pass-Through ELT Election

▷ ELT election made in other state only (**non-refundable** credit for members)

- In general, the individual Wisconsin members of the pass-through entity may claim the credit for the period they were a Wisconsin resident during the tax year (sec. 71.07(7)(b)2., Wis. Stats.)
- Member's credit is based on the member's allocable share of net income or franchise tax paid by the entity on their behalf
- Individuals use Schedule OS, *Credit for Net Tax Paid to Another State*, Parts III and IV to claim the credit



38

Claiming the Other State Tax Credit with the Pass-Through ELT Election

▷ ELT election made in other state only (**refundable** credit to members)

- In general, the individual Wisconsin members of the pass-through entity may claim the credit for the period they were a Wisconsin resident during the tax year (sec. 71.07(7)(b)2., Wis. Stats.)
- Member's credit is based on the member's net income tax paid to the other state on their individual income tax return filed in the other state (sec. Tax 2.955(2)(a), Wis. Adm. Code)
- Individuals use Schedule OS, *Credit for Net Tax Paid to Another State*, Parts I, II, and IV to claim the credit. Do not reduce the net tax on line 22 of Schedule OS by the individual's credit claimed in the other state for tax paid by the entity in the other state.



39

Claiming the Other State Tax Credit with the Pass-Through ELT Election

▷ ELT election made in other state only (**income excludable** for members)

- In general, the individual Wisconsin members of the pass-through entity may claim the credit for the period they were a Wisconsin resident during the tax year (sec. 71.07(7)(b)2., Wis. Stats.)
- Member's credit is based on the member's allocable share of tax paid by the entity on their behalf
- Individuals use Schedule OS, *Credit for Net Tax Paid to Another State*, Parts III and IV to claim the credit



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Claiming the Other State Tax Credit with the Pass-Through ELT Election

▷ ELT election made in Wisconsin and in other state

- Only the pass-through entity may claim the credit (sec. 71.07(7)(b)2., Wis. Stats.)
- Entity's credit based on net income or franchise tax **paid by the entity** to another state on that income and the net income tax on that income **paid by the entity** on behalf of its shareholders, partners, and members that are residents of this state on a composite return filed with the other state against the net income or franchise tax otherwise payable to this state on income of the same year (sec. 71.07(7)(b)3., Wis. Stats.)
- Use Schedule ET-OS, *Credit for Net Tax Paid to Another State*, to claim the credit



Commonly Used Corporate Franchise/Income Tax Credits, Tax Year 2020
(Statistics as of May 4, 2023)

Corporate Tax Credit	Number of Claimants Using Credit	Amount of Credit Used	Credit Available	Credit Carried Forward
Manufacturing credit	464	\$123,242,508	\$248,226,532	\$124,984,024
Enterprise zone jobs credit	13	\$48,716,467	Refundable	
State historic rehabilitation credit	21	\$46,112,263	\$53,832,385	\$7,720,122
Nonrefundable research expense credit	454	\$44,666,993	\$608,708,136	\$564,041,143
Refundable research expense credit	549	\$10,134,603	Refundable	
Business development credit	33	\$8,800,945	Refundable	
Research facility credit	6	\$3,558,980	\$9,484,552	\$5,925,572
Economic development credit	12	\$2,142,679	\$22,638,793	\$20,496,114



Commonly Used Individual Franchise/Income Tax Credits, Tax Year 2021
(Statistics as of February 16, 2023)

Individual Income Tax Credits	Number of Claimants Using Credit	Amount of Credit Used	Credit Available	Credit Carried Forward
Taxes paid to other states credit	81,789	\$459,295,412	\$474,843,648	No carryforward
School property tax credit	1,798,031	\$443,664,380	\$511,925,346	No carryforward
Itemized deduction credit	618,669	\$305,496,454	\$601,769,830	No carryforward
Manufacturing credit	6,036	\$306,135,683	\$573,336,660	\$267,200,977
Married couple credit	618,952	\$258,920,052	\$262,919,821	No carryforward
Earned income credit	198,816	\$76,532,468	Refundable	
Homestead credit	102,516	\$50,027,234	Refundable	
Veterans and surviving spouses property tax credit	12,935	\$43,528,470	Refundable	
Nonrefundable research expense credit	3,761	\$25,283,059	\$66,286,464	\$41,003,405
Agriculture credit	5,283	\$19,794,022	\$81,694,582	\$61,900,560



Income/Franchise Tax Litigation



Litigation – Early Withdrawal Penalty

Scott Cech v. Wisconsin Department of Revenue: Wisconsin Tax Appeals Commission, June 5, 2023

- ▷ Issue: Applicability of the first-time homebuyer exception to the penalty on an early withdrawal from a 401(k) retirement account
- ▷ Taxpayer made an early withdrawal from their 401(k) retirement account and used most of the funds to purchase their first home. The gross distribution was included in taxable income on their return, but no penalty for an early withdrawal was reported.
- ▷ Sec. 72(t)(2)(F), IRC, allows an exception to the penalty for distributions, up to \$10,000, from an "individual retirement plan" that are used to purchase a first home. Per the IRS website: [Retirement Topics – Exceptions to Tax on Early Distributions](#)
- ▷ The Commission decided the taxpayer did not meet the first-time homebuyer's exception to the early withdrawal penalty. Taxpayer did not appeal.



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Litigation – Business Purpose

Skechers USA, Inc. v. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, February 24, 2023).

- ▷ Audit period 2000-2003
- ▷ Taxpayer deducted expenses for intercompany transactions relating to licensing intellectual property and management services
- ▷ DOR disallowed expenses under the authority in sec. 71.30(2), Wis. Stats., in order to clearly reflect the income of the taxpayer and to prevent evasion of taxes
- ▷ Commission concluded the transactions did not have economic substance or a valid business purpose other than tax avoidance
- ▷ Taxpayer appealed to the Circuit Court.
- ▷ See [Wisconsin Tax Bulletin 221](#), page 10 (April 2023)



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Litigation: Manufacturing Credit

General Mills, Inc. v. Wisconsin Department of Revenue: Wisconsin Tax Appeals Commission, October 26, 2022

- ▷ Taxpayer has a manufacturing facility located in Milwaukee, Wisconsin.
- ▷ Taxpayer filed a timely Wisconsin corporation income tax return for the 2013 tax year.
- ▷ The manufacturing credit was not claimed on the original 2013 return.
- ▷ A subsequent field audit issued a Notice of Proposed Audit Report (NOPAR) that found numerous adjustments, but the manufacturing credit was neither adjusted nor the subject of a prior assessment.
- ▷ Taxpayer signed NOPAR agreeing in full and sent a check for the full amount.



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Litigation: Manufacturing Credit

- ▷ The department then sent a Notice of Field Audit Action
- ▷ Taxpayer then sent an amended return for the 2013 tax year claiming a manufacturing credit of \$811,220 and requesting a refund.
- ▷ The department denied the claim for refund under sec. 71.75(4), Wis. Stats., which provides that a taxpayer may not file a claim for refund for any tax year covered by a finalized field audit.
- ▷ The Commission agreed with the refund denial, but asserted the proper statute that bars the refund is sec. 71.75(5), Wis. Stats., which bars a claim for refund in respect to items not adjusted in the notice of assessment or refund.
- ▷ Taxpayer did not appeal decision



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Litigation: Pass-Through Withholding

RADS Partnership, Via Cresta, L.P., Laughing Cow, LP, Finger Living Trust, and Westmar LTD (Petitioners) v. Wisconsin Department of Revenue: Wisconsin Tax Appeals Commission, July 25, 2022

- ▷ All Petitioners are pass-through entities, except Finger Living Trust
- ▷ Petitioners did not file withholding returns in 2013
- ▷ Petitioners claimed they did not have to file withholding returns because they had losses from prior years
- ▷ Petitioners did not timely file returns for years in which losses were incurred



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Litigation: Pass-Through Withholding

- ▷ Commission concluded:
 - Pass-through entities are required to file a timely pass-through withholding form in each year where there is "Wisconsin income" (i.e., not allowed to use prior years' losses)
 - Adding the word "taxable" to "income" under sec. 71.775(2)(a) and (3)(a)2., Wis. Stats., changes the meaning of the statute
 - Pass-through entities must use WI Form PW-1 as the pass-through withholding form



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Litigation: Pass-Through Withholding

- ▷ Petitioners appealed to the Dane County Circuit Court on February 20, 2023.
- ▷ The Dane County Circuit Court dismissed the appeal because the department was not properly served, and the Circuit Court therefore lacks jurisdiction.
- ▷ Petitioners appealed to the Wisconsin Court of Appeals.



Other Income/Franchise Tax Updates & Reminders



Other Updates and Reminders

- ▷ College savings account subtraction
 - Increases to \$3,860 (\$1,930 if married filing separately) per beneficiary
 - 2022 amount was \$3,560
- ▷ Wisconsin tuition and fees subtraction
 - Subtraction – decreased from \$6,976 to \$6,974
 - Includes fees for course related books if paid to institution as condition of enrollment or attendance
 - Phase-out
 - Single or head of household - \$65,370 to \$78,440
 - Married filing joint - \$104,590 to \$130,730
 - Married filing separate - \$52,300 to \$65,370



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Other Updates and Reminders

- ▷ Mileage rates - 2023
 - 65.5 cents per mile for business miles (28 cents per mile is treated as depreciation)
 - 22 cents per mile for medical or moving purposes
 - 14 cents per mile in service of charitable organizations



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Student Loan Forgiveness & SAVE Plan

- ▷ On June 30, 2023, U.S. Supreme Court blocked one-time student debt relief plan put forth by the Biden-Harris Administration
- ▷ The Biden-Harris Administration created the SAVE plan to replace the existing REPAYE plan
 - This is an income-based repayment (IBR) plan
 - Ability for debt under the SAVE plan to be forgiven is the same as any other IBR
- ▷ Wisconsin excludes student loan forgiveness from income under sec. 108 of the IRC as it existed on December 31, 2020
 - Extent insolvent (108(a)(1)(B)) - report on federal Form 982 marked "For Wisconsin Purposes"
 - Public service loan forgiveness (108(f)(1) and (4))
 - Death or total and permanent disability of the student (108(f)(5))
- ▷ Canceled student debt that is excluded for federal purposes but taxable to Wisconsin should be added to federal adjusted gross income on line 1g of Wisconsin Schedule I



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Manufacturing and Agriculture Credit

- ▷ Credit from prior taxable year
 - Credit reported as income in the current taxable year is not included in the numerator of the production gross receipts factor
 - The numerator is production gross receipts of the manufacturer claiming the credit
 - Production gross receipts are receipts from the lease, rental, license, sale, exchange or other disposition of qualified production property.
 - Qualified production property is the tangible personal property manufactured by the claimant.
 - Therefore, prior years credit is not a production gross receipt. However, the prior year credit is included in the denominator because all sources of gross income are included in the denominator
 - See [WTB 220](#), page 10



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Pass-Through Entities: Requirement to file Schedules 2K-1, 3K-1, and 5K-1

- ▷ A pass-through entity is required to do the following by the due date, including extensions, of its income/franchise tax return:
 - Provide a schedule to each owner (partner, shareholder, beneficiary, or member) whose share of income and other items from the entity affect the owner's WI tax liability. The schedule shall separately indicate the owner's share of each item from the entity.
 - Include a copy of the schedule with the entity's WI income/franchise tax return.
- ▷ Trusts and estates use Schedule 2K-1, partnerships use Schedule 3K-1, and tax-option (S) corporations use Schedule 5K-1
- ▷ Failure to file the schedule by the due date may result in a \$50 penalty for each violation (sec. 71.83(1)(a)10., Wis. Stats.).



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Qualified Wisconsin Business (QWIB) – Income Exclusion / Deferral

- ▷ **Capital Gain Exclusion / Deferral**
 - Long-term capital gain from investments made after December 31, 2010, in a qualified Wisconsin business and held for at least five uninterrupted years are excluded from Wisconsin income
 - Exclusion does not apply to any portion of gain due to amount of gain deferred at time of investment
 - See Schedule QI, *Sale of Investment in a Qualified Wisconsin Business*



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Qualified Wisconsin Business (QWIB) Registration

- ▷ A business may register as a QWIB if, in the business's tax year ending immediately before the date of registration:
 - The business has at least 2 full-time employees,
 - The amount of payroll compensation paid by the business in WI is at least 50% of all payroll compensation paid by the business, and
 - The value of real and tangible personal property owned or rented and used by the business in WI is at least 50% of the value of all real and tangible personal property owned or rented and used by the business.
- ▷ Business must register **each year** it desires to be a QWIB (sec. 73.03(69), Wis. Stats.)
 - **Registration for 2023 must be completed by January 2, 2024.**



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QWIB Registration

- ▷ Registration for 2023 must be completed by January 2, 2024.
- ▷ To register your business with the department, use the department's online application here:
 - https://tap.revenue.wi.gov/QualBus/_/
- ▷ A list of QWIBs can be found on the department's website here:
 - <https://www.revenue.wi.gov/Pages/Report/qualified-businesses.aspx>



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Qualified Opportunity Fund (QOF)

- ▷ Certain taxpayers who invest in a QOF may qualify for federal tax benefits:
 - Defer paying tax on capital gains by investing the gains in a QOF
 - Reduce the taxable amount of the deferred capital gains by
 - 10% if QOF investment is made prior to Jan. 1, 2022, and is held for at least 5 years
 - 15% if QOF investment is made prior to Jan. 1, 2020, and is held for at least 7 years
 - Exclude all gains from the sale of a QOF investment by holding the QOF investment for at least 10 years.
- ▷ See sections 1400Z-1 and 1400Z-2 of the Internal Revenue Code (IRC)
- ▷ WI follows the federal tax benefits



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WI Qualified Opportunity Fund (WQOF)

- ▷ A WQOF means a QOF that holds at least 90% of its assets in WI qualified opportunity zone property
- ▷ For taxable years beginning on or after January 1, 2020, a WQOF is required to file WI Form WQOF with the department and provide a copy to each investor by January 31 of the year following the close of the WQOF's taxable year.
- ▷ In addition to the federal QOF tax benefits, certain taxpayers who defer paying tax on their capital gains by investing in a WQOF may qualify for a WI subtraction or basis modification



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WQOF

- ▷ The WI subtraction or basis modification is
 - 10% of the deferred capital gain if
 - The WQOF investment was held for at least 5 years and
 - The taxpayer qualifies for the 10% federal QOF exclusion
 - 15% of the deferred capital gain if
 - The WQOF investment was held for at least 7 years and
 - The taxpayer qualifies for the 15% federal QOF exclusion
- ▷ **Note:** Any failure by a WQOF may result in the WI subtraction or basis modification being denied for investors



WQOF

Resources:

- ▷ Common Questions:
<https://www.revenue.wi.gov/Pages/FAQS/ise-qualified-zones.aspx>
- ▷ Fact Sheet 1121:
<https://www.revenue.wi.gov/DOR%20Publications/1121opportunityzone.pdf>
- ▷ 2023 Form WQOF instructions:
<https://www.revenue.wi.gov/TaxForms2023/2023-FormWQOF-inst.pdf>
- ▷ Sections 71.05(25m), 71.26(3)(vm), 71.34(1k)(p), and 71.45(2)(a)21., Wis. Stats.



Worker Misclassification

- ▷ Every person who pays an individual for work must classify the individual as either an employee or independent contractor.
- ▷ Classification is important because it impacts the payer's requirements for:
 - Federal unemployment insurance, income tax withholding, and information return reporting.
 - WI unemployment insurance, income tax withholding, and information return reporting



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Worker Misclassification

- ▷ Misclassification may result in one or more of the following:
 - A penalty equal to the amount of tax that the payer intentionally failed to withhold.
 - \$25,000 fine for willfully misclassifying a construction worker as a nonemployee.
 - \$10 penalty per incorrect or incomplete Form W-2 or 1099.
 - \$50 or \$150 late filing fee.
 - 25% penalty for negligently failing to withhold or filing incorrectly.
 - 1.5% interest per month for delinquent withholding.
 - Disallowed wage expense deduction for failure to file wage statements.
 - \$10,000 fine and/or 9-month prison sentence for willfully failing or refusing to withhold or willfully rendering a false or fraudulent wage statement or report.
- ▷ For more information, see the article on pages 11-12 of WI Tax Bulletin 222.



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Income Tax Form/Processing Updates and Filing Tips



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Form Changes

- ▷ Form 1NPR Instructions – Numerous improvements made
- ▷ Schedule M instructions – Numerous improvements made
- ▷ Schedule FC – Added line for taxpayers to enter farmland preservation agreement contract numbers
- ▷ Schedule MI – Eliminated because manufacturing investment credit had a 15 year carry forward beginning in 2008. Last year to claim credit was 2022
- ▷ Commercial loan exemption
 - Form 5S, Page 5 – New line 18 for tax-exempt income from commercial loans
 - Schedule 5K-1, page 4 – New line 18 for tax-exempt income from commercial loans
 - Form 6, Page 7 – Added specific code to "Other subtractions" on Part II, line 4n-a
 - Schedule 4W – New line 14 for "Financial institution commercial loan exemption"



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Form Changes

- ▷ Schedule OS instructions, *Credit for Net Tax Paid to Another State*
 - Added instructions to clarify whether to compute the credit in Part II or Part III of the form when the individual is a member of a pass-through entity that pays tax at the entity level in another state, but does not elect to pay tax at the entity level in WI.
- ▷ Schedule I instructions – Pending outcome of WI SB 389 / AB 406
- ▷ Reportable transaction address change – From 8958 to 8906
- ▷ Payments – PO Box 93208 was replaced with PO Box 3028 last year. Payments were forwarded to the correct PO Box, but the forwarding service has expired so payments sent to PO Box 93208 will be returned to taxpayers which could result in a late payment, interest, and penalties.



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2023 Filing Season Tips – Individual Income Tax

- ▷ Be sure to include all forms, schedules and attachments with return
 - Software providers are required to allow attachments to e-filed returns
- ▷ Verify estimated payments and credit carryforward prior to filing
- ▷ Review adjustment notices from prior year to ensure you are using the most updated information
- ▷ Omit nontaxable wages from married couple credit calculation (e.g., military pay subtraction)
- ▷ Returns claiming credits passed through from a partnership or S-Corp may be held if partnership or S-Corp has not yet filed
- ▷ Make sure appropriate documentation for contributions or adjustments from pass-through entities (e.g., Schedule SB lines 43-49) are included with return submission



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2023 Filing Season Tips – Individual Income Tax

- Include Schedule U, *Underpayment of Estimated Tax*, on individual income tax return if income earned unevenly throughout the year AND has underpayment interest
 - *Example:* Taxpayer took a large distribution from a retirement account in November and did not have withholding. DOR will assume income is earned evenly throughout year for purposes of computing underpayment, UNLESS Schedule U is filed.
- Check FEINs on W-2s to ensure they are accurate. FEINs autofill in software from year to year, but businesses (employers) may change FEIN.
- Veterans and surviving spouses property tax credit: property taxes must be paid by December 31st. If veteran has passed away during the year the surviving spouse must get recertification from DVA.



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2023 Filing Season Tips – Individual Income Tax

- Verify certificate of compliance number entered for farmland preservation claims (Sch FC-A) & don't include dashes in number
- Verify farmland preservation agreement numbers entered for farmland preservation claims (Sch FC) & don't include dashes in the number



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2023 Filing Season Tips – Pass Through Entities

- Nonresident individuals part of multiple business (i.e., income from multiple sources) should not be included on composite individual returns (Forms 1CNP or 1CNS); they should file a 1NPR.
- Entity-level tax election: Copies of other state returns should be attached to return when claiming credit for taxes paid to other states – computed on Schedule ET-OS and attached to Form 2, 3, or 5S.
- Manufacturing Credit: Include parcel numbers when submitting Schedule MA-M
- Pass-through withholding tax withheld from lower-tier entity should be entered on Part 1A of Form PW-1 – Do not enter FEIN in Part 1A for the entity filing the PW-1



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2023 Filing Season Tips – Pass Through Entities

- ▷ Attach credit schedules when filing electronically (e.g., attach Schedule FC/FC-A, *Farmland Preservation Credit*, to the Form 2, *Fiduciary Income Tax for Estates and Trusts*)
- ▷ Form 2 for periods longer than 12 months are not accepted
- ▷ Forms 1CNP/CNS, Composite Partner/Shareholder Individual Income Tax Returns: Do not duplicate SSNs on Schedule 2



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Sales and Use Tax Update



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Sales and Use Tax Rate Increase

2023 Wis. Act 12

- ▷ Effective for sales and purchases on or after January 1, 2024
- ▷ City of Milwaukee imposes new 2% sales and use tax
- ▷ Milwaukee County sales and use tax increases from 0.5% to 0.9%
- ▷ Applies to retailers registered to collect Wisconsin sales and use tax making taxable sales to these locations, **regardless of retailer's location** (unless an exemption or small seller exception applies)



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Reminder - Baseball Stadium Sales and Use Tax

- ▷ Baseball stadium tax ended March 31, 2020
- ▷ Tax collected for periods after sunset date must be returned to customer or to DOR if customer cannot be located (penalties may apply)
- ▷ Review client records
 - DOR continues to receive complaints of retailers, primarily restaurants, that continue to collect the 0.1% baseball stadium tax



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Real Property Construction Activities

2023 Wis. Act 12

- ▷ Effective June 22, 2023
- ▷ The definition of real property construction activities is amended
- ▷ The definition no longer requires a determination to be made based on the intent of the purchaser as long as DOR identifies classification of property by administrative rule
- ▷ Gives DOR authority to determine by rule whether tangible personal property that is affixed to real property is a real property construction activity



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New Exemption – Qualified Data Centers

2023 Wis. Act 19

- ▷ Create sec. 77.54(70), effective October 1, 2023
- ▷ Wisconsin Economic Development Corporation (WEDC) may contract with a business to certify a qualified data center for purposes of claiming the sales tax exemption for:
 - Tangible personal property used exclusively for development, construction, renovation, operation, etc., of a qualified data center
 - Tangible personal property used for water cooling or conservation systems exclusively for qualified data centers
 - Tangible personal property sold to a construction contractor and transferred to a qualified data center as a component in real property construction



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New Exemption – Qualified Data Centers

2023 Wis. Act 19

- ▷ The exemption is not available until a data center is certified by WEDC
- ▷ DOR will provide additional information about claiming the exemption when a qualified data center is certified by WEDC



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Retailer's Discount

2023 Wis. Act 19

- ▷ Effective for taxes payable on or after October 1, 2023
 - Discount increased from 0.5% to 0.75%
 - Limit of a retailer's discount increased from \$1,000 to \$8,000 per reporting period
- ▷ Computation: If the total sales tax is
 - \$0 to \$10; the discount is equal to total sales tax
 - \$10 to \$1,333; the discount is \$10
 - Greater than \$1,333; the discount is the total sales tax amount times 0.0075 but cannot exceed \$8,000 per reporting period



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Wisconsin Rate and Boundary Database Files

- ▷ DOR created a database using street address information from property tax records
- ▷ Added premier resort area and local exposition taxes to downloadable rate and boundary files
 - **Note:** Premier resort area and local exposition taxes are not included on the files available on the Streamlined Sales Tax Governing Board's website.
- ▷ Created a guide to aid in understanding the information in the updated rate and boundary files when programmed in computer systems
- ▷ <https://www.revenue.wi.gov/Pages/SSTP/ratebound.aspx>



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Wisconsin State and Local Sales Tax Rate Look-Up

- ▷ Updated look-up tool to determine proper jurisdiction and tax rate by searching:
 - A street address and the 5-digit zip code, or
 - A 9-digit zip code (Zip+4)
- ▷ Search results will provide general sales and use tax rates (state, county, city) and special local taxes (premier resort, local exposition) for each jurisdiction
- ▷ Street address + 5-digit zip code search is only available for transaction dates beginning on or after 10/1/2023
- ▷ Effective January 1, 2024, retailers may no longer use a 5-digit zip code without a street address to determine jurisdiction and tax rate for a transaction.
- ▷ <https://www.revenue.wi.gov/Pages/Apps/strb.aspx>



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Disregarded Entity's Business Assets

- ▷ A single-owner entity that is disregarded as a separate entity for Wisconsin income and franchise tax purposes under Ch. 71, Wis. Stats., is disregarded as a separate entity for sales and use tax
- ▷ Transactions between the owner and its disregarded entity are disregarded for sales and use tax purposes (i.e., not a "sale" transaction). See sec. 77.51(14g), Wis. Stats.



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Disregarded Entity's Business Assets

- ▷ **Caution:** A sale of an interest in a disregarded entity to an unrelated 3rd party is considered the sale of business assets and subject to tax, unless an exemption applies.
- ▷ One exemption that may apply is the occasional sale of business assets
 - See sec. [Tax 11.34](#), Wis. Adm. Code
 - See [Fact Sheet 2110](#), *Occasional Sales of Business Assets for Examples*.

Note: If the sale of an asset qualifies for the occasional sales exemption, the purchaser is not required to remit use tax on the asset purchase.



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Disregarded Entity's Business Assets

Example: Company A is the single owner of a disregarded entity (LLC). LLC purchased assets (e.g., office equipment, furniture) for use in LLC's business activities. At a later date, Company B, an unrelated entity, purchased 100% of Company A's interest in LLC. Later, LLC sells one-half of its business assets to Company B.

Treatment of the transactions:

1. LLC purchases business assets – Purchases are subject to tax, unless an exemption applies (e.g., manufacturing)
2. Company A sells 100% of its disregarded LLC interest to Company B – The sale is considered a sale of assets by Company A to unrelated Company B and is subject to tax unless an exemption applies (e.g., occasional sale of business assets)
3. LLC sells ½ of the business assets to Company B – The sale is not recognized as a sale for tax purposes because LLC is disregarded entity of Company B for tax purposes



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Temporary Event Reporting

- ▷ We continue to identify and educate temporary event operators (persons who arrange, organize, promote or sponsor an event) on requirement to report the event and participating vendors
- ▷ Temporary event is an activity at one place of operation for a brief duration where taxable sales are made
- ▷ Form S-240, *Wisconsin Temporary Event Report* (rev. June 2022) is the only accepted reporting method
- ▷ Penalties may be assessed for failure to report vendors attending temporary events



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Marketplace Providers and Sellers

Administrative Rule Changes – effective July 1, 2023

- ▷ Renamed sec. Tax 11.55, Wis. Adm. Code from "Agents, consignees, lienors, and brokers" to "Repossessions and sales of property to enforce liens."
- ▷ Repealed sec. Tax 11.55(1) and (2), Wis. Adm. Code relating to disclosed and undisclosed principals.
 - Persons selling products and services on behalf of others are retailers and must collect tax regardless of whether the person they are selling on behalf of is disclosed to the purchaser.
 - Agents, cosigners, and brokers are often "marketplace providers" under the provisions created in 2019 Wisconsin Act 10, effective January 1, 2020.
- ▷ Repealed and recreated sec. Tax 11.88(6), Wis. Adm. Code, "Consignment sales," to explain that a recreational vehicle dealer that advertises and sells a recreational vehicle on behalf of another person is a marketplace provider and required to collect and remit the tax.



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Marketplace Providers and Sellers

- ▶ Created sec. Tax 11.555, Wis. Adm. Code, which includes:
 - The marketplace provider's requirement to notify the seller they are collecting and remitting tax.
 - Who can be audited and held liable for the tax.
 - Requests for waiver from marketplace provider responsibilities.
 - DOR may regard the marketplace seller as a retailer in certain situations.
 - Marketplace provisions apply to both online and physical marketplaces (e.g., stores).
 - Reporting and recordkeeping requirements, such as filing returns, exemption certificates, bad debt deduction, and nexus provisions (i.e., small seller exception).
 - A marketplace provider is required to collect and remit tax on taxable sales it facilitates on behalf of a nonprofit organization, even if the nonprofit organization would qualify for the occasional sales exemption had it made its own direct sales to customers.



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Litigation

Oshkosh Corporation: Dane County Circuit Court, June 29, 2023

- ▶ Issue – Whether indirect materials (office equipment and supplies) used in fulfilling contracts with the federal government were purchased by the taxpayer for resale if only the title to, but not possession of, the indirect materials passes to the federal government.
- ▶ Tax Appeals Commission (TAC) concluded:
 - "Sale" in sec. 77.51(14), Wis. Stats., includes the transfer of ownership of, title to, possession of, or enjoyment of tangible personal property
 - Title transfer alone is sufficient to constitute a sale
- ▶ The Circuit Court affirmed the TAC's Final Ruling and Order.
- ▶ The department will not appeal this decision.



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Litigation

StubHub Inc: Wisconsin Tax Appeals Commission, February 28, 2023

- ▷ Issue - Is sales tax due on secondary ticket sales.
- ▷ Commission concluded:
 - StubHub operated an online marketplace for ticket sales and acted as a retailer, selling tickets to taxable events in Wisconsin, such as amusement, athletic, entertainment, and recreational events.
 - StubHub was liable in the alternative for sales tax with ticketholders who listed tickets on its online marketplace.
 - StubHub met the nexus criteria for being subject to the state's sales tax laws.
 - The penalty imposed by the department was not justified by the facts, law, or relevant publications at the time of the transactions.
- ▷ Taxpayer has appealed.



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Litigation

Citations Partners LLC: Wisconsin Supreme Court, March 1, 2023

- ▷ Issue – Is the total amount paid for an aircraft lease taxable or is the portion attributable to aircraft maintenance and engine maintenance excluded from tax?
- ▷ Tax Appeals Commission (TAC) ruled the cost of maintenance services and repair parts is expense of lessor, which is included in the "sales price" of the leases.
- ▷ Circuit Court overturned TAC decision
- ▷ Court of Appeals reversed the Circuit Court decision stating tax cannot be avoided by dividing up lease price into categories or affixing labels.
- ▷ Wisconsin Supreme Court affirmed the Court of Appeals' decision



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Litigation

Green Cab of Madison, Inc.: Circuit Court of Dane County, February 14, 2023

- ▷ Issue - Are lease of taxicabs subject to 5% state rental vehicle fee under sec. [77.995\(2\)](#), Wis. Stats.
- ▷ WTAC concluded:
 - Taxicabs are Type 1 motor vehicles
 - Taxpayer's primary business is rental of driverless vehicle to independent contractor, licensed taxi drivers
 - Rental of driverless vehicles licensed as a taxicab to a driver holding a valid taxicab driver's permit is subject to the state rental vehicle fee
- ▷ Circuit Court agreed that Green Cab's main business involved short-term vehicle rentals without drivers.
- ▷ The time for Green Cab to appeal the Circuit Court's decision has expired, and as no appeal was filed, the decision is now final.



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Litigation

William Becker: Court of Appeals District 1, July 25, 2023

- ▷ Issue - Are trailers "truck bodies" for purposes of sales tax exemption under sec. [77.54\(5\)\(a\)\(4\)](#), Wis. Stats.
- ▷ Taxpayer sold single-axle, tandem-axle, and gooseneck trailers designed to be used with a motor vehicle (car or pickup truck)
- ▷ WTAC ruled trailers did not qualify for the exemption:
 - *Trudell* decision limits "trucks and truck bodies" exemption
 - Trailer type vehicles sold by Becker have no trucks for which the truck bodies were made
- ▷ Circuit Court found trailers sold are "truck bodies" and qualify for the exemption
- ▷ Court of Appeals found trailers sold by Becker were **not** "truck bodies"
- ▷ Taxpayer has appealed to the Supreme Court



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Litigation

Verizon Connect NWF, Inc.: Wisconsin Tax Appeals Commission, October 2, 2023

- ▷ Issue - Are fleet management services which gather, analyze, and translate data, and generate reports from vehicle on-board diagnostic systems to an online platform available to customers subject to sales and use tax?
- ▷ WTAC concluded:
 - These fleet management services in *its entirety* are taxable inspection services under sec. 77.52(2)(a)10., Wis. Stats.
 - The fleet management services performs the same diagnostic functions as a mechanic in a modern garage
 - The *Janesville Data* case is not controlling because the facts of that case were significantly different
 - The receipt of the final reported information is the primary purpose of the services and the primary reason customer pay for those services



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Unclaimed Property Updates



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Unclaimed Property: Holder Updates

- ▷ Holder reports are due November 1 every year.
- ▷ Holders may request up to a 60-day extension to file the report and remit unclaimed property through My Tax Account. *Caution:* extension requests must be received prior to the November 1 deadline.
- ▷ The Voluntary Disclosure Agreement program for holders ran from February 1, 2022 through February 28, 2023. A total of 740 agreements were completed during this period.
- ▷ Late-filed reports are subject to \$150 penalty. Late payments are subject to a penalty equal to 15% of the value of the property. DOR may impose a further \$100/day penalty for each day past the due date of a written request by DOR to pay or deliver property.
- ▷ DOR will be sending requests to file and educational letters to holders who have not remitted timely reports.



Unclaimed Property: Statistics

- ▷ The Unclaimed Property Program is experiencing record growth as a result of the outreach related to holder filing requirements.
- ▷ Increase in Property Counts and Money Reported (FY 2022 – FY 2023)
 - Properties Reported: 705,767 → 728,059
 - Money Reported: \$99,078,598 → \$101,620,656
 - Claims: 37,577 → 53,081
 - Money Claimed: \$31,272,401 → \$40,356,473



Unclaimed Property: Litigation

- ▷ *Delaware v. Pennsylvania and Wisconsin, et al.* (United States Supreme Court, February 28, 2023), aka The MoneyGram Case.
- ▷ The issue was whether abandoned proceeds from official checks are sent to the unclaimed property agency of the State in which the owning corporation is incorporated or the state in which the property was purchased.
- ▷ The court found that the abandoned official checks must be reported to and given to the unclaimed property agency of the state where the products were purchased. This means that official checks purchased in Wisconsin will now be reported to and provided to the State of Wisconsin.



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101

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102

Personal Property Tax

Wisconsin Act 12



103

Exempt Personal Property

- ▷ 2023 Wisconsin Act 12
- ▷ Effective – January 1, 2024
- ▷ Exempts personal property from taxation beginning with assessments as of January 1, 2024



104

Exempt Personal Property

- ▷ Establishes a process for municipalities to request DOR adjust the base values of Tax Incremental Districts (TIDs) for personal property
- ▷ Provides a process for manufacturing establishments that do not own real property in this state to continue claiming the manufacturing income tax credit
- ▷ Moves the airline hub exemption from Ch 70 to Ch 76
- ▷ Creates aid payments to taxing jurisdictions for the loss of property tax revenue



105

Exempt Personal Property

- ▷ Exemption applies to:
 - Personal property as defined in sec. 70.04, Wis. Stats.
 - Steam and other vessels, furniture, and equipment
- ▷ Sec. 70.04, Wis. Stats. – definition of personal property. In chapters 70 to 79, "personal property" includes all of the following:
 - (1g) All goods, wares, merchandise, chattels, and effects, of any nature or description, having any real or marketable value, and not included in the term "real property," as defined in s. 70.03



106

Exempt Personal Property

- ▷ Sec. 70.04, Wis. Stats. – definition of personal property. In chapters 70 to 79, "personal property" includes all the following:
 - (1r) Saw logs, timber, and lumber, either upon land or afloat; steamboats, ships, and other vessels, whether at home or abroad; ferry boats, including the franchise for running the same; ice cut and stored for use, sale, or shipment; and manufacturing machinery and equipment, as defined in s. 70.11 (27)
 - (2) Irrigation implements used by a farmer, including pumps, power units to drive the pumps, transmission units, sprinkler devices, and sectional piping
 - (3) An off-premises advertising sign. In this subsection, "off-premises advertising sign" means a sign that does not advertise the business or activity that occurs at the site where the sign is located



107

Taxable Real Property

- ▷ Exemption does not apply to real property as defined in sec. 70.03, Wis. Stats.
 - (1) In chs. 70 to 76, 78, and 79, "real property," "real estate," and "land" include not only the land itself but all buildings and improvements thereon, and all fixtures and rights and privileges appertaining thereto, except as provided in sub. (2) and except that for the purpose of time-share property, as defined in s. 707.02 (32), real property does not include recurrent exclusive use and occupancy on a periodic basis or other rights, including, but not limited to, membership rights, vacation services, and club memberships
 - (2) "Real property" and "real estate" do not include any permit or license required to place, operate, or maintain at a specific location one or more articles of personal property described under s. 70.04 (3) or any value associated with the permit or license



108

Taxable Real Property

- ▷ Exemption does not apply to:
 - Manufactured and mobile homes (not otherwise exempt)
 - Buildings, improvements, fixtures on leased lands, exempt lands, forest croplands, managed forest lands
 - Must be assessed as real property under 70.17(3) starting 2024



109

Buildings, Improvements and Fixtures

- ▷ Starting January 1, 2024, 70.17(3) requires real property assessment for buildings, improvements and fixtures when located on:
 - Leased lands – the landowner leases the land to a tenant who owns a building, improvement or fixture on that land
 - Exempt lands – taxable building, improvements and fixtured on exempt land:
 - 70.174 – provides that improvements on land owned by the United States shall be assessed as real as provided under 70.17 (3)
 - Forest croplands and managed forest lands (MFL):
 - 77.04(1) – buildings on forest crop land shall be assessed as real property
 - 77.84(1) – building, improvements, fixtures on MFL is subject to taxation as real property



110

Leasehold Improvements

- ▷ Leasehold improvements are additions, renovations and similar improvements made to a leased property by the lessee
 - May be real property or personal property
 - Apply state law (70.03, 70.17(3)) and state case law
 - 70.03 defines real property as the land and all buildings, improvements and fixtures
 - 70.17(3) require real property assessment for buildings, improvements and fixtures
 - State court cases provide a three-part test



111

Practitioner Impact

- ▷ Exemption does not impact 2023 and prior personal property taxes
 - No change to 2023 personal property tax bill distribution – by the third Monday in December
 - No change to 2023 personal property tax bill payment date – by January 31, 2024
- ▷ Statements of Personal Property are not required for 2024
 - Act 12 amended 70.35(3) to end collection of the PA-003 with the 2023 assessment
 - *For assessments made before January 1, 2024, each return shall be filed with the assessor on or before March 1 of the year in which the assessment provided by s. 70.10 is made...*



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Resources



- ▷ [WI Act 12 Information – DOR overview/summary of act](https://revenue.wi.gov/Documents/2023-Act12-Information.pdf)
- ▷ [WI Act 12 – Personal Property Exemption information](https://revenue.wi.gov/Documents/2023-Act12-PersonalPropertyExemption.pdf)
- ▷ [TID Base Value Adjustment Request Due to Personal Property Exemption](#)



Personal Property Repeal – Contact Info

- ▷ Property assessment – bapdor@wisconsin.gov
- ▷ Manufacturing
 - Income tax credit – DORFranchise@wisconsin.gov
 - Property assessment – contact the [district office](#) where the property is located
- ▷ Airlines, railroads, telecommunications and utilities – utility@wisconsin.gov
- ▷ Aid payments, local government finance – lgs@wisconsin.gov
- ▷ Tax incremental finance (TIF) – tif@wisconsin.gov



Other Updates



Filing Tips – Sales & Withholding

- ▷ Include city and county sales tax, if applicable
- ▷ Seller permit site locations being updated timely will assist sales tax processing
- ▷ Fiscal-year filers with a quarterly or annual period start date in 2023 and a period end date in 2024, and have Milwaukee County Tax due, will be required to file on paper for the one period
- ▷ 1099s with withholding must be filed to DOR by January 31st! Combined fed-state cannot be used in this case
- ▷ Filing 1099s without withholding directly to Wisconsin by January 31st, will assist fraud prevention and expedite income tax return and refund processing
- ▷ \$10 penalty issued for failing to file W-2s/1099s, filing late, or failing to file electronically if 10 or more filed on paper



Payroll Service Providers Schemas

- ▷ All software providers and transmitters MUST support the Enrollment schema if they are submitting withholding returns via XML. You can find the EnrollmentDataExchangeV2.0 schema package in the Wisconsin Withholding folder in the FTA State Exchange System. DOR uses the same schema in two distinct ways:
 - 1. Payroll service providers submitting their client lists for withholding tax filing
 - 2. Payroll service providers submitting client lists to facilitate the automated issuance of wage attachment orders and process employer responses
- ▷ The department will provide a 3 month testing window where all providers will be required to test and be accepted. We will notify you when it is time for you to begin testing.
- ▷ Voluntary registration is open, contact DORDeveloperRelations@wisconsin.gov



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Payroll Service Providers Schemas

- ▷ Wage Attachment schema will provide an electronic notice to let DOR know of the employers the PSP represents for doing Wage Certifications/Levies on their clients' employees' wages. DOR will note the PSP authority to do E-Wage Certs on behalf of the customer.
- ▷ Electronic Notice schema provides real time electronic notification of letters going to clients. There is an electronic summary of the notice and a pdf copy of the letter with the schema. Withholding notices include file frequency changes, bills, or other notices.
- ▷ Providers must support the enrollment schema and wage attachments schema to be approved for the notice schema.



118

You Are A Target! Protect Your Clients; Protect Yourself

- ▷ Accounting firms hold valuable client data and e-filing credentials which make them the target of cybercriminals
- ▷ Spear phishing scams from those posing as clients, tax software or cloud storage providers and the IRS are common
- ▷ Each year Wisconsin firms fall victim to these scams. Stolen data can be misused for years to come.
- ▷ Security guides and other resources are available on the IRS's [Identity Theft Information for Tax Professionals](#) page
- ▷ Be on the lookout for data theft red flags:
 - ▷ Increase in rejects because a return was already filed
 - ▷ Clients receive IRS or state authentication letters when they haven't yet filed a return
 - ▷ Clients receive unexpected refunds, transcripts or notices about IRS online accounts
 - ▷ Number of returns e-filed with your EFIN or PTIN exceed the number you submitted
 - ▷ You receive responses to emails you did not send
 - ▷ Unusual computer activity (e.g., running slower, lockouts, cursor moving)



119

Data Breach Reporting

- ▷ **IRS Stakeholder Liaison:** liaison will notify IRS Criminal Investigation and others within the agency. For Wisconsin, contact CL.SL.Area.6@irs.gov or 206-946-3703.
- ▷ **States in which you prepare state returns:**
 - ▷ Wisconsin: email DORIDTheft@Wisconsin.gov. Include your organization's name, brief description of the incident and contact information for the individual who will be working with DOR. Do not include personally identifiable information (PII) for impacted employees or customers in your email. DOR's fraud team will contact the firm (typically the same day) to discuss next steps.
 - ▷ Other states: see the Federation of Tax Administrator's [Report a Data Breach](#) page for contact information
- ▷ **Local law enforcement**
- ▷ **Security experts:** it's important to determine the cause and scope of the breach and to prevent further breaches from occurring
- ▷ **Affected staff and clients:** Wisconsin statutes require most businesses to notify individuals if an unauthorized person has acquired their personal information. To learn more, see the [Wisconsin's Data Breach Notification Law](#) guide.
- ▷ **Insurance company:** check if your insurance policy covers data breach mitigation expenses



120

Identity Theft Reporting

- ▶ New identity theft reporting form (Form ID-100 Identity Theft Declaration) created in June of 2023
- ▶ Replaces use of DATCP Identity Theft and Non-Consent forms for tax-related ID theft reporting
- ▶ Taxpayers should continue to reach out to DATCP for assistance with credit and consumer issues or education regarding ID theft
- ▶ [Form ID-100](#) is available on DOR's webpage in fillable format but currently must be mailed



Make a Payment Page

- ▶ Expanded [Make a Payment page](#) last year to include major tax types
- ▶ Paying electronically reduces processing time, eliminates risk of lost payments, and reduces risk of misapplied payments
- ▶ Page includes all appropriate payment methods by tax type and links to interactive vouchers
 - Confirm PO Box 3028 is on vouchers printed through your software
- ▶ Quick Pay button takes user directly to MTA screen for making unregistered payments for individual income tax, fiduciary income tax, occasional consumer use tax, and non-tax debt



Make a Payment Page

The screenshot shows the homepage of the State of Wisconsin Department of Revenue (DOR). At the top, there is a navigation bar with categories: ONLINE SERVICES, BUSINESSES, INDIVIDUALS, TAX PROFESSIONALS, GOVERNMENTS, and UNCLAIMED PROPERTY. Below this is a search bar and a message from Secretary Barca. The main content area is divided into three columns: Online Services (with icons for eDelivery, MY tax ACCOUNT, REFUND, RETR, and ID), Business Development (with a map of Wisconsin and the text 'Whether you want to start a new business or expand a current one, BDGR can help you find resources to start, grow & thrive.'), and Quick Links (with links for Forms, Publications, Reports, Owe back taxes, Report tax fraud, and Make a payment). A red arrow points to the 'Make a payment' link in the Quick Links section.

123

Credit Card and Other Payment Options

- ▶ DOR switched to a new credit card payment processing vendor last year
- ▶ New options available as of January 2023: Apple Pay, PayPal
 - Coming Soon: CheckFreePay
- ▶ [DOR Credit Card and Other Payment Options \(wi.gov\)](https://www.wisconsin.gov/dor/credit-card-and-other-payment-options) provides additional information, including fees

124

Continuous Recruitment Efforts-Agents

- ▷ Revenue Agents are responsible for customer service call center, tax return processing, collections, bill adjustments
- ▷ Three successful rounds of continuous recruitment
 - May 2022-September 2022 – 26 hires
 - January 2023 – May 2023 – 37 hires
 - July 2023 – September 2023 – 23 hires
- ▷ Currently, normal vacancy rates of 5% or less
- ▷ Additional initiatives
 - Limited Term Employees – great way to test out the work
 - Re-thinking training to help keep agents learning and growing



125

Continuous Recruitment Efforts-Auditors

- ▷ Slow progress over three rounds
 - June 2022-November 2022 – 5 hires
 - January 2023-May 2023 – 9 hires (5 External Gateway Program Completions)
 - August 2023-November 2023 – in progress – goal: 20
- ▷ Vacancy rate for auditors is still high
- ▷ Additional Initiatives:
 - Launched an Internal Gateway Program
 - help agents earn their 4-year accounting degree so they can become auditors
 - On campus interviews
 - Trying 2 different campuses this fall



126

My Tax Account (MTA) Updates



127

MTA: Personal Users

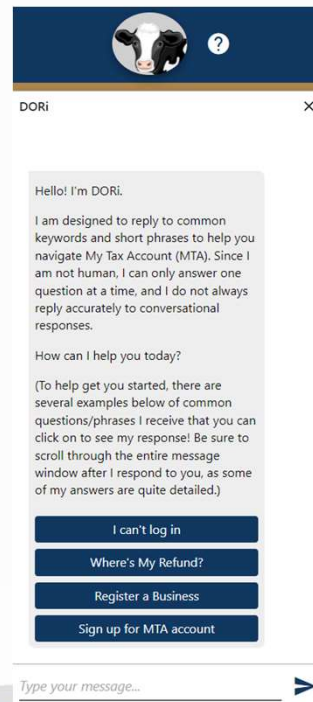
- ▷ Encourage clients to register for My Tax Account (MTA) as personal users
 - Benefits: electronic notice delivery, make/view/cancel estimated payments, check refund status, and more
 - No third-party access yet - when it goes live, your client must have MTA to be able to grant you access, and you must have a valid POA on file with us
 - Email Form A-222 to DORPOA@wisconsin.gov or fax to 608-267-1030
- ▷ WI Identity Protection (IP) PIN
 - Ensures someone cannot file a WI return in your client's name
 - Enrollment is optional and completed via MTA
 - Once enrolled, must list PIN on all future returns (2021 and forward)
 - Different from IRS IP PIN
 - Expires 12/31 each year, new PIN issued in January



128

DORi

- ▶ Virtual assistant (chatbot)
- ▶ Designed to provide automated assistance with My Tax Account navigation and issues
- ▶ Icon on the top of all MTA pages
- ▶ Use the "DORi's answer doesn't make sense" link to help us continuously improve content
- ▶ Tip: use short phrases
- ▶ Not linked to live chat



129

MTA: My Case Manager

- ▶ My Case Manager is available to help you and your clients make the audit process smoother. You can:
 - Follow the progress of the audit
 - Review requests and deadlines
 - Send secure messages back & forth with the auditor
 - Send documents securely (up to 30 MB)
 - Locate the supervisor's contact information
- ▶ Resources:
 - [Publication 701, My Case Manager User Guide](#)
 - [My Case Manager Common Questions](#)
 - [Audit Web Page](#)

130

MTA – M-Forms & Utility Annual Reports

2023 Filing Season

- ▷ Successful transition of manufacturing forms and utility annual reports to My Tax Account (MTA)
- ▷ Benefits:
 - Familiar – consolidated tax filing to a system most businesses already used to file and pay business taxes
 - Ease of use – MTA allows authorized users to complete many tasks, such as:
 - Request extensions, file returns
 - File/pay manufacturing assessment appeals, make penalty payments
 - Modify and manage user access
 - Secure – no downloading forms using third-party software



131

MTA – Mfg. Assessment Appeals

- ▷ File appeal and pay fee within My Tax Account (MTA)
- ▷ More timely, efficient and cost effective (saves paper, postage, and more)
- ▷ MTA also alerts you of any fees you owe
- ▷ To file an appeal:
 - Go to My Tax Account
 - Select Manufacturing Real Estate Account
 - Click File/View Return
 - Click Appeal in the top right corner



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MTA – Manufacturing Forms

2024 Filing Season

- ▷ Manufacturing Real Estate form – only form to file due to 2023 Act 12 personal property repeal
- ▷ Forms no longer required include:
 - Manufacturing Personal Property return (Form M-P)
 - Wisconsin Leased or Loaned Personal Property return (Form M-L)
- ▷ SLF's Manufacturing bureau:
 - Working to move buildings on leased land from personal property to real estate
 - Will continue to classify business activity as manufacturing for the purpose of DOR ISE's administration of the manufacturing and agriculture income tax credit



133

WisTax: Replacing WI e-file

- ▷ Retiring WI e-file and adding Form 1 and Schedule CC filing to WisTax
 - WisTax is part of unregistered My Tax Account (no username/password required)
 - MeF no longer available for Schedule CC
- ▷ Homestead credit claimants must file Schedule H separately from Form 1 if using WisTax
- ▷ Not allowed in WisTax:
 - Amended returns
 - Form 1NPR
 - Prior-year returns
 - Various schedules
- ▷ WI participating in the Free File Alliance

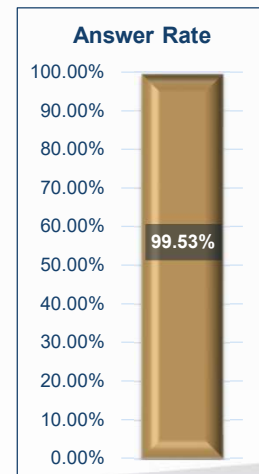
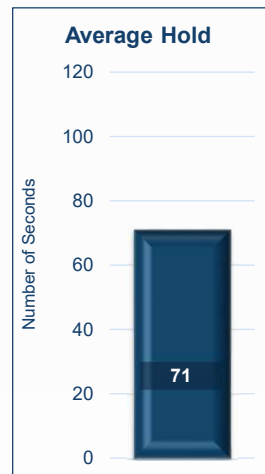
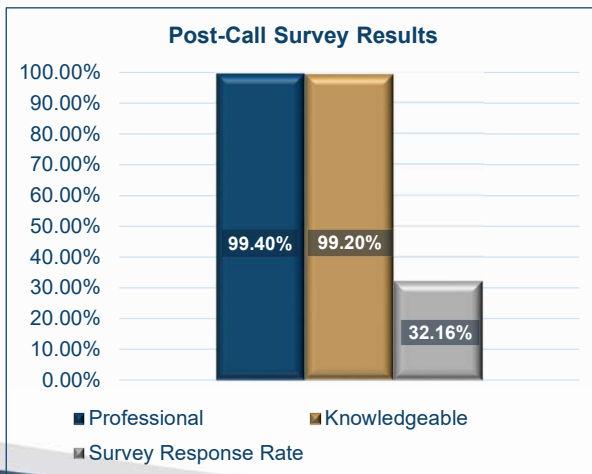


134

Statistics

FY23 IS&E Division Phone Statistics

▷ 725,705 calls handled*



*includes outbound calls

DOR Initiatives – ID Verification

	FY23	FY22	FY21	FY20
Returns Evaluated	3,157,506	3,150,305	3,453,483	2,875,034
Quizzes Required	3,671	4,362	2,352	3,083
PINs Required	52,135	56,373	39,226	36,480
ID Docs Required	4,829	6,870	3,263	4,931
ID Docs Reviewed	6,306	5,764	4,059	6,597
Total ID Verification Actions Required	60,635	67,605	44,841	44,494
% of Returns Evaluated Requiring ID Verification	1.92%	2.15%	1.30%	1.55%
Refunds Denied for Failure to Verify ID	23,896	10,994	6,387	12,198



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DOR Initiatives – Bad Refunds Stopped

Bad Refunds Adjusted/Stopped	Fraud Detection With Analytics	Processing Fraud - OCI	Processing Fraud - Tax Ops	Earned Income Credit	Homestead Credit	Total for Specific Initiatives
FY23	\$12,009,837	\$296,182,433*	\$9,126,383	\$21,113,030	\$18,943,325	\$357,375,008
FY22	\$5,705,235	\$10,571,743	\$6,662,514	\$23,387,279	\$23,197,939	\$69,524,710
FY21	\$3,190,632	\$9,878,995	\$4,631,190	\$19,748,512	\$24,148,497	\$61,597,826
FY20	\$5,613,849	\$7,940,577	\$2,656,902	\$8,123,852	\$4,776,598	\$29,111,778
FY19	\$8,595,686	\$5,970,625	\$6,020,804	\$20,436,036	\$14,358,603	\$55,381,754
FY18	\$7,052,669	\$5,869,413	\$5,628,995	\$17,943,046	\$14,862,551	\$51,356,674
FY17	\$9,300,745	\$6,059,255	\$8,044,070	\$20,134,976	\$16,046,799	\$59,585,845
FY16	\$11,149,599	\$8,092,817	\$6,849,591	\$19,946,592	\$17,004,928	\$63,043,527
FY15	\$11,050,119	\$7,335,531	\$6,889,513	\$16,682,990	\$15,828,093	\$57,786,246
FY14	\$3,550,473	\$4,904,089	\$8,195,222	\$17,710,656	\$15,299,425	\$49,659,865
FY13		\$3,434,613		\$14,257,838	\$12,480,794	\$30,173,245
FY12		\$1,702,300		\$9,341,511	\$14,694,458	\$25,738,269
						\$910,334,747

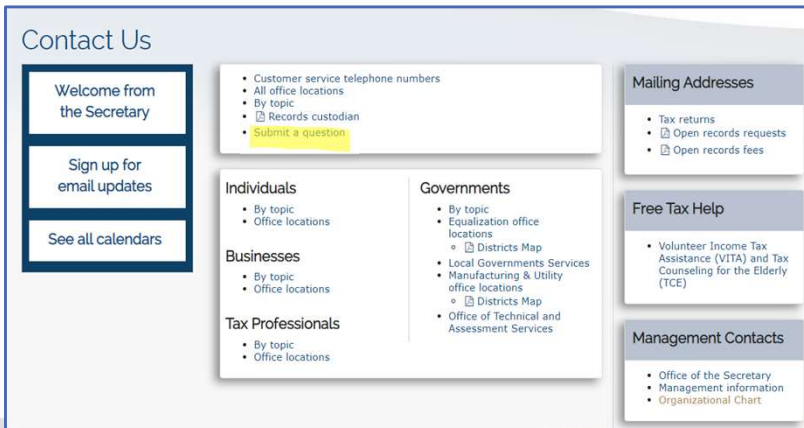
*FY23 OCI figure includes \$279,946,028 from one fraudulent return



138

Contact Us

- ▷ Visit the "Contact Us" page to find contact information for various areas of DOR
- ▷ Use the "Submit a question" link to email us



Submit a Question

- ▷ Subject helps route questions to the appropriate staff to handle

Submit a Question

For questions about responding to an identity verification letter, see our [Identity Verification page](#).

If you searched our website, tried the [refund inquiry](#) option, and still have questions or comments, send the Wisconsin Department of Revenue (DOR) an email using the form below.

Provide **all** the requested information in the boxes below. Do not include any **confidential** information in the message box. We will use the information to reply to your inquiry.

DOR responds to all questions during **normal business hours**; however, we cannot always respond immediately. For the quickest response, be sure to provide us your correct email address. Also, if you have suggestions to improve our website, use this form to submit your comments to our Webmaster.

* Indicates a required field.

***Name/Business Name**

***Daytime Telephone Number** (between 7:45-4:30)

***Street Address**

***Email Address**

***City, State, Zip**

***Last 4 of SSN/FEIN**

***Subject**

***Message**

Submit Message Clear

General "Submit a question" link will show all available subjects in dropdown



Submit a Question

- ▶ To see a filtered list of subjects, choose "By topic" from the "Contact Us" page, choose the topic, then select the email link

The screenshot displays the 'Contact Us' page with several sections:

- Contact Us** (Main Header)
- Welcome from the Secretary** (Left sidebar)
- Sign up for email updates** (Left sidebar)
- See all calendars** (Left sidebar)
- Customer service telephone numbers** (List: All office locations, **By topic**, Records custodian, Submit a question)
- Mailing Addresses** (List: Tax returns, Open records requests, Open records fees)
- Free Tax Help** (List: Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE))
- Management Contacts** (List: Office of the Secretary, Management information, Organizational Chart)
- Individuals** (List: **By topic**, Office locations)
- Governments** (List: **By topic**, Equalization office locations, Districts Map, Local Governments Services, Manufacturing & Utility office locations, Districts Map, Office of Technical and Assessment Services)
- Businesses** (List: **By topic**, Office locations)
- Tax Professionals** (List: **By topic**, Office locations)
- Homestead Credit** (Section)
- ID Theft** (Section)
- Individual Income** (Section: PO Box 59, Madison, WI 53785-0001, PO Box 268, Madison, WI 53790-0001, (608) 266-2486)
- Email Questions** (Section: Additional Information)
- Local Government Finance** (Section)
- Subject** (Dropdown menu: Select a subject, Select a subject, Income Tax - Individuals, Withholding Taxes - Pass-Through Income)

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Contact Us

- ▶ Practitioner email address and phone number
 - Do not share with your clients
 - DORTaxPractitioners@wisconsin.gov
 - (608) 261-5199

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Presenter

- ▷ Nate Weber, Director of Technical Services
 - (608) 266-8025
 - nathaniel.weber@wisconsin.gov



Thanks!
Any questions?



11 a.m. – 12 p.m.

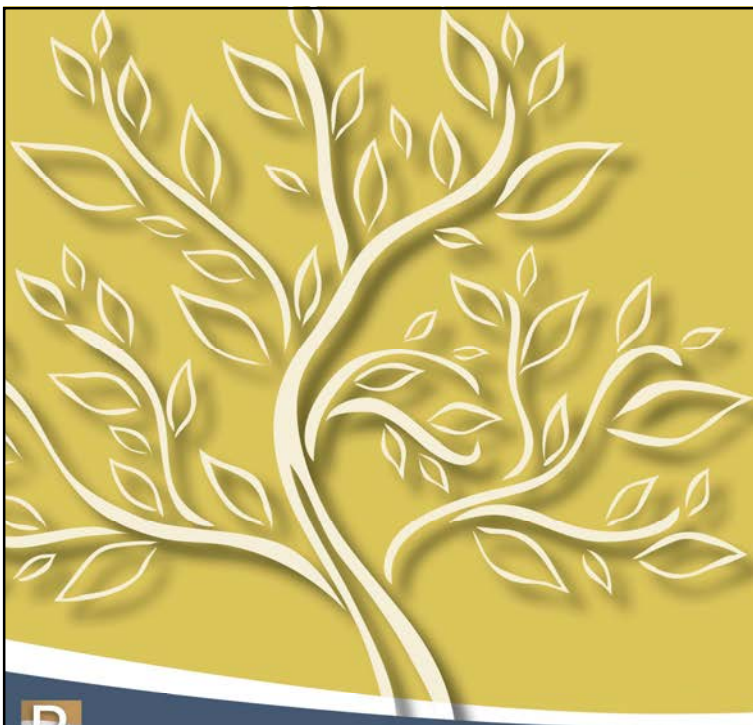
Entity-Level Tax Election & Other State Tax Credit

Joseph Wasicak, CPA, *Technical Specialist, Wisconsin
Department of Revenue*



Pass-Through Entity-Level Tax Election and Wisconsin's Credit for Taxes Paid to Another State

WI Department of Revenue | Division of Income, Sales, and Excise Tax
Fall 2023



Mission

Strengthen Wisconsin through fair tax and lottery administration, while educating and serving the public, our customers and communities.

Vision

To be the premier agency in providing innovative, accessible resources, and exceptional customer service built on a foundation of trust, inclusivity and creativity.

Values

- Integrity
- Innovation
- Inclusivity
- Knowledge
- Empathy
- Security



Topics

- ▷ Wisconsin's Pass-Through Entity-Level Tax Election Overview
- ▷ Different State Pass-Through Entity-Level Tax Elections
- ▷ Claiming Wisconsin's Credit for Taxes Paid to Another State with the Pass-Through Entity-Level Tax Election



3

Wisconsin's Pass-Through Entity-Level Tax Election Overview



4

Pass-Through Entity-Level Tax (ELT) Election Overview

- ▷ 2017 Wis. Act 368
- ▷ Tax-option (S) corporations and partnerships may elect to pay tax on items that would otherwise be reported by the owner(s)
- ▷ Must have consent from owners who hold an aggregate of more than 50% of the shares (or capital and profits interest) on the day of election
- ▷ Election is made on the entity's Wisconsin tax return



5

Pass-Through ELT Election Overview

- ▷ Election must be made (or revoked) by the extended due date of the return
- ▷ S corporations - taxable years beginning on or after January 1, 2018
- ▷ Partnerships - taxable years beginning on or after January 1, 2019



6

Polling Question 1



Pass-Through ELT Election Overview

2021 Tax Year (Statistics as of July 15, 2023)	
Tax-Option (S) Corporations (Form 5S) Filing Stats	
Tax-Option (S) Corporation returns filed	86,789
Tax-Option (S) Corporation entity-level tax elections filed	6,048
Percent of entity-level tax elections filed	6.97%
Partnership (Form 3) Filing Stats	
Partnership returns filed	85,382
Partnership entity-level tax elections filed	3,009
Percent of entity-level tax elections filed	3.52%
Pass-Through Entity Filing Stats - TOTAL	
Pass-through entity returns filed	172,171
Entity-level tax elections filed	9,057
Percent of entity-level tax elections filed	5.26%



Pass-Through ELT Election Overview

Facts for Calendar Year 2022:

- ▷ Tax-option (S) corporation is 100% owned by Individual A
- ▷ Tax-option (S) corporation makes the election to pay tax at the entity level
- ▷ Individual A is a WI resident and single
- ▷ Federal standard deduction is \$12,950 in 2022
- ▷ WI exemption deduction is \$700
- ▷ Individual A does not have any other sources of income, loss, deduction, etc.
- ▷ Assume all estimated taxes paid and deductible in 2022



- ▷ Reduction in tax:
\$19,767

Tax Year 2022 - SALT Limitation		
	No ELT Election	ELT Election
Wisconsin Form 55		
Income	\$1,000,000	\$1,000,000
Wisconsin tax	\$0	79\$79,000
Federal Form 1120S		
Gross receipts	\$1,000,000	\$1,000,000
Expenses (tax paid)	\$0	(\$79,000)
Income	\$1,000,000	\$921,000
Wisconsin Form 1		
Wisconsin taxable income	\$999,300	\$0
Wisconsin tax	\$69,537	\$0
Federal Form 1040		
Taxable income	\$987,050	\$908,050
Federal tax	\$328,164	\$298,934
Total federal and WI Tax	\$397,701	\$377,934



Polling Question 2



11

Pass-Through ELT Election Overview

- ▷ Section 11042 of Public Law 115-97 (Tax Cuts and Jobs Act) created the federal limitation of \$10,000 when claiming itemized deductions for state and local taxes
- ▷ Provision is set to expire for taxable years beginning on or after January 1, 2026



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▷ Increase in tax:
\$1,171

Tax Year 2022 – No SALT Limitation		
	No ELT Election	ELT Election
Wisconsin Form 55		
Income	\$1,000,000	\$1,000,000
Wisconsin tax	\$0	\$79,000
Federal Form 1120S		
Gross receipts	\$1,000,000	\$1,000,000
Expenses (tax paid)	\$0	(\$79,000)
Income	\$1,000,000	\$921,000
Wisconsin Form 1		
Wisconsin taxable income	\$999,300	\$0
Wisconsin tax	\$69,537	\$0
Federal Form 1040		
Taxable income	\$930,463	\$908,050
Federal tax	\$307,226	\$298,934
Total federal and WI Tax	\$376,763	\$377,934



Polling Question 3



Different State Pass-Through Entity- Level Tax Elections



State	Entity-Level Tax (Optional Election)	Member May Claim Nonrefundable Credit for Allocable Portion of Entity-Level Tax Paid	Member May Claim Refundable Credit for Allocable Portion of Entity-Level Tax Paid	Member May Exclude Allocable Portion of Income Passed-Through from Entity Making Entity-Level Tax Election
Wisconsin	Yes	No	No	Yes
Alabama	Yes	NA	Yes	No
California	Yes	Yes	No	No
Oklahoma	Yes	No	No	Yes



Claiming Wisconsin's Credit for Taxes Paid to Another State with the Pass-Through Entity-Level Tax Election



17

Polling Question 4



18

Claiming Wisconsin's Credit for Taxes Paid to Another State with the ELT Election

▷ Five scenarios to consider when claiming Wisconsin's credit for taxes paid to another state:

1. ELT election made in Wisconsin only
2. ELT election made in other state only (nonrefundable credit for members)
3. ELT election made in other state only (refundable credit for members)
4. ELT election made in other state only (income excludable for members)
5. ELT election made in Wisconsin and in other state



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Claiming Wisconsin's Credit for Taxes Paid to Another State with the ELT Election

▷ ELT election made in Wisconsin only

- Only the pass-through entity may claim the credit (sec. 71.07(7)(b)2., Wis. Stats.)
- Entity's credit is based on net income or franchise tax paid by the entity to another state on that income and the net income tax on that income paid by the entity on behalf of its shareholders, partners, and members that are residents of this state on a composite return filed with the other state against the net income or franchise tax otherwise payable to this state on income of the same year (sec. 71.07(7)(b)3., Wis. Stats.)
- Use Schedule ET-OS, *Credit for Net Tax Paid to Another State*, to claim the credit



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Claiming Wisconsin's Credit for Taxes Paid to Another State with the ELT Election

▷ ELT election made in other state only (**nonrefundable** credit for members)

- In general, the individual Wisconsin members of the pass-through entity may claim the credit for the period they were a Wisconsin resident during the tax year (sec. 71.07(7)(b)2., Wis. Stats.)
- Member's credit is based on the member's allocable share of net income or franchise tax paid by the entity on their behalf
- Individuals use Schedule OS, *Credit for Net Tax Paid to Another State*, Parts III and IV to claim the credit



PART III – Calculation of Credit (Shareholders, Partners, and Members)

Caution: See Instructions

	State 1	State 2
24 Postal abbreviation for state to which tax was paid 24	<input type="text"/>	<input type="text"/>
25 Income taxable to both Wisconsin and other state (see instructions) 25	<input type="text"/> .00	<input type="text"/> .00
26 Total income taxed by the other state (see instructions) 26	<input type="text"/> .00	<input type="text"/> .00
27 Divide line 25 by line 26. Carry the decimal to four places and fill in on line 27. If line 26 is less than line 25, enter 1.0000 27	<input type="text"/> . <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>	<input type="text"/> . <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>
28 From the income tax return of the other state, fill in the net tax amount after subtracting all nonrefundable and refundable credits (see instructions) 28	<input type="text"/> .00	<input type="text"/> .00
29 Multiply line 27 by line 28. Round the result to the nearest dollar. If claiming a credit for net tax paid to Minnesota, Iowa, Illinois, or Michigan, skip lines 30 through 34 and fill in the amount from line 29 on line 36 29	<input type="text"/> .00	<input type="text"/> .00



Claiming Wisconsin's Credit for Taxes Paid to Another State with the ELT Election

▷ ELT election made in other state only (refundable credit to members)

- In general, the individual Wisconsin members of the pass-through entity may claim the credit for the period they were a Wisconsin resident during the tax year (sec. 71.07(7)(b)2., Wis. Stats.)
- Member's credit is based on the member's net income tax paid to the other state on their individual income tax return filed in the other state (sec. Tax 2.955(2)(a), Wis. Adm. Code)
- Individuals use Schedule OS, *Credit for Net Tax Paid to Another State*, Parts I, II, and IV to claim the credit. Do not reduce the net tax on line 22 of Schedule OS by the individual's credit claimed in the other state for tax paid by the entity in the other state.



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Example 1

▷ Facts for tax year 2022:

- Tax-option (S) corporation ABC is 100% owned by individual Shareholder D
- Individual Shareholder D is a full-year Wisconsin resident filing as single
- All of ABC's income is reportable to Alabama
- ABC elects to pay tax at the entity level in Alabama
- ABC does **not** elect to pay tax at the entity level in Wisconsin
- Shareholder D is required to report their allocable share of ABC's items of income, loss, and deductions on their Alabama individual income tax return
- Alabama's ELT election provides for a refundable credit on Shareholder D's Alabama individual income tax return for their allocable portion of tax paid by ABC



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Example 1 (continued)

ABC's Alabama taxable income (ordinary income)	\$100,000
Alabama's pass-through entity-level tax rate (made up for purposes of this example)	<u>6%</u>
ABC's Alabama income tax	\$6,000
Individual Shareholder D's taxable wages in Alabama	\$10,000
Shareholder D's allocable portion of ABC's taxable income	<u>\$100,000</u>
Total Alabama taxable income	\$110,000
Alabama individual tax rate (made up for purposes of this example)	<u>4%</u>
Net Tax	\$4,400
Shareholder D's refundable credit for income tax paid by ABC	<u>(\$6,000)</u>
Shareholder D's individual income tax/(refund)	(\$1,600)



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Example 1 (continued)

▷ Conclusion:

- Shareholder D's Wisconsin credit for taxes paid to another state is based on the \$4,400 net income tax from Shareholder D's Alabama individual income tax return
- Shareholder D uses Schedule OS, Parts I, II, and IV to compute Wisconsin's credit for taxes paid to another state



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PART I – Income From Other State		Postal abbr. →		State 1	State 2
		A	L		
<u>1</u>	Wages, salaries, tips, etc	1		10000.00	.00
<u>2</u>	Business income / loss	2		.00	.00
<u>3</u>	Capital gain / loss	3		.00	.00
<u>4</u>	Other gains / losses	4		.00	.00
<u>5</u>	IRA distributions, pensions, and annuities	5		.00	.00
<u>6</u>	Rental real estate, royalties, partnerships, S corporations, trusts, etc	6		100000.00	.00
<u>7</u>	Farm income / loss	7		.00	.00
<u>8</u>	Unemployment compensation	8		.00	.00
<u>9</u>	Social security benefits	9		.00	.00
<u>10</u>	Other income <input type="text"/>	10		.00	.00
<u>11</u>	Add lines 1 through 10 in each column	11		110000.00	.00



18 Total income taxed by other state – subtract line 17 from line 11 18

PART II – Calculation of Credit (Individual, Estate, or Trust Income Tax)

19 Income taxable to both Wisconsin and other state (see instructions) 19

20 Total income taxed by the other state (see instructions) 20

21 Divide line 19 by line 20. Carry the decimal to four places and fill in on line 21. If line 20 is less than line 19, enter 1.0000 21

22 From the income tax return of the other state, fill in the net tax amount after subtracting all nonrefundable and refundable credits (see instructions) 22

23 Multiply line 21 by line 22. Round the result to the nearest dollar. If tax was paid to another state and passed through to you by a tax-option (S) corporation, limited liability company, or partnership, go on to Part III. Otherwise, skip lines 25 through 29 and go on to Part IV. If claiming a credit for net tax paid to Minnesota, Iowa, Illinois, or Michigan, skip lines 30 through 34 and fill in the amount from line 23 on line 35 23



PART IV - Credit Allowed

30	Income taxable to both Wisconsin and other state (see instructions)	30	110000.00	.00
31	Wisconsin income from Form 1, line 7, Form 1NPR, line 30, or Form 2, see instructions	31	110000.00	.00
32	Divide line 30 by line 31. Carry the decimal to four places and fill in on line 32. If line 31 is less than line 30, fill in 1.0000	32	1 . 0 0 0 0
33	Fill in the Wisconsin net income tax from: • Form 1, line 12, less the amounts on lines 13 through 18 • Form 1NPR, line 46, less the amounts on lines 47 through 49 • Form 2, line 6c, less the amount on line 7	33	5454.00	.00
34	Multiply line 32 by line 33. Round the result to the nearest dollar	34	5454.00	.00
35	Fill in the amount from line 23	35	4400.00	.00
36	Fill in the amount from line 29	36	.00	.00
37	Add lines 35 and 36	37	4400.00	.00



38	Fill in the smaller of line 34 or line 37. If claiming a credit for net tax paid to Minnesota, Iowa, Illinois, or Michigan, fill in the amount from line 37	38	4400.00	.00
39	Add the amounts in each column of line 38. Fill in the total here	39	4400.00	
40	If you have tax paid to more than 2 states, fill in the amount from line 39 of any additional Schedules OS	40		.00
41	Add lines 39 and 40. This is your credit for tax paid to another state (see instructions)	41	4400.00	



Example 2

▷ **Facts:**

- Same facts as example 1, and
- Assume Alabama has 1% franchise tax on ordinary income of a pass-through entity
- There is no individual income tax credit passed through for the franchise tax

ABC's Alabama ordinary income	\$100,000
Alabama's PTE franchise tax rate (made up for purposes of this example)	<u>1%</u>
ABC's Alabama PTE franchise tax	\$1,000



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Example 2

▷ **Conclusion:**

- Shareholder D's Wisconsin credit for taxes paid to another state is based on the \$4,400 net income tax from Shareholder D's Alabama individual income tax return
- Shareholder D uses Schedule OS, Parts I, II, and IV to compute Wisconsin's credit for taxes paid to another state
- **Shareholder D uses Schedule OS, Parts III and IV to report the \$1,000 franchise tax paid by ABC when computing their Wisconsin credit for taxes paid to another state**



32

		State 1		State 2	
PART I – Income From Other State		A L			
		Postal abbr. →			
<u>1</u>	Wages, salaries, tips, etc	1	10000.00		.00
<u>2</u>	Business income / loss	2	.00		.00
<u>3</u>	Capital gain / loss	3	.00		.00
<u>4</u>	Other gains / losses	4	.00		.00
<u>5</u>	IRA distributions, pensions, and annuities	5	.00		.00
<u>6</u>	Rental real estate, royalties, partnerships, S corporations, trusts, etc	6	100000.00		.00
<u>7</u>	Farm income / loss	7	.00		.00
<u>8</u>	Unemployment compensation	8	.00		.00
<u>9</u>	Social security benefits	9	.00		.00
<u>10</u>	Other income <input type="text"/>	10	.00		.00
<u>11</u>	Add lines 1 through 10 in each column	11	110000.00		.00



18 Total income taxed by other state – subtract line 17 from line 11 18

PART II – Calculation of Credit (Individual, Estate, or Trust Income Tax)

19 Income taxable to both Wisconsin and other state (see instructions) 19

20 Total income taxed by the other state (see instructions) 20

21 Divide line 19 by line 20. Carry the decimal to four places and fill in on line 21. If line 20 is less than line 19, enter 1.0000 21

22 From the income tax return of the other state, fill in the net tax amount after subtracting all nonrefundable and refundable credits (see instructions) 22

23 Multiply line 21 by line 22. Round the result to the nearest dollar. If tax was paid to another state and passed through to you by a tax-option (S) corporation, limited liability company, or partnership, go on to Part III. Otherwise, skip lines 25 through 29 and go on to Part IV. If claiming a credit for net tax paid to Minnesota, Iowa, Illinois, or Michigan, skip lines 30 through 34 and fill in the amount from line 23 on line 35 23



PART III – Calculation of Credit (Shareholders, Partners, and Members)

Caution: See Instructions

		State 1	State 2
24	Postal abbreviation for state to which tax was paid	A I	
25	Income taxable to both Wisconsin and other state (see instructions)	100000.00	.00
26	Total income taxed by the other state (see instructions)	100000.00	.00
27	Divide line 25 by line 26. Carry the decimal to four places and fill in on line 27. If line 26 is less than line 25, enter 1.0000	1 . 0 0 0 0	
28	From the income tax return of the other state, fill in the net tax amount after subtracting all nonrefundable and refundable credits (see instructions)	1000.00	.00
29	Multiply line 27 by line 28. Round the result to the nearest dollar. If claiming a credit for net tax paid to Minnesota, Iowa, Illinois, or Michigan, skip lines 30 through 34 and fill in the amount from line 29 on line 36	1000.00	.00



PART IV - Credit Allowed

30	Income taxable to both Wisconsin and other state (see instructions)	110000.00	.00
31	Wisconsin income from Form 1, line 7, Form 1NPR, line 30, or Form 2, see instructions	110000.00	.00
32	Divide line 30 by line 31. Carry the decimal to four places and fill in on line 32. If line 31 is less than line 30, fill in 1.0000	1 . 0 0 0 0	
33	Fill in the Wisconsin net income tax from: <ul style="list-style-type: none"> • Form 1, line 12, less the amounts on lines 13 through 18 • Form 1NPR, line 46, less the amounts on lines 47 through 49 • Form 2, line 6c, less the amount on line 7 	5454.00	.00
34	Multiply line 32 by line 33. Round the result to the nearest dollar	5454.00	.00
35	Fill in the amount from line 23	4400.00	.00
36	Fill in the amount from line 29	1000.00	.00
37	Add lines 35 and 36	5400.00	.00



38	Fill in the smaller of line 34 or line 37. If claiming a credit for net tax paid to Minnesota, Iowa, Illinois, or Michigan, fill in the amount from line 37	38	5400.00	.00
39	Add the amounts in each column of line 38. Fill in the total here	39		5400.00
40	If you have tax paid to more than 2 states, fill in the amount from line 39 of any additional Schedules OS	40		.00
41	Add lines 39 and 40. This is your credit for tax paid to another state (see instructions)	41		5400.00



Claiming Wisconsin's Credit for Taxes Paid to Another State with the ELT Election

▷ ELT election made in other state only (income excludable for members)

- In general, the individual Wisconsin members of the pass-through entity may claim the credit for the period they were a Wisconsin resident during the tax year (sec. 71.07(7)(b)2., Wis. Stats.)
- Member's credit is based on the member's allocable share of tax paid by the entity on their behalf
- Individuals use Schedule OS, *Credit for Net Tax Paid to Another State*, Parts III and IV to claim the credit



Polling Question 5



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Claiming Wisconsin's Credit for Taxes Paid to Another State with the ELT Election

▷ ELT election made in Wisconsin and in other state

- Only the pass-through entity may claim the credit (sec. 71.07(7)(b)2., Wis. Stats.)
- Entity's credit based on net income or franchise tax paid by the entity to another state on that income and the net income tax on that income paid by the entity on behalf of its shareholders, partners, and members that are residents of this state on a composite return filed with the other state against the net income or franchise tax otherwise payable to this state on income of the same year (sec. 71.07(7)(b)3., Wis. Stats.)
- Use Schedule ET-OS, *Credit for Net Tax Paid to Another State*, to claim the credit



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Resources

- ▷ [Schedule OS and instructions](#)
- ▷ [Pass-Through Entity-Level Tax: Partnership Determining Income and Computing Tax common questions](#)
- ▷ [Pass-Through Entity-Level Tax: Partnership Partner Reporting common questions](#)
- ▷ [Pass-Through Entity-Level Tax: Tax-Option \(S\) Corporation Determining Income and Computing Tax common questions](#)
- ▷ [Pass-Through Entity-Level Tax: Tax-Option \(S\) Corporation Shareholder Reporting common questions](#)



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Contact Us

- ▷ Practitioner email address and phone number
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 - (608) 261-5199



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Presenter

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 - joseph.wasicak@wisconsin.gov



Thanks!
Any questions?



11 a.m. – 12 p.m.

Multistate Taxation of Trusts

Julie Bogle, JD, *Tax Principal, BDO USA LLP*

Mark Shiller, JD, *Attorney, Certus Legal Group Ltd.*

Multistate Taxation of Trusts

**WICPA Tax Conference
November 3, 2023**

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I. Trust Situs Concerns

A. Income Tax

With the variation in state income taxation of trust, trust situs for tax purposes may be very significant – particularly in large trusts.

There are eight states that do not have a trust income tax: Alaska, Florida, New Hampshire, Nevada, South Dakota, Texas, Washington and Wyoming. In 2022, Tennessee phased out its taxation of interest and dividends in non-grantor trusts. Some other states, including Wisconsin, will not tax trusts created by residents of other states that transfer situs to those states.

B. Distribution Matters

Although there may be important distinctions in a state’s definition of trust “income” or of ascertainable standards, etc., perhaps the clearest example of an important state law difference related to distribution matters concerns total return trusts. The absence of total return trusts in a particular state’s statutes may encourage a trustee to seek a different trust situs. Similar considerations may also be present in the power to adjust between principal and income.

C. Investment Matters

Whether the location of a particular investment advisor or fiduciary leads to a move of trust situs, or a trustee simply wishes to be governed by, for instance, the prudent investor rule, investment matters may lead one to take action that impacts trust situs.

D. Asset Protection

Domestic self-settled trusts available in Alabama, Alaska, Colorado,¹ Connecticut, Delaware, Hawaii, Mississippi, Missouri, Nevada, New Hampshire, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Virginia, West Virginia and Wyoming. While a move of a trust to, or decision to create a trust with a situs in, one of such states may, arguably, provide asset protection for an individual, the 2005 changes to the Bankruptcy Code have created a 10-year look back to transfers to such trusts for purposes of determining the exclusion of such transfers from the bankruptcy estate.

In addition, asset protection for beneficiaries may also vary from state to state. This has been highlighted in the adoption of various iterations of the Uniform Trust Code (“UTC”) in a number of states. Perhaps the most controversial provisions of the UTC as promulgated by the Uniform Law Commission relate to the ability of creditors to access a trust beneficiary’s interest for certain obligations including child support, certain government liens, etc. This move from the long-standing rules of many states may make states adopting the UTC less attractive to certain beneficiaries. Wisconsin’s adoption of the UTC in the 2014 version of the Wisconsin Trust Code did not, however, diminish asset protection for trust beneficiaries. Also, there is an effort to consider the introduction of Domestic Asset Protection legislation currently underway in Wisconsin.

E. Perpetuities

Variances in rules relating to the Rule Against Perpetuities or the length of time a trust may continue may clearly be important in dynasty trust planning. Over 20 States have abolished the common law Rule Against Perpetuities, and at least 8 others allow trusts with durations of anywhere from 150 to 1,000 years. Wisconsin is unusual in that it has never had a Rule Against Perpetuities.

F. Fiduciary Matters

Consider, for example, the importance that some fiduciaries may place on the ability to delegate investment responsibility and liability, as under the Uniform Prudent Investor Act. In the minority of states that do not presently have the Act in place, a move may provide some comfort to the trustee.

¹ There are differences of opinion as to whether Colorado truly has a Domestic Asset Protection Trust statute/concept available.

G. Other Factors

- 1. Construction**
- 2. Administrative Efficiency**
- 3. Judicial System**
- 4. Beneficiary Rights**

II. Determination of Situs

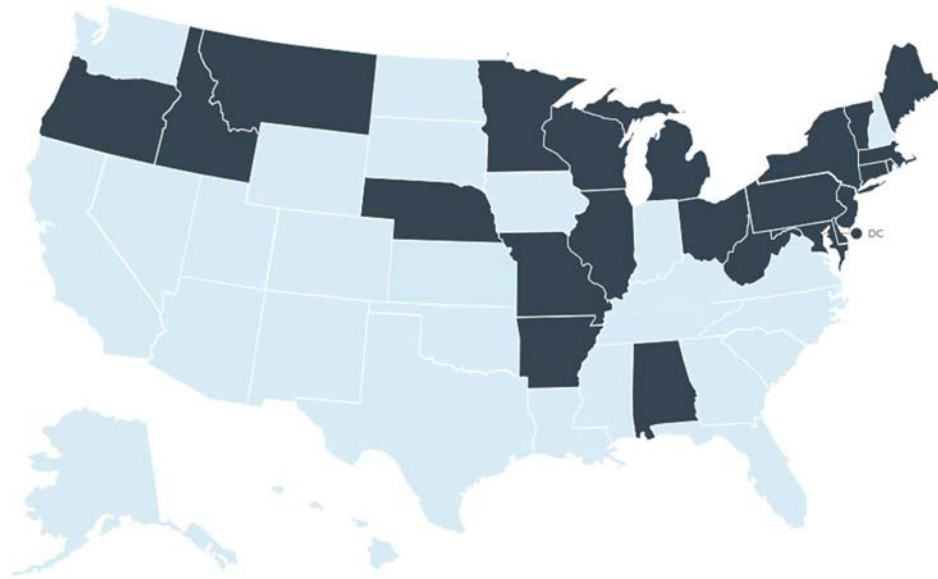
A. Relevant Factors

Although there are a variety of tests, the factors in play are rather common and limited in number. The main factors are:

1. Residence of Trust Creator

Twenty-two states determine tax situs based on the residence of the trust's creator. There are a number of potential arguments suggesting that such determinations are appropriate – however, there are also arguments which would lead to the opposite conclusion. One particular argument is that the nexus of a trust created by a state's resident is connected to the protection of that's state's court system. This is, most commentators appear to concede, relatively persuasive with regard to testamentary trusts. The same spirit of concession may not, however, be as prevalent for *inter vivos* trusts.

- a. Date of Creation**
- b. Date of Funding**
- c. Date Trust Becomes Irrevocable**



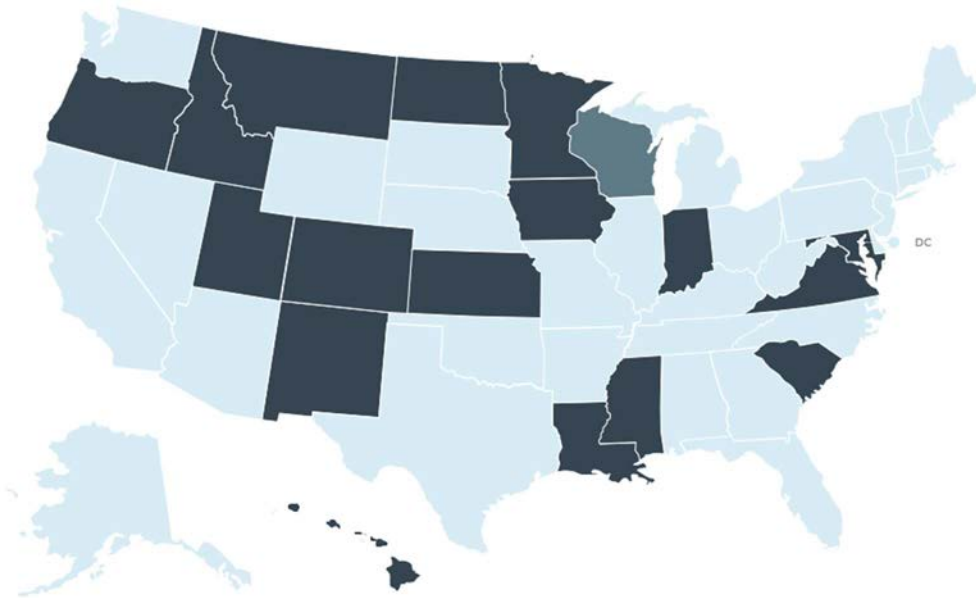
Taxation based on Residence of Settlor²

2. Place of Administration

Pabst v. Wisconsin Dept. of Taxation, 19 Wis.2d 313, 120 N.W.2d 77 (Wis. Sup Ct., 1963) is often cited as standing for the proposition that administration within a particular state is sufficient nexus to tax a trust as a resident trust of such state.

² Wisconsin's rules vary based on when the trust became irrevocable. Trusts which became irrevocable after October 29, 1999 are taxed solely based on the residence of the trust's "fundor." Wis. Stat. §71.14(3m).

Missouri also requires the presence of a resident trustee to impose taxation based on the residence of the trust creator. New York will not impose tax on this base if none of the trustees are resident in New York, all property of the trust is located outside of that state, and all income or gains are attributable to out-of-state sources.



Taxation Based on Place of Administration

Section 108 of the Uniform Trust Code uses the term “Principal Place of Administration” in much the same way as, the author suggests, we think of trust situs. However, it may also be viewed as a blending of traditional notions of trust situs and what constitutes a trust’s place of administration. The Section states:

- (a) Without precluding other means for establishing a sufficient connection with the designated jurisdiction, terms of a trust designating the principal place of administration are valid and controlling if:
 - (1) a trustee’s principal place of business is located in or a trustee is a resident of the designated jurisdiction; or
 - (2) all or part of the administration occurs in the designated jurisdiction.

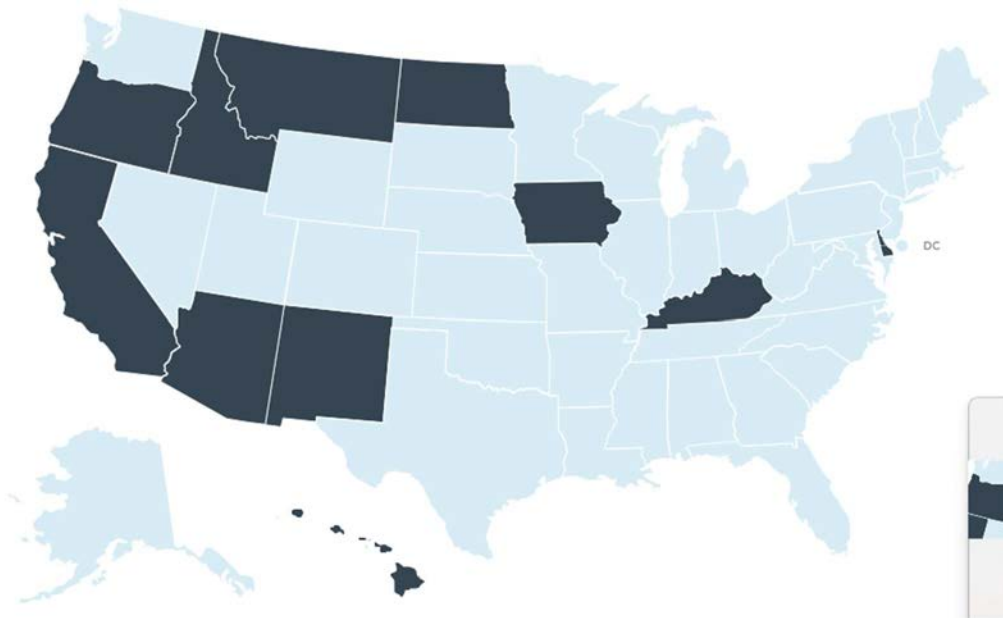
In addition, the trustee is obligated to choose a principal place of administration based on the interests of the beneficiaries. UTC §108(b). This duty was not incorporated into the recent Wisconsin Trust Code changes.

The comments to the UTC state that its rules do not preclude other interpretations, by a settlor’s appointment, rules spelled out in the

governing instrument, etc. Perhaps the structure chosen as a default rule, can best be explained by the uniform law commission's concern with defining trust situs with multiple trustees from various jurisdictions. *See Comments to UTC §108.*

3. Residence of Trustee

Residence of a trustee should also be sufficient nexus for income taxation in the state of residence. *See, e.g., Harvard Trust Co. v. Commissioner of Corps & Taxation*, 284 Mass. 224, 187 N.E. 596 (1933). *See also, State ex. rel. Wisconsin Trust Co. v. Widule*, 164 Wis. 56, 159 N.W. 630 (1916) (although this decision would not have been reached under the current Wis. Stat. §71.14(3m), the case still stands for the proposition that residence of a trustee is sufficient nexus).



Taxation Based on Trustee Residence

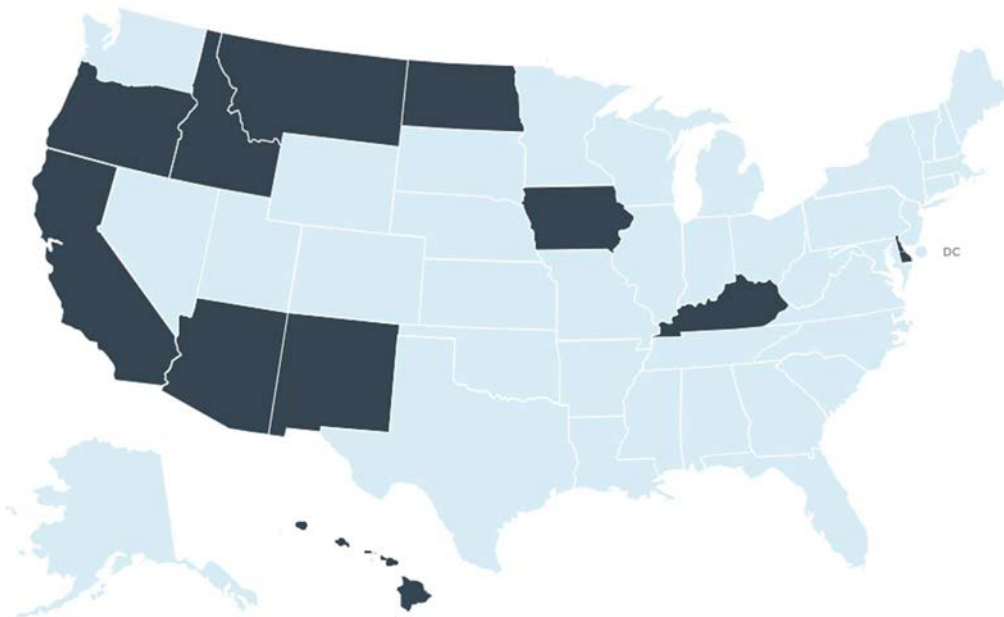
The use of a trust tax system based on trustee residence clearly is an impediment to that state's attraction of trust business.

Note the recent decision in *Bank of America v. Commissioner of Revenue*, 54 N.E.2d 13 (Mass. 2016) which indicates that corporate residence is not necessarily determinative of the

“residence” of a corporate fiduciary. In *Bank of America* the court found that maintenance of over 200 branch offices in the state and the conduct of trust administration activities in the state were sufficient to determine that Bank of America was a resident (or “inhabitant,” to use the language of the decision) of Massachusetts and therefore impose Massachusetts fiduciary income tax.

4. Residence of Beneficiary

Most states do not tax trusts based on the residency of its beneficiaries. However, there are a number that do. The presence of a beneficiary is likely, in the author’s view, a stronger nexus than residence of a grantor of an *inter vivos* trust.



Taxation Based on Residence of a Beneficiary

Taxation of beneficiaries domiciled in a particular state is constitutional -- even if the trust has a different situs and there is no income from property with a situs in that state. *See, e.g., Oklahoma Tax Comm’n v. Chickasaw Nation*, 515 U.S. 450, 462-63 (1965).

5. Situs of Trust Property

Property with a situs in a particular state may properly be subject to tax by such state. *See, e.g., Shaffer v. Carter*, 252 U.S. 37

(1920) (“Just as a state may impose general income taxes upon its own citizens and residents whose persons are subject to its control, it may, as a necessary consequence, levy a duty of like character, and not more onerous in its effect, upon the incomes accruing to nonresidents from their property or business within the state, or their occupations carried on therein, enforcing payment, so far as it can, by the exercise of a just control over persons and their property within its borders.”).

Be careful, though, as the presence of some income from property or assets in a particular state may create tax consequences in that state.

6. Governing Law

Although not commonly considered as a factor for trust situs or tax situs, governing law is a primary factor in Louisiana and a potentially important factor in Idaho regarding tax situs. In addition, governing law can be indicative of residency or a nexus factor. That said, the line between the laws applicable to administration versus meaning and effect is not necessarily as definite as we might think. Consider this chart and allocations of governing law vs. trust situs items from an article/outline entitled *Down the Rabbit Hole and Through the Looking Glass* by Margaret E.W. Sager and Bradley D. Terebelo:

<u>Theoretically the Law of the “State of Origin” or “Pitching” State</u>	<u>Theoretically the Law of the State of the New Situs or “Receiving” State</u>
<u>Validity and Construction</u>	<u>Administration</u>
Capacity of Settlor (validity)	
Effectiveness of Execution (validity)	
Rights of Adoptees (construction)	
Rights of Illegitimates (construction)	
Rule Against Perpetuities (validity)	
Principal versus Income (construction ?)	Principal versus Income (?)
Unitrust/Power to Adjust (construction ?)	Unitrust/Power to Adjust (?)
Per Stirpes / Per Capita (construction)	
Entitlement to Distribution (construction)	
	Qualification of Trustees
	Removal and Replacement of Trustees
	Prudent Investor Act
	Self-Dealing of Fiduciary
Failure of Beneficiaries (i.e., intestacy; escheat) (construction)	
Marital Rights (i.e., election against will; upon divorce) (construction)	
	Rights of Creditors
Beneficiary Notice Requirements (?)	Beneficiary Notice Requirements (?)
Decanting (?)	Decanting (?)
	Virtual Representation
	Delegation of Fiduciary Responsibilities
	Directed Trusts

Here are a few potential additions to the above list:

Plan of Distribution Effectiveness
Choice of Mandatory Provisions
Right to Substitute
Fiduciary vs. Non-Fiduciary nature of powers or offices
within a trust
Modification of Irrevocable Trusts
Trust Protector Authority/Standards
Material Purpose Definition

What other items might be added? How might they be classified?
Which law determines which classification?

- a. Consider Wis. Stat. §701.0105(2) with respect to mandatory rules:

701.0105 Default and mandatory rules.

* * * * *

(2) The terms of a trust prevail over any provision of this chapter except for the following:

- (a) The requirements for creating a trust.
- (b) The duty of a trustee or a directing party to act in good faith and in accordance with the terms and purposes of a trust instrument and the interests of the beneficiaries.
- (c) The requirement that a trust and its terms be for the benefit of its beneficiaries, and that the trust have a purpose that is lawful.
- (d) The power of a court to modify or terminate a trust under ss. 701.0410 to 701.0416.
- (e) The effect of a spendthrift provision and the rights of certain creditors and assignees to reach a trust as provided in ss. 701.0501 to 701.0508.
- (f) The power of the court under s. 701.0702.

(g) The power of the court under s. 701.0708 (2) to adjust a trustee's, directing party's, or trust protector's compensation specified in the terms of the trust.

(h) The effect of an exculpatory term under s. 701.1008.

(i) The rights under ss. 701.1010 to 701.1013 of a person other than a trustee or beneficiary.

(j) Periods of limitation for commencing a judicial proceeding.

(k) The power of the court to take such action and exercise such jurisdiction as may be necessary in the interests of justice.

(L) The jurisdiction of the court and venue for commencing a proceeding as provided in ss. 701.0202, 701.0203, and 701.0204.

(m) The jurisdiction of the court under ss. 701.0807 (4), 701.0808 (9), and 701.0818 (12).

(n) The legal capacity under s. 701.0818 (2) (c) in which a trust protector who is also serving as a trustee or a directing party must exercise any power granted to the trust protector.

Do any of the above raise questions about whether governing law can be changed on a topic? Or whether administrative situs can be shifted on certain issues?

- b.** Can you include a provision in a trust to allow for a change in governing law? Draftspersons have included such provisions in trusts for many years – although it would appear to be a minority that do so. Are they effective? And to what extent?
- c.** If you can change governing law, what impact does that have on a trust's GST exempt status? Is there a gift implication? Who would be the donor or transferor of any negative answer?

- d. Can you change the governing law of a trust that includes the below?

(1) Governing Law. The law of the jurisdiction where the trust is being administered shall govern its administration, but the law of the State of Wisconsin shall be controlling for purposes of determining the validity of the trust and the interpretation of its provisions.

- d. Clients are certainly much more mobile than they used to be. And their moves do raise a host of issues for an estate planner to consider. But what about governing law of a revocable trust? Does a trust created in Wisconsin by a Wisconsin resident become a Minnesota trust at the settlor's death if the settlor moved to Minnesota after the trust's creation? What if amendments are made? What if the trust is restated? What about the exercise of limited powers of appointment granted to beneficiaries?

In addition, there are generation-skipping transfer tax implications to consider if a change in governing law (or trust situs for that matter) results in a lengthening of a GST exempt or grandfathered trust's term. *See*, Treas. Reg. § 26.2601-1(b)(4)(i)(E), ex. 4. Same would be true for the exercise of a limited power of appointment. Treas. Reg. § 26.2601-1(b)(1)(v)(B). Query whether a change of governing law impacts a trust's duration or is that an immutable item at the trust's formation?

Lastly, we should recognize that this topic is likely to garner increased scrutiny with the proliferation of Domestic Asset Protection Trusts. The battle ground that determines what the boundaries of changing governing law might be could very well center on the rights of creditors of trust creators or beneficiaries who seek to establish such trusts or stronger creditor protection in outside jurisdictions.

B. Changing Trust Situs

1. Methods to Change Situs

There are three main ways for trust situs to be changed:

a. Trustee Action

Generally, if authorized in the document or applicable local law, trustee action will be sufficient to alter trust situs. There may be a requirement, however, of notice to beneficiaries, consent by such beneficiaries, or other such limitations on a trustee's ability to change trust situs.

b. Court Proceeding

Resort to the courts is generally available for changing a trust's situs. However, such a change may not alter the trust's tax situs.

c. Change in Circumstances

i. Entity Planning

As referenced above, most states will take certain assets, such as real estate, partnerships, corporations, etc. based on the situs of the property or entity. Some states, however, may have laws that would presume to subject all of a trust subject to tax if, either alone or in conjunction with other factors, the trust contains assets with a physical situs in that state. Moving real estate in that state, for example, into a limited liability company may be enough to avoid taxation based on the property's situs.

ii. Border Crossing

If a trustee or beneficiary moves to another state, they may trigger a change of situs where their residence is the determining factor.

iii. Place of Administration

As referenced above, where a trust's place of administration is can be a tricky question to answer. For example, if a corporate trustee with a presence in one state out-sources (or in-sources) certain administrative or investment functions to an office in another state, where is the place of administration?

iv. Adding Advisors

There are occasions where it makes sense to divide trustee-type responsibilities among various parties and/or retain advisors to handle certain trust tasks. Consider whether the residence of such advisors may make an impact on situs.

d. Decanting

The theory of decanting is relatively simple – a trust may pour-over (decant) to another. The pouring trust ends, while the receiving trust continues (or begins). A number of states, including Wisconsin, have decanting statutes, with the first arising in New York State in 1992. These statutes create a process and conditions for a proper transfer from one trust to another.³

The power to decant may be present under the common law of some states – although the subject has received little treatment in most jurisdictions (at least those without decanting statutes). If the power to decant is not present in the trust instrument, consider whether decanting is advisable or permissible (absent a court's exercise of its equitable powers to modify trusts) due to:

i. Spendthrift Protection

Will spendthrift provisions or ascertainable standards prevent a trustee from distributing assets to another trust (absent specific authority to do so under state law or the governing instrument)?

ii. GST Exempt Status

Treas. Reg. §26.2601-1(b)(4)(i)(D)(1) provides:

A modification of the governing instrument of an exempt trust (including [certain] trustee distribution[s] . . .) by judicial

³ Delaware and Tennessee's decanting statutes differ from New York and Alaska's statutes in that they do not require absolute discretion as a condition to the ability to decant a trust. Rather, they simply require that a trustee have the power to invade trust principal.

reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation . . . than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust.

iii. Rule Against Perpetuities

Is a decant from a trust subject to the Rule Against Perpetuities to one that is not a violation of the Rule itself?

iv. Trust Situs Based on Settlor's Residence

Will a settlor's residence pour with the assets decanted into the new trust?

2. "Unchangeable" Factors

As certain jurisdictions tax trusts based on factors that are set in stone, it may be impossible to alter situs (at least tax situs) in quite a few states. A grantor's domicile is what it is at any point in time (e.g., at death, at funding, at creation, etc.).

a. Constitutionality Questions

Some states, including Wisconsin, purport to require payment of income tax on certain trusts for the duration of the trust. Consider the following:

Wisconsin domiciliary creates and funds a revocable trust. He dies on February 16, 2007 without changing domicile. Upon his death, his trustee is a South Dakota trust company, all aspects of trust administration occur in South Dakota, and all beneficiaries are residents of Nevada. No Wisconsin-situs trust property is present either.

Wis. Stat. §71.14(3m), which is clearly applicable in this hypothetical, reads as follows:

(3m)(a) Subject to par. (b) and except as provided in sub. (2) and s. 71.04 (1) (b) 2., only the following trusts, or portions of trusts, that become irrevocable on or after October 29, 1999, or that became irrevocable before October 29, 1999, and are first administered in this state on or after October 29, 1999, are resident of this state:

1. Trusts, or portions of trusts, the assets of which consist of property placed in the trust by a person who is a resident of this state at the time that the property was placed in the trust if, at the time that the assets were placed in the trust, the trust was irrevocable.
2. Trusts, or portions of trusts, the assets of which consist of property placed in the trust by a person who is a resident of this state at the time that the trust became irrevocable if, at the time that the property was placed in the trust, the trust was revocable.

(b) A trust described under par. (a):

1. Is revocable if the person whose property constitutes the trust may revest title to the property in that person.
2. Is irrevocable if the power to revest title, as described in subd. 1., does not exist.

Contrast the above with Wis. Stat. §71.04(1)(a), a general section on taxability based on situs. It simply states that “All income or loss of resident individuals and resident estates and trusts shall follow the residence of the individual, estate or trust.”

While there is no question of the constitutionality of the choice not to tax non-Wisconsin trusts, the inverse is not as clear. According to the US Supreme Court

[t]he course of decisions does reflect at least consistent adherence to one time-honored concept: that due process requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.

Miller Bros. v. Maryland, 347 U.S. 340, 344-45 (1953). To date, the Supreme Court has not provided any meaningful guidance on what is a “minimum connection” and what is not for state taxation of trusts. And, not surprisingly, the state court decisions are anything but uniform on the subject. See, e.g., *John S. Swift, Jr. Trust v. Dir. of Revenue*, 727 S.W.2d 880 (Sup. Ct. Mo., 1987) (“An income tax is justified only when contemporary benefits and protections are provided the subject property or entity during the relevant taxing period.”) and *Chase Manhattan Bank v. Gavin*, aff’d 249 Conn. 172 (1999), cert. denied 120 S. Ct. 401 (1999) (standing for the proposition that taxation based on the domicile of the grantor at the time his *inter vivos* trust became irrevocable is permissible).

The state of Michigan had a very similar statute to our Wis. Stat. §71.14(3m). However, that statute was declared unconstitutional by a Michigan Court in *Blue v. Michigan Department of Treasury*, Michigan Court of Appeals Decision No. 116666 (Sept. 11, 1990).

The *Blue* case, while interesting to us here in Wisconsin, was decided before *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). This case is often cited as a significant shift in the constitutionality of income taxation of trusts.⁴ *Quill Corp.* dealt with the application of due process concerns and the commerce clause to the constitutionality of assessing and collecting a tax on catalog sales to North Dakota resident by a company with no other North Dakota contacts. Although there are clear differences between catalog sales and trust income taxation, at least one state (well, the District of Columbia) court has held that *Quill Corp.* was a repudiation of the *Swift* line of cases referred to above. *District of Columbia v. Chase Manhattan Bank*, 689 A.2d 539 (D.C. 1997).

⁴ *Safe-Deposit & Trust Co. v. Virginia*, 280 U.S. 83 (1929) was not specifically overruled by *Quill Corp.* However, this case, relied on by various state courts for the proposition that residence of a grantor is insufficient nexus, has not, to the author’s knowledge, been so relied on by a state court since *Quill Corp.* was decided.

What the final answer is regarding constitutionality is still up in the air – although it is worth noting that there has been court activity mostly favorable to taxpayers in federal courts as well as cases in Illinois, Minnesota, New Jersey, North Carolina, and Pennsylvania. The Illinois and Minnesota cases, along with the Michigan history, are interesting to us given the parallels with our current system of taxation of non-grantor trusts. However, we do not have a US Supreme Court or 7th Circuit opinion that would be definitive on these matters in Wisconsin – although the trends seem to be in favor of the taxpayer.

b. Decanting as Potential Solution

If the receiving trust does not have offending characteristic(s), and decanting does not cause or have some of the other issues referenced above, perhaps the problems arising in a decanting trust may be resolved?

3. General Ability Change Trust Situs

While most trusts do (and should) include some reference to the ability to change a trust's situs, generally the law will allow such a change. Scott on Trusts, for example, states:

If it is an inter-vivos trust and the trustee has not become subject to the jurisdiction of any particular court to which he is thereafter accountable, it is not necessary to apply to a court for permission to remove the trust assets to another state and to administer the trust there, unless by the terms by the trust, express or implied, they are not to be removed.

..

[If authority to transfer is unclear, or if the trust is subject to court supervision,] the court will permit a change in the place of administration if this would be in accordance with the intention of the settlor or testator, either express or implied. . . Such a change may be expressly authorized in the Will or trust instrument [for instance, by a provision to that effect, by the appointment of an out-of-state successor fiduciary, or by permitting the appointment of successor fiduciaries without limiting such successors to residents of the original state]. . . Where the intention of the testator is

thus clearly expressed, there is no reason or policy precluding the carrying out of his wishes.

Scott, A. and Fratcher, W., *The Law of Trusts*, 4th Ed., Vol. VA, Sec. 614 at p. 353, 355. Nevertheless, the statutes of the current situs of the trust, and the statutes of the proposed situs, should be consulted before embarking on any such move.

II. Tax Consequences of Situs

A. What Income is Taxed

For those states that do impose income tax on trusts, most will only apply the tax on accumulated income or capital gain if not distributed for tax and/or property law purposes.

Note: Although most states recognize grantor trust treatment in a manner consistent with the federal tax law, that is not the case across the board. *See, e.g.*, La. R.S. 47:187 (Louisiana) and D.C. Code §47-1809.7, - 1809.8 (District of Columbia). As not all states are explicit regarding grantor trust taxation, there may be additional states that may give rise to inconsistent tax treatment for federal and state income tax purposes.

B. Multiple Situs Problem

Although most states will allow for a credit for taxes paid to another, the credit may only apply to tax consequences of property with a situs in that other state. This may lead to constitutional issues that are not fully resolved. Further, there may be a need to determine a priority of credits for trusts subject to taxation in more than one state.

C. Taxation Based on Residence of a Beneficiary

In addition to taxing trusts based on the residency of trustees, California also applies a tax based on the proportion of beneficiaries residing in California. When there are no California trustees, the trust is responsible for payment of income tax attributable to non-contingent beneficiaries. The tax will apply at the time the subject beneficiary receives a distribution from the trust (thus ending his or her non-contingent status as to the distributed amount).

D. 645 Election with Diversity of Estate and Trust Situs

645 Elections with non-resident or non-reporting trusts might be more challenging.

E. Estate Tax Inclusion

The move of trusts with a situs in a decedent's state that utilized a state qualified terminable interest property election might be included in that state at the surviving spouse's death, even if he or she changes residency. For instance, in *Comptroller of the Treasury v. Taylor*, 189 A.3d 799 (Md. Ct. Spec. App. July 25, 2018), the first spouse died domiciled in Michigan and created a trust to which federal and Michigan QTIP elections were made. The surviving spouse then moved to Maryland and died domiciled there.

The Maryland court held that Maryland cannot tax the QTIP trust because no Maryland QTIP election had been made. The court cited Code of Maryland-Tax-General §7-309(b)(6)(i) (emphasis added): "For purposes of calculating Maryland estate tax, a decedent shall be deemed to have had a qualifying income interest for life under §2044(a) of the Internal Revenue Code with regard to any property for which a marital deduction qualified terminable interest property election was made for the decedent's predeceased spouse on a timely filed Maryland estate tax return."

F. Homeless/Orphan Trusts

An interesting consequence of the crazy-quilt of trust situs determination is the not insubstantial probability of having trusts that have no state filing requirements – something that is very much the case for many states that are administered in Wisconsin but funded by out-of-state donors. In that case, there may be discomfort with the lack of filing and therefore a desire to find a state home.

This is particular of concern in circumstances where the nexus between a state seems tenuous or no longer in existence. Some practitioners choose to ignore state requirements entirely, while others are more likely to tow the line despite how tenuous the connections might otherwise be.

III. Property Law Consequences of Situs

A. Distribution Matters

B. Investment Matters

- C. **Asset Protection**
 - D. **Perpetuities**
 - E. **Construction**
 - F. **Fiduciary Matters**
 - G. **Administrative Efficiency**
 - H. **Judicial System**
 - I. **Beneficiary Rights**
- IV. **Drafting and Planning Considerations**

A. Trustee Appointments

Fiduciary appointments are often made based on the skills, abilities and other attributes of a particular person or institution. However, such person or institution may carry certain “situs baggage” that may suggest he, she or it is not the ideal choice from a tax perspective. Reviewing the options, and the consequences of particular choices, with a client is worthwhile. In Wisconsin, however, the utility of this exercise is premised on the notion that Wis. Stat. §71.14(3m) is unconstitutional.⁵

B. Change of Residence of Client

If a client intends to enter a state (like Wisconsin) that taxes trusts based on the residence of a grantor from a state that does not, the client may consider creating an irrevocable (for property law purposes, but not for income or estate and gift tax purposes) trust to hold his or her property prior to assuming the new residence.

C. Discretionary vs. Mandatory Distribution Standards

As some states tax based on the residence of a trust’s beneficiaries, the definition of who is a beneficiary and who is not becomes important. It may be preferable to create discretionary distribution standards to minimize the impact of a state’s trust income tax. In some states, including California, a non-vested interest will not cause a trust to be subject to that state’s trust income tax.

⁵ Note that Wis. Stat. §71.14(3m) is not driven by the residence of the grantor so much as it is driven by the residence of the “fundor” or a trust.

D. Include Decanting Language in a Trust

When a state taxes trusts based on the residence of a grantor, a decanting statute may provide an option to avoid the offending state's taxation of the trust. In the alternative, significant distribution powers may be given to a trustee or significant powers of appointment may be given to an independent party or a beneficiary with a view towards avoiding resident trust status based on the grantor's residence.

E. Divide and Conquer

If there is concern about the taxation of a trust based on the situs of certain property or the beneficiaries, consider whether the segregation of the offending property or beneficial interests will provide a tax savings or other advantages. Consider the application of Missouri's statute, which will provide for taxation of a trust if just one of many beneficiaries is a resident of that state. *See*, Mo. Rev. Stat. §143.331 (a resident trust includes a trust that has "at least one income beneficiary who, on the last day of the taxable year, was a resident of [Missouri].").

F. Duty to Change Situs

Commentary on issues of trust situs has included reference to a possible duty to remove a trust to a more efficient situs. In fact, as referenced above, the Uniform Trust Code includes such a duty. *See*, Uniform Trust Code §108(b) (a trustee must administer the trust "at a place appropriate to its purposes, its administration, and the interests of the beneficiaries."). Should such a duty be waived? or stated explicitly in the trust document?

Note that Wis. Stat. §701.0108(3) provides "a trustee may, but has no affirmative duty to, transfer a trust's principal place of administration to another state or to a jurisdiction outside of the United States."

G. Change of Governing Law if Change of Situs

Generally, the choice of governing law and trust situs need not go hand-in-hand. The author suggests specific reference to the fact that such matters may be handled independent of one another.

H. Take Advantage of Foreign Trust Advantages

While there may be disadvantages to having trusts taxed as foreign trusts during a trust grantor's lifetime, the classification may have certain advantages if trust accumulation is desirable.

The tax definition of US and foreign trusts were changed in 1996. In short, in order to be considered a US trust, a trust must meet two tests:

1. Court Test

The trust must be subject to primary supervision over its administration by a US court.

2. Control Test

Only US fiduciary or fiduciaries have the power to control all substantial decisions of the trust. Substantial decisions would include:

- a. Timing and amount of distributions;
- b. Selection of beneficiaries;
- c. Allocation between principal and income;
- d. The power to terminate the trust (or the power to block such termination).
- e. Power to compromise, arbitrate, or abandon claims of the trust and to decide whether to sue on behalf of or defend suits against the trust;
- f. Power to remove, add or replace a trustee;
- g. Power to appoint successor trustees (as long as not limited by aspects of changing the trust's situs);
- h. Power to make investment decisions.

See, I.R.C. §7701(a)(30); Treas. Reg. §301.7701-7(d)(1)(ii).

Upon death, a foreign non-grantor trust may prove advantageous. For US income tax purpose, a foreign trust invested in appropriately sourced income, US income taxes may be deferred. These advantages must be considered with the potential penalties that may apply upon distribution to US beneficiaries. *See*, I.R.C. §663(a)(1).

11 a.m. – 12 p.m.

The Employee Retention Credit: Navigating Areas of Ambiguity

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The Employee Retention Credit: Navigating Areas of Ambiguity

William Wong, Bee Yang, Christopher Dowse

Lesson Objective(s)

- (1) Analyze issues in determining ERC eligibility.
- (2) Apply IRS guidance to the ERC eligibility analysis.
- (3) Recognize areas of ERC where guidance is lacking.

Agenda

I. Background

- i. How we got here
- ii. ERC Engagement Process
- iii. Aggregation, FTE, and Other General Considerations.

II. ERC Eligibility

- i. Gross Receipts Test
- ii. Suspension Test
 - a. Government Orders
 - b. Full Suspension
 - c. Partial Suspension
 - I. Modifications
 - II. Nominal Effect
 - III. Supplier Exception

III. Moving Forward

- i. IRS Moratorium
- ii. Reaching a Supportable Position
- iii. Professional Responsibility

I. Background

- i. How we got here
- ii. ERC Engagement Process
- iii. Aggregation, FTE, and Other General Considerations

What is the Employee Retention Credit (ERC)?

- Fully refundable quarterly *payroll tax* credit.
- Available to eligible employers under either:
 - *Gross Receipts Eligibility Test*
 - *Suspension Eligibility Test*
 - *Recovery Start-up Business*
- ERC is calculated as a percentage of *qualified wages*.

Law and History of ERC - 2020

- § 2301 - CARES Act- signed into law March 27, 2020
 - First introduced the Employee Retention Credit.
 - All employers who carry on a trade or business and pay wages to employees between Mar. 13, 2020, and Dec. 31, 2020, are eligible if they meet one of the requirement tests:
 - (1) The employer was under a governmental order to shut-down operations due to COVID-19; *or*
 - (2) The employer experienced a significant decline in gross receipts during that cover period.
 - Provided a credit of 50% of up to \$10,000 of wages and qualified medical expenses paid to employees between Mar. 13, 2020, and Dec. 31, 2020.
 - Maximum credit amount that may be claimed for each employee for all four calendar quarters in 2020 is \$5,000.
 - As originally enacted, prohibited PPP loan recipients from also taking ERC

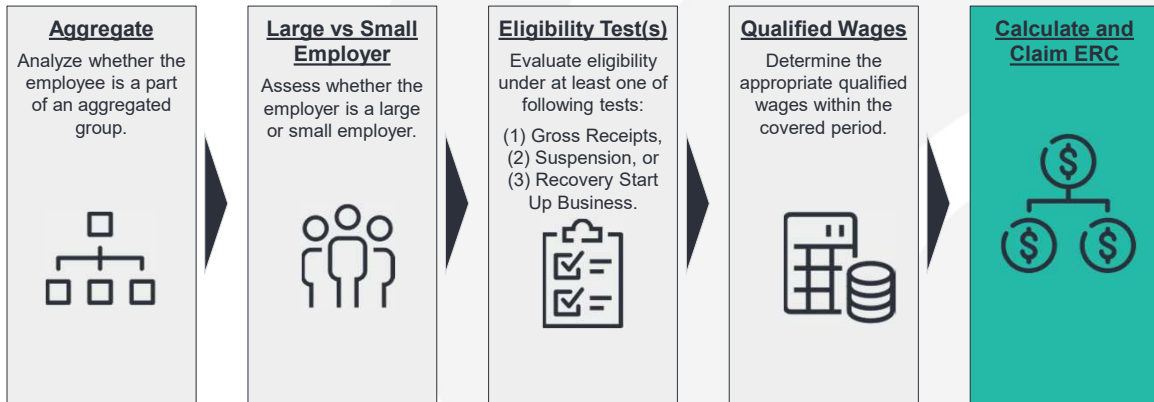
Law and History of ERC - 2021

- Consolidated Appropriations Act (CAA)-signed into law Dec 27, 2020
 - Extended ERC through June 30, 2021.
 - Percentage of available credit for qualified wages in 2021 = 70% of \$10,000
 - Max ERC = \$7,000 per employee per quarter
 - Retroactively provides that recipients of PPP loans are eligible to claim ERC for 2020 and 2021.
 - Large employer threshold increased to 500 from 100.
- § 3134 - American Rescue Plan Act (ARPA)-signed into law March 11, 2021
 - Extended ERC through Dec. 31, 2021.
 - Introduced Recovery Start-Up Businesses.
 - Extended the IRS audit period to 5 years.
 - Applies to 2021 Q3 and Q4.
- Infrastructure Investment and Jobs Act (IIJA)-signed into law November 15, 2021
 - Eliminated the Q4 2021 ERC for all non-Recovery Start-Up Businesses.

IRS Guidance

- IRS Notice 2021-20 (3/1/2021)
 - Applies to credit claimed After March 12, 2020, and before January 1, 2021.
 - Provides guidance for those who are claiming the credit for the tax year 2020 only.
- IRS Notice 2021-23 (4/2/2021)
 - Provides guidance for those claiming ERC in first and second quarter of 2021.
- IRS Notice 2021-49 (8/23/2021)
 - Clarifies rules regarding recovery start up businesses ERC eligibility.
 - Provides guidance for those claiming ERC in the third quarter of 2021.
- IR-2023-105 (5/25/2023)
 - Outlines red flags for ERC claims and warning signs of aggressive ERC marketing
- AM 2023-005 (7/21/2023)
 - IRS Office of Chief Counsel General Advice Legal Memorandum offering insight into eligibility positions for employers with suspended suppliers of critical goods.
- IR-2023-169 (9/14/2023)
 - Updated IRS Question and Answers related to ERC, along with FAQs.

General ERC Engagement Process



Aggregation & FTE

- **Aggregation**
 - Businesses that treated as a single employer under § 52(a) or (b) or subsection (m) or (o) of § 414 must be aggregated for ERC purposes
 - § 52(a) “Controlled Group” or § 52(b) “Common Control”
 - Parent-Subsidiary Group – More than 50% ownership, vote or value
 - Brother-Sister Group – 5 or fewer common owners having both a *controlling interest* (80% or more, vote or value) and *effective control* (more than 50%, vote or value)
 - Combined Group – A combination of both Parent-Subsidiary Group and Brother-Sister Group (minimum three organizations).
 - § 414(m) and (o) apply to affiliated service groups
 - *Impacts:* Eligibility Testing, Large Employer vs Small Employer Assessment, and Apportionment of Credit
- **Large Employer vs Small Employer**
 - Limits the qualified wages an employer may use to claim ERC
 - Based on the number of *full-time employees* in calendar year 2019
 - *Full-Time Employee:* Employee that worked at least 30 hours per week or 130 hours in a month
 - Calculated in accordance with § 4980H
 - Large Employer: may *only* use wages paid to employees for services not rendered to calculate ERC
 - 2020 – Greater than 100 Full-Time Employees
 - 2021 – Greater than 500 Full-Time Employees
 - Small Employer: may use *all* otherwise qualified wages (services performed or not)
 - 2020 – 100 or fewer Full-Time Employees
 - 2021 – 500 or fewer Full-Time Employees

General Considerations

- **Credit Amount**
 - 2020 – Credit of 50% of up to \$10,000 of qualified wages per employee for all quarters
 - Maximum credit per employee = \$5,000
 - 2021 – Credit of 70% of up to \$10,000 of qualified wages per employee for each quarter (Q1, Q2, and Q3)
 - Maximum credit per employee = \$21,000
- **Qualified Wages**
 - **Included:**
 - Gross Wages paid in eligible period
 - FICA wages (except non-qualified pre-tax items)
 - Employee pre-tax healthcare costs and employer paid health insurance
 - **Not included:**
 - Wages paid to over 50% owner(s) or “related” employees.
 - PPP Forgiveness Wages
 - FFCRA, FMLA, and other specified credits
 - Large Employer limitation
- **Recovery Start Up Businesses**
 - Potential eligibility for employers that began carrying on a trade or business *after* February 15, 2020
 - Cannot not exceed \$1,000,000 average annual gross receipts for the three taxable-year period ending with the taxable year which precedes the calendar quarter for which the credit is determined
 - Aggregation rules still apply
 - Considerations for employers that began carrying on a new trade or business in 2021
 - Eligibility for ERC in 2021 Q3 and Q4
 - Capped at \$50,000 for each quarter
- **Amending Businesses Tax Return**
 - Taxpayers should file an amended federal income tax return or administrative adjustment request (AAR), if applicable, for the taxable year in which the qualified wages used to claim the ERC were paid/incurred.
 - This is done to correct any overstated deduction taken with respect to those same wages on the original federal income tax return.
 - (See, IRS Notice 2021-49 pg. 24-25.)



Gross Receipts Test

ERC Eligibility

- i. Gross Receipts Test
- ii. Suspension Test
 - a. Government Orders
 - b. Full Suspension
 - c. Partial Suspension
 - I. Modifications
 - II. Nominal Effect
 - III. Supplier Exception

Gross Receipts Eligibility Test

- **Significant Decline**

- 2020:
 - Greater than **50%** decline in gross receipts for a calendar quarter in 2020, when compared to same quarter in 2019
 - For 2020, eligibility ends in the calendar quarter *after* the calendar quarter in which the employer's gross receipts are more than 80% of the same calendar quarter in 2019.
- 2021:
 - Greater than **20%** decline in gross receipts for a calendar quarter in 2021, when compared to same quarter in 2019
 - **Preceding Quarter Election:**
 - For 2021, an employer may elect to determine gross receipts eligibility for a calendar quarter by comparing the immediately preceding calendar quarter with those of the corresponding calendar quarter in 2019

Ex. 2021 - Preceding Quarter Election

	2019 Gross Receipts	2020 Gross Receipts	Decline %
Q4	\$100,000	\$33,000	-67%
	2019 Gross Receipts	2021 Gross Receipts	Decline %
Q1	\$100,000	\$90,000	-10%
Q2	\$100,000	\$33,000	-67%

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Gross Receipts Eligibility Test

- **Gross Receipts**
 - Defined as gross receipts of the taxable year in which such receipts were properly recognized under the taxpayer's accounting method used in the taxable year for federal income tax purposes
 - Generally determined under IRC § 448(c), referencing Reg. § 1.448-1T(f)(2)(iv)
 - Tax-Exempt Organizations – Gross Receipts defined in IRC § 6033
- **Gross Receipts include:**
 - Total Sales (net of returns and allowances)
 - All amounts received for services
 - Any income from investments and incidental/outside sources
 - Ex. interest, dividends, rents, royalties, and annuities. (regardless of whether such amounts are derived in the ordinary course of the employer's trade or business.
- **Not** reduced by the cost of goods sold, or by the cost of property sold—if such property is described in IRC § 1221 or § 1221(2)
 - However, gross receipts *must* be reduced by the employer's adjusted basis in such property
- **Gross receipts do not include:**
 - Repayment of a loan or similar instrument
 - Forgiven PPP loans, Shuttered Venue Operator Grants, Restaurant Revitalization Grants (Rev. Proc. 2021-33)
 - Amounts received by the employer with respect to sales tax or other similar state and local taxes if, under the applicable state or local law, the tax is legally imposed on the purchaser of the good or service, and the taxpayer merely collects and remits to the taxing authority
 - Please note that, gross receipts *must* include the amounts received that are allocable to the payment of such tax if, the tax is imposed on the taxpayer.
- **Acquired Entities**
 - An employer may include the 2019 gross receipts of a business it acquired in 2020 or 2021 to the extent the information is available.¹⁴
 - See, IRS Notice 2021-20 Answer 28.

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Suspension Eligibility Test

- An employer is eligible for ERC under the suspension eligibility test if:
 - 1) The employer’s operations were either (a) *fully*, or (b) *partially*, suspended during a calendar quarter in 2020 or 2021,
 - 2) Due to *orders* from an appropriate government authority limiting commerce, travel, or group meetings due to COVID-19, and
 - 3) The employer was impacted *more than nominally* by the suspension or could not continue comparable operations via telework.



Government Orders & Preliminary Considerations

- **Government Orders**
 - “Orders, proclamations, or decrees from the Federal government or any State or local government”
 - Statements from governmental officials are *insufficient*
 - Government orders that encourage—but do not mandate—employers to take certain actions are *insufficient* for eligibility
 - *Must* limit either: Commerce, Travel, or Group meetings (for commercial, social, religious, or other purposes), *due to COVID-19*
 - Government orders not from the Federal Government, must be from a State or local government that has *jurisdiction* over the employer’s operations
 - Orders must *directly* relate to the employer’s *suspension* of operations
 - CDC and OSHA guidance alone are not valid government orders
- **Preliminary Considerations**
 - Aggregated group:
 - If a trade or business is operated by multiple members of an aggregated group, the suspension of one member may make all members eligible under the suspension test
 - See, Notice 2021-20 Answer #21
 - Employer’s operating in multiple jurisdictions:
 - *May* be suspended if “some but not all” jurisdictions have government orders mandating suspension



Suspension Eligibility Period & Full Suspension

- **Eligibility Period**

- The employer would be *eligible* for the entire calendar quarter that their business operations were suspended.
- However, only wages paid with respect to the period the valid government order suspended the employer's business operations may be used to determine the ERC.
 - See, IRS FAQ, referencing IRS Notice 2021-20 Answer #22, where an employer was suspended by a government order that mandated closure of non-essential businesses from March 10 through April 30 of 2020. The employer was *eligible* for ERC in 2020 Q1 and Q2, but could only claim the credit for qualified wages paid from March 13, 2020 (effective date of § 2301 of the CARES Act) through April 30, 2020 (the final effective date of the government order mandate for non-essential businesses to close)

- **“Full suspension”**

- A complete shutdown of an employer's business operations due to a valid government order

- **Closure of a *portion* of business operations**

- Suspension may also be met if the employer has a *more than nominal portion* of their business operations completely shutdown due to a valid government order
- Portion of an employer's business operations will be “*more than nominal*” if either:
 - A. Gross Receipts from that *portion of the business* operations account for 10% or more of the *total gross receipts* in the same calendar quarter in 2019, or
 - B. Hours of employee service in that *portion of the business* operations accounts for 10% or more of the *total number of hours of service* performed by all employees in the business in the same calendar quarter of 2019



Partial Suspension & Modifications

- **“Partial Suspension”**

- Employer's business operations remained open but were subject to modifications due to valid government orders.
 - *Examples of modifications: “Those required by a governmental order as a condition of reopening a physical space for business”*
 - Ex. Limiting occupancy, changes to the format of an employer's service, etc.

- **Modifications**

- The existence of modifications alone is not enough to satisfy eligibility
- Modifications must result in a more than nominal effect on the business
- Modifications to customer behavior—such as mask requirements or limiting direction of store aisles—or requiring employees to wear masks and gloves will “not result in more than a nominal effect on the business”
- Declines in customer demand
 - Suspension of business operations due to declines in customer demand are also *insufficient*

- **“More than a nominal effect”**

- A modification will result in a *more than nominal effect* if there is a 10% or more reduction in an employer's ability to provide goods or services in its normal course of business



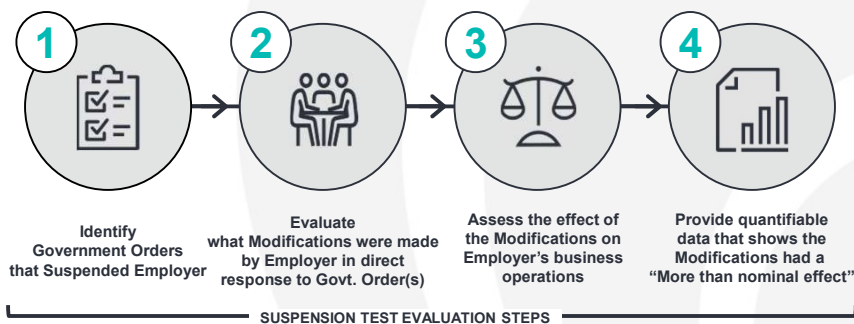
Suspension Test – Partial Suspension

• Quantifying a “More than a nominal effect”

- Scant Guidance provided
- Facts and Circumstances determination
- Examples from IRS Notice 2021-20 on “more than a nominal effect”:
 - Restaurant allowed to continue indoor dining service, but tables must be spaced out at least six feet apart, causing a spacing constraint on the restaurant.
 - “Based on the facts and circumstances” the Government Order restricting the restaurant’s indoor dining service *would have* more than a nominal effect on the restaurant’s operations.
 - Large retailer must enforce social distancing and occupancy requirements, but due to size of stores, these modifications only result in customers waiting in line for a short period to enter the store during busy times of the week.
 - “Based on the facts and circumstances” the Government Order enforcing social distancing guidelines *would not have* a more than nominal effect on the retailer’s operations.

Suspension Test – Partial Suspension

Evaluation Process for Partial Suspension Test



Suspended Supplier Exception

- **Partial Suspension Eligibility Test – Suspended Supplier Exception**

- An employer may be eligible for ERC, if their “supplier of critical goods or materials” is subject to a COVID-19 related government ordered shutdown or modification.
- IRS Notice 2021-20 Answer #12 Example:
 - An auto parts manufacturing business’ supplier of raw materials is required to “fully suspend” its operations pursuant to a government order.
 - The manufacturer is unable to obtain these materials from an alternate supplier, and as a result, *“is not able to perform its operations for a period of time.”*
 - Under these facts and circumstances, the manufacturer is considered eligible for the ERC under the suspension test.

- **IRS General Legal Advice Memorandum (“GLAM”) – 7/21/2023**

- The GLAM provides five scenarios in which employers deal with varying forms of supply chain issues.
 - Only one of the five scenarios results in employer eligibility for the ERC.
 - (In that scenario the employer was also directly subject to a government order)
- General Guidance from Five Scenarios:
 - Employer’s must demonstrate that delays of critical goods was directly caused by their supplier being suspended as a direct result of a governmental order.
 - An employer that can continue its operations despite its supplier’s suspension is not eligible under the suspension test.
 - “[The] relevant inquiry is whether Employer A’s trade or business operations could continue[.]”
 - Employers must demonstrate that delays or bottlenecks at a domestic shipping port are directly caused by a governmental order, and that their supplier was suspended as a result of that order.
 - An Employer’s eligibility ends upon the lifting of the government order, regardless of the significant residual issues the employer experiences.
 - Employer are ineligible if they could obtain critical goods from an alternate supplier and thus continue operations, regardless of the fact they acquired the goods at a significantly higher cost.

Moving Forward

- i. IRS Moratorium
- ii. Reaching a Supportable Position
- iii. Professional Responsibility

Moratorium - Temporary ERC Processing

- **Temporary Stop**
 - On September 14, 2023, the IRS placed a temporary stop on the *processing of new* ERC claims through “at least the end of the 2023 calendar year.”
 - The IRS is taking this time to work with the justice department “to address fraud in the ERC program[.]”
- **Processing Backlog**
 - IRS currently has a back log of over 600,000 ERC claims that *it will continue to process*.
 - Processing “goal” has been increased from 90 to 180 days.
- **New Programs for Taxpayers**
 - **(1) Withdrawal Option for ERC unprocessed claims:** Taxpayer may choose this option even if ERC claim is under or awaiting audit.
 - **(2) ERC settlement program:** Will allow employers to repay ERCs received to avoid penalties and future compliance action.
 - These programs do *not* protect taxpayer against prosecution for willfully submitted fraudulent claims
 - Details for these programs remain outstanding
- **Statute of Limitations**
 - The moratorium does not pause the statute of limitations for claiming ERC.
 - Taxpayers must claim the ERC by:
 - **2020** – April 15, 2024 **2021** – April 15, 2025
 - At this time, the statute of limitations for IRS assessments on ERC claims are:
 - **2020** – Three (3) years after the latter of – the date on which the original return which includes the calendar quarter with respect to which such credit is determined is filed, or the date on which such return is treated as filed under § 6501(b)(2).
 - **2021 Q1, Q2** – Three (3) years after the latter of – the date on which the original return which includes the calendar quarter with respect to which such credit is determined is filed, or the date on which such return is treated as filed under § 6501(b)(2).
 - **2021 Q3, Q4** – Five (5) years after the latter of – the date on which the original return which includes the calendar quarter with respect to which such credit is determined is filed, or the date on which such return is treated as filed under § 6501(b)(2).



ERC in the Future

- **Aspects of ERC lacking IRS Guidance:**
 - Suspension Test
 - Quantifying “more than a nominal effect”
 - Mergers and Acquisitions
 - Aggregation
 - Private Equity
- **IRS Remains Focused on Auditing ERC**
 - Compliance Audits of ERC claims continue to be a focus for the IRS.
 - “The further we get from the pandemic, the further we see the good intentions of this important program abused.” – Danny Werfel, IRS Commissioner



Reaching a Supportable Position

- **Assess all Facts and Circumstances of the Employer**
 - Make all relevant inquiries
 - Inform client of potentially aggressive positions and penalties
- **Follow engagement process steps**
 - Ensure all areas of ERC are addressed. (e.g., Aggregation, FTE, Eligibility, Qualified Wages.)
- **Review data and base analysis on the IRS Hierarchy of Authority**
 - **Will:** Generally, 90% or greater probability success on the merits
 - **Should:** Generally, 70% to 90% likelihood of success on the merits
 - **More Likely Than Not:** Greater than 50% likelihood of success on the merits
 - **Substantial Authority:** Weight of authorities in support of a position is substantial. Generally, 40% to 50% likelihood of success on the merits
 - **Reasonable Basis:** 33% to 40% of likelihood of success on the merits
 - **Not Frivolous:** Some merit to position 10% to 33% of likelihood of success on the merits
 - **Frivolous:** Below 10% chance of success



IRS Audit Experience

- **Auditors want to know:**
 - Why the taxpayer is eligible
 - How did the taxpayer learn about the credit
 - Who did the eligibility testing
 - If a promotor:
 - What was the taxpayer promised
 - How did the learn about the promotor
 - Was there a contingency fee
 - How the calculations were done
 - What prohibited funds (e.g., PPP loans) could have been used to pay wages
- **Expansive Information Document Request (IDR)**
 - Field auditors have little information at their disposal when assigned to review an ERC since they credit is filed using an amended Form 941 with no substantiation
 - Often subsequent IDRs



Professional Responsibility

- **Issue Number: 2023-02**

- IRS Office of Professional Responsibility (OPR) issued guidance for tax professionals “to ensure they are meeting their Circular 230 professional responsibilities and the standards required to prepare and sign original tax returns, amended returns, or claims for refund relating to [ERC claims].”
- **Diligence as to Accuracy**
 - “If the practitioner cannot *reasonably* conclude (consistent with the standards discussed in this guidance) that the client is or was eligible to claim the ERC, then the practitioner should not prepare an original or amended return that claims or perpetuates a potentially improper credit.”
- **Standards for Tax Returns and other documents**
 - Prohibited from advising a client to take a position that lacks reasonable basis
 - “As a best practice, the practitioner should consider advising the client of the option of filing an amended return.”
- **Written Advice**
 - Practitioners advising clients may rely on the advice of others only if the reliance is reasonable under all the facts and circumstances.
 - *Example:* A practitioner’s reliance on another adviser, who may have advised the client to claim ERC and has a conflict because of the amount or character of the fee the adviser charged for the advice at the time, may not be reasonable.



Questions?

Stay in touch

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1 – 2 p.m.

How to Recognize & Correct Code 409A Failures

Martin P. Tierney, JD, *Partner, Michael Best & Friedrich LLP*



How to Recognize and Correct Code Section 409A Failures



Martin Tierney
November 3, 2023



Code Section 409A Basics

Code section 409A imposes certain requirements upon any deferred compensation arrangement between a service provider and a service recipient.

- Must be in writing
 - Must comply with 409A's requirements in writing and in operation
- Basic 409A Requirements:
 - Payment Timing
 - Death
 - Disability
 - Change in Control
 - Separation from Service
 - Unforeseeable emergency
 - Fixed date
 - No acceleration of payment
 - Deferral elections must meet strict timing rules



Cost of a 409A Failure

- The tax penalties for failure to meet the requirements of Section 409A are severe and are imposed on the service provider (employee or consultant), not the service recipient (employer)
- Compensation under the non-compliant arrangement (and any similar arrangements that must be aggregated with it) is included in income when it vests.
- A 20% penalty tax is imposed on the amount involved.
- An increased interest rate is imposed on the late payment of the income tax due on the compensation.



What is deferred compensation subject to Code section 409A?

- Deferred compensation is very broadly defined as any form of compensation which is or may be paid in a year following the year in which the legal right to the payment arises. The critical concept is that the service provider has a legally binding right to a payment in a year following the year in which the services are provided.
- Compensation can be considered deferred compensation as soon as the legal right to compensation arises, even if that right is not vested (that is, the right to compensation is subject to the performance of future services or to a future event).
- For example, the legal right to severance arises when the agreement is signed and becomes effective, but the severance may be paid in a later year, if at all.
- BUT the real action is in the exceptions...



What is deferred compensation subject to Code section 409A?

Short Term Deferral Exception

- Payments made within a short time frame following the end of the year in which the compensation is no longer subject to a substantial risk of forfeiture (SROF) are not considered deferred compensation and therefore are not subject to Section 409A.
- In the calendar year context, this short-term deferral exception applies to compensation paid not later than March 15 of the year following the year in which the employee's right to the compensation is no longer subject to a SROF.
- Cannot have other contingent events (e.g., paid upon completion of audit).

SROF is very specifically defined in the regulations.

- A SROF exists if an employee's entitlement to an amount is conditioned on either:
 - The performance of substantial future services.
 - The occurrence of a condition related to a purpose of the compensation which relates to:
 - the employee's performance; or
 - the employer's business activities or organizational goals (for example, the attainment of a certain level of earnings).
- The possibility of forfeiture must be substantial, as determined based on the facts and circumstances.
- Involuntary termination and good reason can be SROF, non-compete cannot.



What is deferred compensation subject to Code section 409A?

Severance Pay Exception

- Certain severance payments are treated as exempt from Section 409A if the severance pay meets the following requirements:
 1. It is payable only on an involuntary termination.
 2. It is paid by December 31 of the second year after the year in which the termination occurs.

3. The amount does not exceed two times the lesser of:
 - (i) the employee's annual compensation for the year before termination of employment (or in the case of an employee whose employment begins and ends in the same taxable year, the employee's annualized compensation for the year of termination of employment) or
 - (ii) the IRS limit on compensation under a qualified pension plan for the year of termination of employment (\$330,000 for 2023).



Plan Document Failure vs. Operational Failures

- Two types of 409A compliance failures
- Written plan document is required
- Plan document failure
 - Failure of plan to comply with 409A's requirements
 - Applies to all participants in the plan
 - But plan aggregation rules do not apply, so the negative tax impacts of 409A are limited to the amounts deferred under the plan.
 - What is the "plan"?
- Operational Failure
 - Failure to follow the terms of the plan or code section 409A
 - Applies only to the participant with respect to which error was made
 - All such participant's nonqualified deferred compensation in the same category is aggregated (for these purposes, there are nine different categories of deferred compensation)



409A Failures Apply to Each Tax Year Independently

- Proposed Regulations for Calculating the 409A Tax, if incurred
 - Extremely complicated
 - Critical concept: A failure to meet the requirements of section 409A during one taxable year generally would not affect the taxation of amounts deferred under the plan for a subsequent taxable year during which the plan complies with section 409A in form and in operation with respect to all amounts deferred under the plan.
- Each taxable year is analyzed independently to determine if there was a failure.
- As a result, assessment of tax liabilities due to a plan's failure to comply with the requirements of section 409A in a closed year would be time-barred.
- But, if there is a failure to include amounts in income in an earlier year as a result of the assessment becoming time-barred, then the taxpayer's duty of consistency would prevent the service provider from claiming a tax benefit in a later year with respect to such amount (such as, for example, by claiming any type of "basis" or "investment in the contract" when the amount is paid in a future year).



Common Code section 409A Errors: Separation from Service

- Termination of employment is "...based on whether the facts and circumstances indicate that the employer and employee reasonably anticipated that no further services would be performed after a certain date or that the level of bona fide services the employee would perform after such date (whether as an employee or as an independent contractor) would permanently decrease to no more than 20 percent of the average level of bona fide services performed (whether as an employee or an independent contractor) over the immediately preceding 36-month period (or the full period of services to the employer if the employee has been providing services to the employer less than 36 months)."
- Separation from Service is very explicitly defined in the regulations and includes termination of employment
- Separate rules apply for independent contractors (expiration of contract – good faith and complete termination of the contractual relationship)
- BUT changing to an independent contractor does not result in a Separation from Service unless it would result in a termination of employment using the termination of employment rules.



Common Code section 409A Errors: Substitutions

- "...the payment of an amount as a substitute for a payment of deferred compensation will be treated as a payment of the deferred compensation. A forfeiture or voluntary relinquishment of an amount of deferred compensation will not be treated as a payment of the compensation, but there is no forfeiture or voluntary relinquishment for this purpose if an amount is paid, or a legally binding right to a payment is created, that acts as a substitute for the forfeited or voluntarily relinquished amount."
- If you replace an existing right to deferred compensation, even if the existing right is not vested, then the new right is a substitution. If the new right will result in a change in the timing of payment (either earlier or later) the result is a violation of Code section 409A.
- Very tricky, hard to spot, often seems innocuous.



Common Code section 409A Errors: Short-Term Deferral Errors

- Short term deferral rule generally requires payment by March 15th of the year following the year in which the compensation becomes vested (no longer subject to a substantial risk of forfeiture).
- Common Error 1: Payment actually occurs after March 15th
 - Impact depends on what's in writing
- Common Error 2: Bonus plan indicates that payment will not happen until an event occurs (e.g., the audit is complete, the financials are closed, etc.)
 - Automatically a 409A failure (unless there is great savings language)



Common Code section 409A Errors: Elective Deferrals; Definition of Compensation

- Elective deferral arrangements generally allow for deferrals based on a definition of compensation
- Often the definition of compensation is not well developed or properly coordinated with other deferrals (such as those under a 401(k) plan).
- If the Plan's definition of compensation is not followed, the result is an operational violation of Code section 409A
- Even tiny dollar amounts cause a violation with respect to the entire account balance (and any other aggregated plans)
- Correction can be difficult and costly



Common Code section 409A Errors: Accelerations; Changes in Time or Form

- Participants will often request or demand early payments of deferred compensation
- In most cases this is not possible and results in a violation of Code section 409A
- Some exceptions can be applied, but they are very detailed in their requirements.
- Participants planning for retirement or trying to avoid taxes often request further deferrals or changes in the time or form of payment
- The general rule is that this is not allowed, but there is a special "5-year kick-out" rule
- Employers may, but are not generally required to, allow participants to further defer or change the form of payment if the 5-year kick-out rule requirements are met
 - Election must occur 12 months before payment date
 - Election effective 12 months after made
 - Must delay payment a minimum of 5 years
 - Application of these rules is extremely complicated



Common Code section 409A Errors: Stock Options and Valuations

- Stock options and stock appreciation rights that are not designed to meet the payment timing rules of Code section 409A must meet certain requirements in order to avoid being considered deferred compensation.
- Must be granted with an exercise price equal to fair market value
- May not have any other features for the deferral of compensation
- Valuation issues present a risk
- Previously common plan provisions create issues as well (e.g., provisions that pay the purchase price over time)



Common Code section 409A Errors: Offsets

- Many employment and deferred compensation agreements contain language indicating that payments under the plan/agreement may be used to offset other debts incurred by the employee to the company
- These are generally noncompliant plan terms under Code section 409A
- The regulations do allow a maximum offset of \$5,000.



Correction Programs

Notice 2010-6

- Allow for corrections of certain plan document failures
- Generally requires filings with the IRS by both the employee and employer in the year of correction
- Can still impose partial 409A taxes if certain events occur within a set time period after the correction
- Commonly correctable provisions include:
 - Incorrect definitions of Separation from service, Disability, Change in Control
 - Impermissible toggles (e.g., lump sum if involuntary termination, but installments if voluntary termination)
 - Impermissible payment period following a permissible payment event (e.g., payment period of more than 90 days after a permissible event or a period that allows the employee to choose the tax year).



Correction Programs

Notice 2010-6

- Also allows for interpretive room in the event of ambiguous plan terms and ambiguous payment timing, but must comply in operation
- Scope is limited
- For definitions, they must actually be ambiguous or undefined (e.g., payment upon “termination of employment”)
- If plan contains savings language, then it is not ambiguous
- Ambiguous payment timing includes phrases such as “as soon as reasonably practicable” – but they must still be tied to an otherwise good payment event and must be interpreted consistently with 409A



Correction Programs

Notice 2008-113

- Allows for correction of operational errors under Code section 409A
- Generally requires both employer and employee to provide corrective filings with their tax returns for the year in which the correction is made (and sometimes certain other tax years)
- There’s usually a price in the form of the partial payment of the 409A tax – but it’s worth it because the aggregation rule is generally waived!
- Types of failures that can be corrected:
 - Acceleration failures (includes early payments and failures to implement deferral elections)
 - Six month rule violations
 - Further deferrals (either failures to pay or erroneous deferrals)
 - Stock option and stock appreciation rights failures (erroneous establishment of the exercise price)
- The penalty generally gets worse depending on how long ago the failure occurred
- Generally not available if the failure is not corrected by the end of the second year following the year in which it occurred



Correcting Outside of the 409A Correction Programs

Same year tax correction principle

- Using this rule is “expert mode” and requires a good understanding of applicable case law
- Generally can unwind transactions in the same year in which they arise under the doctrine of rescission and the rule for reversing mistaken payments under *Couch v. Commissioner* and *Russel v. Commissioner*.

Correcting unvested amounts

- The preamble to the proposed regulations for calculating the tax indicate that a correction can occur with no consequences if the correction occurs in a tax year before the year in which vesting occurs
- This makes sense because the 409A taxes do not apply until the first year in which there is first no longer a substantial risk of forfeiture



Thank you, and now for the disclaimer section of this presentation...

- This presentation is intended for general information purposes only and does not constitute legal advice. Specific questions and requests for legal advice should be addressed to legal counsel. Nothing contained in this presentation is intended as tax advice. Any taxpayer should seek advice based on the taxpayer’s particular circumstances from an independent tax advisor with respect to any federal or state tax transaction or matter described in this presentation.

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1 – 2 p.m.

Why Should You Care About Social Security Benefits?

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Why Should You Care About Social Security Benefits?



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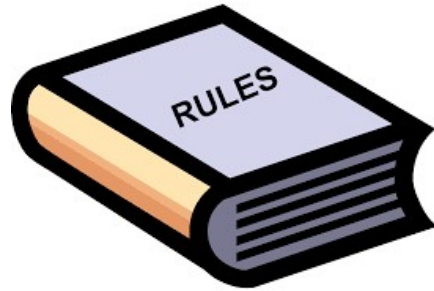
In 2023, almost 67M people (more than 1 of every 6 U.S. residents) receive social security benefits every month



Social Security accounts for 40% of average retiree's income and among elderly beneficiaries, 12% of men and 15% of women rely on Social Security for more than 90% of their income.

Source: Social Security Administration, April 2018

A brief
review of
the
rules



Social Security Retirement Benefits Formula

$$B(a) = PIA(a) \times (1 - e(n)) \times (1 + d(n)) \times Z(a) + \max((.5 \times PIA^*(a) - PIA(a) \times (1 + d(n))) \times E(a), 0) \times (1 - u(a, q, n, m)) \times D(a)$$

Eligibility And Primary Insurance Amount

Eligibility



Primary Insurance Amount (PIA)



Retiree's 3 Choices:

1. Early Retirement

- Age 62 until FRA
- Permanent reduction in benefits

2. Full Retirement Age (FRA)

- Primary Insurance Amount (PIA)

3. Delaying to age 70

- Delayed Retirement Credits (DRCs)



Year of Birth	Full Ret. Age	Months Early if 62	Reduced \$1000 Benefit	Reduction
1943-1954	66	48	\$750	25.00%
1955	66 and 2 months	50	\$741	25.83%
1956	66 and 4 months	52	\$733	26.67%
1957	66 and 6 months	54	\$725	27.50%
1958	66 and 8 months	56	\$716	28.33%
1959	66 and 10 months	58	\$708	29.17%
1960 and later	67	60	\$700	30.00%

The Future of Social Security and Medicare



By the Numbers: 2023 Trustees Report

MEDICARE

2031 -- Hospital Insurance Trust Fund reserves will be Exhausted.

- Medicare will still be able to pay 90% of scheduled benefits.

SOCIAL SECURITY

- 2035 – The surplus in the trust funds will be depleted.
- Social Security will still be able to pay about 77% of the benefits to which retired and disabled workers are entitled.

But did you know...
Social Security has been nearly broke
twice before.

1977

-Changed benefit structure and increased withholding

1983

FRA was increased from age 65 to current staggered ages; taxation of Social Security benefits.

Sources:

Social Security Amendments of 1977: Legislative History and Summary of Provisions (Social Security Bulletin, March 1978)

Social Security Amendments of 1983: Legislative History and Summary of Provisions (Social Security Bulletin, July 1983)

Spousal Benefits

- Must have been married to worker for at least 1 year
- Benefits can begin as early as age **62**
 - Any age if caring for the worker's child who is under 16 or disabled
- Primary worker **MUST HAVE** applied for their own benefit before spouse can receive spousal benefit



Spousal Benefit Amount

Spouse at FRA receives 50% of worker's PIA

- Benefit is calculated on the full payment, not on what the worker is actually receiving

If spouse collects prior to FRA, benefits are reduced

- Earnings limit applies

A spousal benefit **NEVER** EARNS DRCs

Former Spouse Benefits



- Can begin as early as age 62
- Must be currently unmarried
- Must have been married for at least 10 years
 - If 62, can begin receiving benefits on the worker's record as soon the worker reaches 62



**Former
Spouse
Benefit
Amount**

Former spouse at FRA receives 50% of worker's PIA

- Benefit is calculated on the full payment, not on what the worker is actually receiving

If former spouse collects prior to FRA, benefits are reduced

- Earnings limit applies

Survivor Benefits



- Must have been married to worker for at least 9 months
- Survivor can begin to collect benefits at 60
 - Any age if caring for the worker's child who is under 16 or disabled
- Survivor benefits based on insured worker's PIA on date of death
- A divorced spouse may also be entitled to survivor's benefits.

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Survivor Benefit Amount

A widow(er) at FRA will receive 100% of deceased worker's full benefit

- Benefit reduced if taken prior to survivor's FRA
- Be aware of slightly different FRA table for survivor benefits

A survivor benefit DOES NOT EARN DRCs

- Can receive them, but never earns them

A divorced spouse may also be entitled to survivor's benefits.

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Earnings Limit



- Only applies to wages or salary earned **prior to full retirement age**
- Applies to ALL benefits-retirement, spousal, former spouse, survivor, child
- In 2023, benefit reduced by \$1 for every \$2 over \$21,240. Benefit reduced by \$1 for every \$3 over \$56,520 (2023) in the year you reach full retirement age (FRA).

Taxation of Social Security Benefits

- You will pay tax on only 85 percent of your Social Security benefits, based on Internal Revenue Service (IRS) rules. If you:
 - **file a federal tax return as an "individual"** and your *combined income** is
 - between \$25,000 and \$34,000, you may have to pay income tax on up to 50 percent of your benefits.
 - more than \$34,000, up to 85 percent of your benefits may be taxable.
 - **file a joint return**, and you and your spouse have a *combined income** that is
 - between \$32,000 and \$44,000, you may have to pay income tax on up to 50 percent of your benefits.
 - more than \$44,000, up to 85 percent of your benefits may be taxable.
- *Combined Income = Your adjusted gross income + your taxable income + ½ of your Social Security benefits



The Strategies – What's Left?



Clever Strategy #1:
FILE AND SUSPEND



Clever Strategy #2:
Claim Now; Claim More Later



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Clever Strategy #3:
The Merry Widow(er)



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Survivor Benefit: Case Example



- Sue is 60 yrs old. Her husband recently passed away unexpectedly.
- Her retirement benefit at her FRA (66 + 6 months) is \$1,030/month and at age 70 it would be \$1,325/month.
- The survivor benefit at age 60 is \$1,423/month and is \$1,991/month at her FRA.
- **Recommendation:**
 - Sue plans to continue to work and use life insurance proceeds of \$100,000 to supplement income until age 62
 - Begin taking her reduced retirement benefit of \$735/month at age 62
 - At her FRA, switch to full survivor benefit of \$1,991/month

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Clever Strategy #4: The Old Guy and the Baby



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Child Benefit While Delaying Retirement Benefit



John



Jackie



Amanda

- John is 62, wife Jackie is 60 and daughter Amanda is 12
- John's retirement benefit is \$1,465/month at 62 and \$1,991/month at FRA

Recommendation:

- John claim's retirement benefit of \$1,465/month making daughter eligible for benefit of \$995/month
- Upon daughter turning age 18, John will stop retirement benefit and begin receiving Delayed Retirement Credits of 8%/year
 - John will have received \$105,480 of benefits and his daughter will have received \$71,640 of benefits
- At age 70, he will begin receiving benefit of \$1,699/month and his wife will receive \$995/month

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Do-Over Strategy

- Individual can withdraw application within 12 months of first claiming benefits.
 - ✓ Repay all benefits received, including spouse and children
 - ✓ No interest due



Another Do-Over Strategy

- Claim benefits at 62 and then change mind
- Example:
 - Eligible for \$2,000/month at full retirement age
 - Starts benefit at 62, receiving \$1,500/month
 - At full retirement age (66), suspends benefits, but cannot repay (>12 months)
 - Receives delayed retirement credits of 8%/year from 66 – 70
 - At age 70, begins receiving benefit of \$1,980 ($75\% \times 1.32\%$)



Thank you!



2:15 – 3:45 p.m.

Preparing for Sunset

Robert Keebler, CPA/PFS, MST, AEP (Distinguished), *Partner,*
Keebler & Associates, LLP

TCJA Sunset

Robert S. Keebler, CPS/PFS, MST, AEP (Distinguished)
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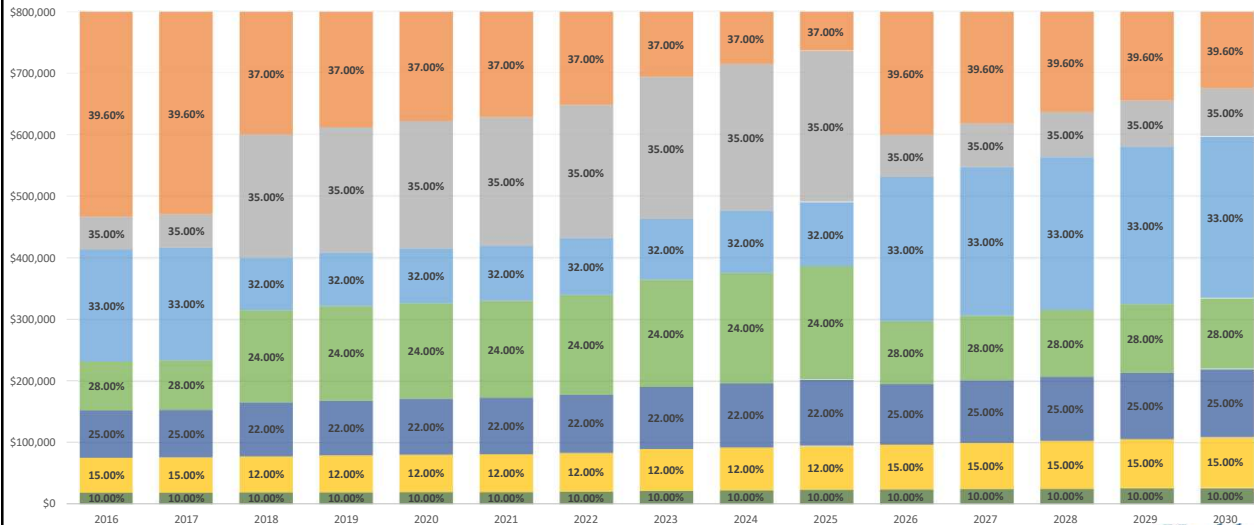
The Tax Cuts & Jobs Act Sunset

Coming Sooner than You Think



Individual Income Tax Rates

MARRIED FILING JOINTLY



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Provisions Important for Individuals

- Individual tax brackets
- Child tax credit
- AMT
- Standard deduction
- Personal exemptions
- Home mortgage interest – acquisition and equity loans
- Charity cash percent limitation
- Misc. itemized deductions, including casualty losses
- PEASE limitation
- Moving expenses
- Student loan & home mortgage discharge
- Certain ABL account provisions
- 199A
- Estate & gift tax exemption

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Individual Taxpayer General Review

	2018-2025	2026+
Individual Rates	Rate decrease; 7 brackets	Rate increase; 7 brackets
Standard Deduction	\$27,700 2023 MFJ (Doubled of prior/sunset law)	\$16,000 2026 MFJ (projected) (projected using the average rate of inflation over the TJCA period)
Personal Exemptions	\$0; Repealed	\$5,300 2026 MFJ (projected) (projected using the average rate of inflation over the TJCA period)
Child/Family Credit	Doubled to \$2,000 and AGI-limit increased to 400k	Reverts to \$1,000/child AGI-limit reverts to \$110,000
AMT	Exemption increased; Exemption phaseout threshold substantially increased	Exemption reduced; Exemption phaseout threshold substantially reduced
Pease Limitation	Suspended	Reinstated

Individual provisions sunset December 31, 2025

Tax Reform Review – Critical Changes

- AMT exemption increase & upcoming sunset

AMT	2017	2023	2026 ?
Single or Head of Household	\$54,300	\$81,300	
Married Filing Jointly	\$84,500	\$126,500	
Begin of Phaseout, Single or HoH	\$120,000	\$578,150	"I'm Back!"
Begin of Phaseout, MFJ	\$160,900	\$1,156,300	
28% Bracket Starts	\$187,800	\$220,700	

§ 55

Itemized Deduction Review

	2018-2025	2026+
SALT Deduction (§ 164, § 11042)	Limited to \$10,000	Prior law reinstated: No limit
Mortgage Interest Deduction (§ 163, § 11043)	Limited to interest on up to \$750,000 of acquisition indebtedness; Repeals deduction for home equity indebtedness	Prior law reinstated: Home equity indebtedness deduction allowed Acquisition debt reverts to \$1,000,000
Charitable Contributions (§ 170, § 11023)	Percentage Limit increased from 50% to 60% (for cash);	Prior law reinstated: 50%-AGI limit for cash applies
Personal Casualty Losses (§165, § 11044)	Repealed, except for declared disasters	Prior law reinstated
Medical Expenses (§213, § 11027)	Expanded for two years by setting the deduction threshold to 7.5% of AGI for all taxpayers	7.5% limitation continues to apply
Job Expenses & Miscellaneous Deductions (§67, § 11045)	Deductions subject to the 2% floor generally suspended	Prior law reinstated
Alimony Paid (§71, § 11051)	Repealed for any divorce or separate instrument executed after 12/31/18	Permanent change; Section 71 is not scheduled to be reinstated at sunset
Moving Expenses (§217, § 11049)	Suspended (except for armed forces)	Prior law reinstated

Deductions

TIMING WILL BE KEY

PEP/PEASE Review

- Phase-out of personal exemptions (PEP) and limitations on itemized deductions (Pease) as income rises above the following threshold amounts:

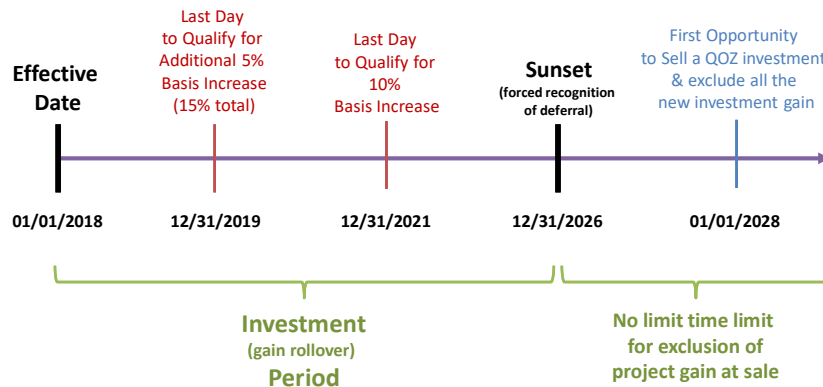
	Statutory Amount	Indexed Amount as of 2017	Projected Figure for 2026
Single	\$250,000	\$261,500	\$329,400
HoH	\$275,000	\$287,650	\$362,300
MFJ	\$300,000	\$313,800	\$395,200

PEP/PEASE Review

- PEP reduces personal exemption by 2% (up to \$0) for every -
 - \$2,500 of income above the threshold amount for single taxpayers
 - \$1,250 of income above the threshold amount for married taxpayers filing jointly
- Pease cuts itemized deductions by 3% of AGI above the threshold amounts up to a maximum of 80%.
 - Standard deduction not reduced; i.e. will apply if the reduction is too great
 - Deductions not limited: Investment interest; Medical expenses; Casualty, theft and wagering losses

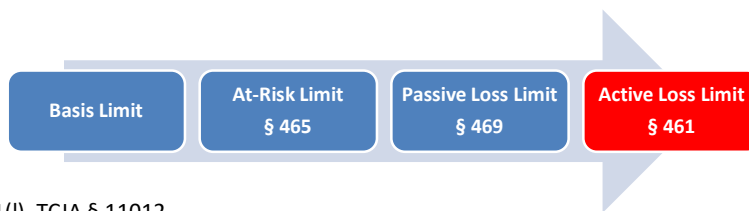
BUSINESS PROVISIONS

Opportunity Zone Timeline



Limitation on Excess Business Losses

- The TCJA amended Section 461 to add a new subsection (l)
- The new section disallows certain excess business losses
 - Must be carried-forward
 - Applies to taxpayers with income exceeding \$500,000 (MFJ)
 - Applies at the partner or shareholder level
- The current statute sunsets the limitation for tax years beginning after 12/31/25



IRC § 461(l), TCJA § 11012

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Bonus Depreciation

- The TCJA provided for 100% bonus depreciation through 2022 (i.e. 100% deduction for property that would otherwise be capitalized & depreciated)
- It is scheduled to be phased out in 20% intervals from 2023-2026

2022	100%
2023	80%
2024	60%
2025	40%
2026	20%
2027	0%

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Section 179

- Before the TCJA, a taxpayer could expense up to \$500,000 of property.
 - However, it was phased out if a business places over \$2,000,000 of property in service during the tax year.
 - This phaseout of course makes it less useful for larger businesses, but those subject to the limitation could still use bonus depreciation.
- The TCJA increased the deduction limit to \$1,000,000 and the start of the placed in-service limit to \$2,500,000.
 - **This change was permanent; i.e. not subject to sunset.**
 - Section 179 will remain the useful for your client's small businesses following sunset (except rental real estate, generally).

IRC § 179, TCJA § 13101

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QUALIFIED BUSINESS INCOME DEDUCTION

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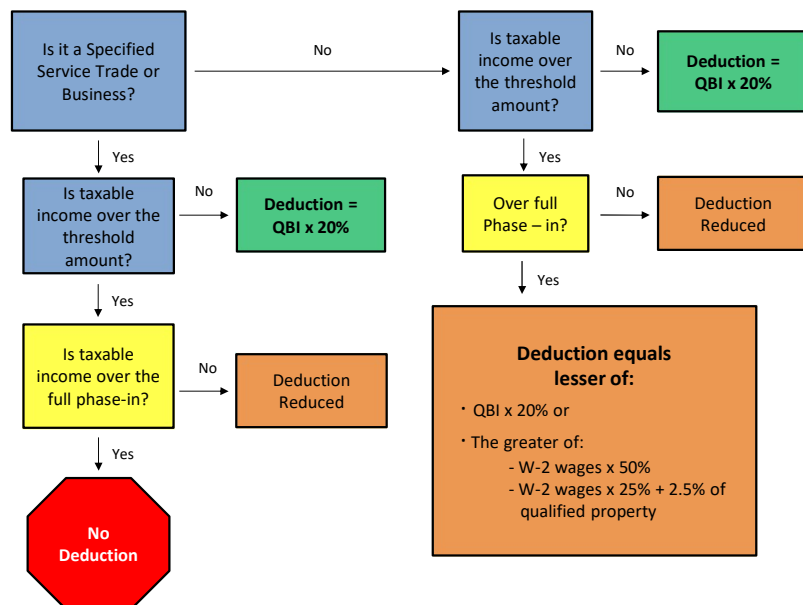
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Qualified Business Income Deduction

- Deduction equals 20% of Qualified Business Income
- Generally available to owners of pass-through businesses
- Limited by the business owner's taxable income
 - Limited for Specified Service Trades or Businesses (SSTB)
 - Limited by wages paid and capital investment

Qualified Business Income Deduction



Qualified Business Income Deduction

SUNSET: IRC § 199A(i) Termination.

This section shall not apply to taxable years beginning after December 31, 2025.

**199A SUNSET ELIMINATES
THE LONG-STANDING TAX ADVANTAGE
WHICH SMALL BUSINESS ENJOYS**

Qualified Business Income Deduction

Top Pass-through Rate	2013-2017	39.6%		78% of total corporate rate, including double taxation (39.6/50.5)
Top Pass-through Rate (199A limitations don't apply)	2018-2025	29.6%	$37\% \times (1-20\%) = 29.6\%$	74% of corporate rate, including double taxation (29.6/39.8)
Top Pass-through Rate (199A limitations apply)	2018-2025	37%		93% of corporate rate, including double taxation (37/39.8)
Top Pass-through Rate (if sunset occurs)	2026-?	39.6%		99% of corporate rate, including double taxation (39.6/39.8)
Corporate Tax Rate – single layer (basically)	1993-2017	35%		
Corporate Tax Rate – double tax (including taxes on dividends)	2013-2017	50.5%	$35\% + 23.8\% \times (1-.35)$	
Corporate Tax Rate – single layer (does not sunset under TCJA)	2018-?	21%		
Corporate Tax Rate – double tax (including taxes on dividends)	2018-?	39.8%	$21\% + 23.8\% \times (1-.21)$	

Sunset Motivated Roth Conversions Bracket Management

Roth Conversions *2017 Tax Reform Refresher*

TAX REFORM PERMINANTLY REPEALED
THE ABILITY TO RECHARACTERIZE
A ROTH CONVERSION

However, it is still possible to
recharacterize a Roth contribution.

Mathematics of Roth IRA Conversions

	Traditional IRA	Roth IRA	Buy Insurance
Current IRA Balance	\$ 1,000,000	\$ 1,000,000	\$ 1,000,000
Less: Income Taxes @ 40%	-	(400,000)	(400,000)
Net Balance	\$ 1,000,000	\$ 600,000	\$ 600,000
Growth Until Death	200.00%	200.00%	200.00%
IRA Balance @ Death	\$ 2,000,000	\$ 1,200,000	\$ 1,200,000
Less: Income Taxes @ 40%	(800,000)	-	-
Net to Family	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000

Mathematics of Roth IRA Conversions

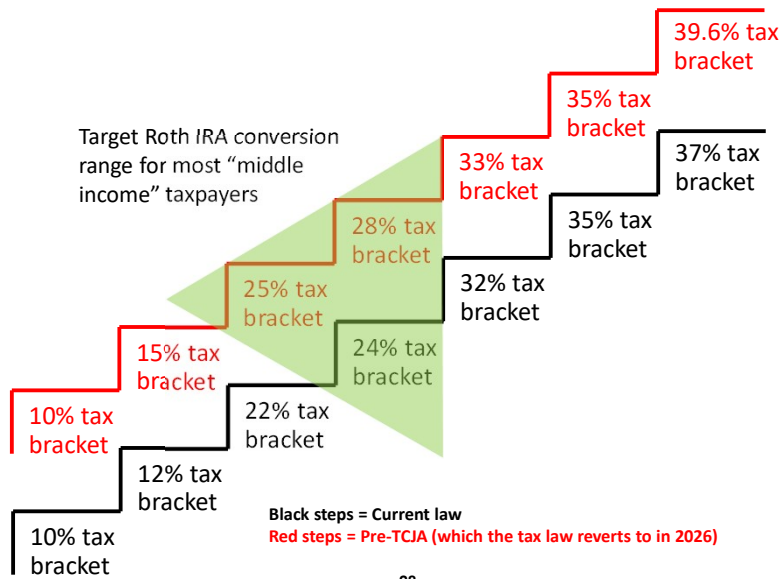
Reasons for converting to a Roth IRA

1. The taxpayer have special favorable tax attributes that need to be consumed such as charitable deduction carry-forwards, investment tax credits, NOLs, etc....
2. The client expect the converted amount to grow significantly
3. Current marginal income tax rate is likely lower than at distribution
4. Cash outside the qualified account is available to pay the income tax due to the conversion
5. The funds converted are not required for living expenses, or otherwise, for a long period
6. The client expects their spouse to outlive them and will require the funds for living expenses
7. The client expects to owe estate tax

Mathematics of Roth IRA Conversions

- The key to successful Roth IRA conversions is often to keep as much of the conversion income as possible in the current marginal tax bracket
 - However, there are times when it may make sense to convert more and go into higher tax brackets
 - Need to take into consideration the 3.8% Medicare “surtax”
 - Need to take into consideration phase-outs of tax-benefits
 - Need to take into consideration the impact of AMT

Mathematics of Roth Conversions



Estate Tax Considerations

- The same amount GST exemption must be allocated for a Traditional IRA or a Roth IRA – the Roth is much more efficient

		Traditional IRA	Roth IRA
Value of Assets		\$ 1,000,000	\$ 1,000,000
Less: Income Tax	37%	(370,000)	-
Net to Trust		\$ 630,000	\$ 1,000,000
GST Exemption Allocated		\$ 1,000,000	\$ 1,000,000

Estate Tax Considerations

- “Missing” IRC § 691(c) deduction
 - To prevent double-taxation, a beneficiary can claim an income tax deduction for estate taxes paid on IRD
 - However, the deduction is equal to the amount of federal estate tax paid
 - The deduction state estate tax paid is “missing”

Estate Tax Considerations

“Missing” IRC § 691(c) deduction example

	Traditional	
	IRA	Roth IRA
IRA balance	\$ 1,000,000	\$ 1,000,000
Less: Federal and state income taxes on Roth IRA conversion (40%)	-	(400,000)
Taxable Estate	\$ 1,000,000	\$ 600,000
Federal estate tax (40%)	\$ 400,000	\$ 240,000
State death tax (10%)	100,000	60,000
Total estate taxes	\$ 500,000	\$ 300,000
Post-death traditional IRA balance	\$ 1,000,000	
Less: IRC §691(c) deduction	(400,000)	
Post-death traditional IRA balance subject to income tax	\$ 600,000	
Federal and state income taxes on IRA distributions (40%)	\$ 240,000	\$ -
Net IRA balance to beneficiaries	\$ 260,000	\$ 300,000

Reconciliation: \$100,000 state death tax x 40% post-death income tax rate = \$40,000 (double-tax component) *OR*
 \$400,000 income tax on conversion x 10% state death tax rate = \$40,000 (estate tax savings)

Estate Tax Considerations

- “Fading” IRC § 691(c) deduction
 - The deduction is calculated on the date of death value
 - Post-death appreciation of pre-tax assets is not offset
 - This results in the relative amount of the deduction “fading” over time

Frozen-in-Time

Estate Tax Considerations

- “Fading” IRC § 691(c) deduction example

	No Planning	Roth IRA Conversion at Death
Traditional IRA balance at death	\$ 1,000,000	\$ 1,000,000
Less: IRC §691(c) deduction	-	(450,000)
Taxable portion of Roth IRA conversion	\$ 1,000,000	\$ 550,000
Federal and state income taxes on Roth IRA conversion (40%)	\$ -	\$ 220,000
IRA balance available for future distributions	<u>\$ 1,000,000</u>	<u>\$ 780,000</u>
Total future IRA distributions	\$ 2,000,000	\$ 1,560,000
Less: IRC §691(c) deduction	(450,000)	-
Less: Amounts not subject to income tax	-	(1,560,000)
Taxable portion of future IRA distributions	<u>\$ 1,550,000</u>	<u>\$ -</u>
Federal and state income taxes on future IRA distributions (40%)	\$ 620,000	\$ -
After-tax total future IRA distributions	<u>\$ 1,380,000</u>	<u>\$ 1,560,000</u>

Reconciliation: \$1,560,000 - \$1,380,000 = \$180,000 *OR* \$620,000 future income tax liability - \$440,000 future value of income tax liability on Roth IRA conversion (i.e. \$220,000 x 2).

Estate & Gift Taxes

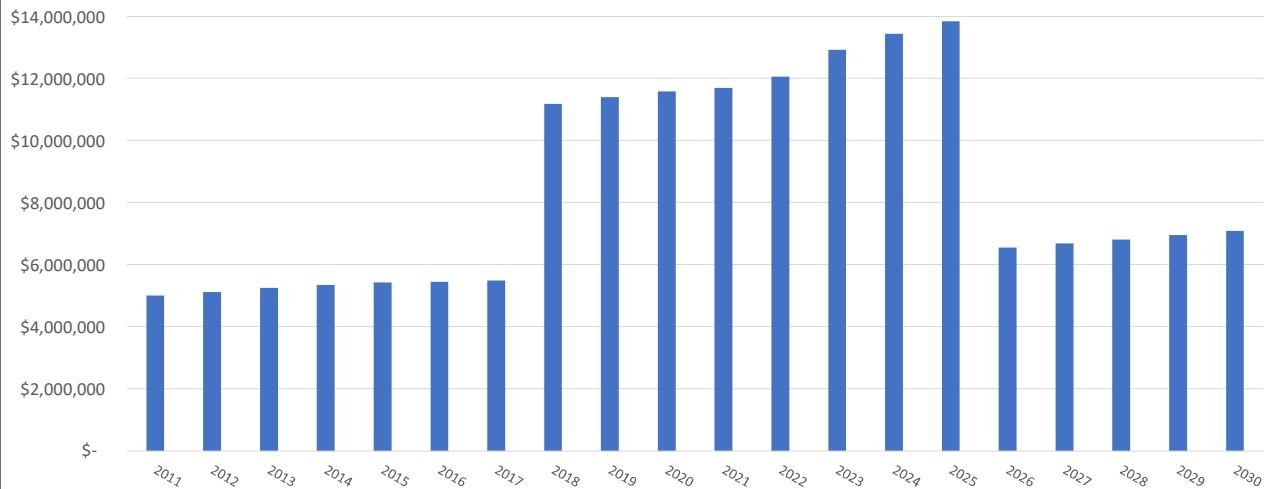
Tax Reform Review – Critical Changes

- Estate & GST tax
 - The TJCA “Doubled” the exemption from 2018 to 2025 (\$12.92M in 2023)
 - Sunsets December 31, 2025
 - **NO CLAW BACK FOR THOSE WHO GIFT BEFORE SUNSET, BUT DIE AFTER SUNSET**
 - Step-up in basis retained at death



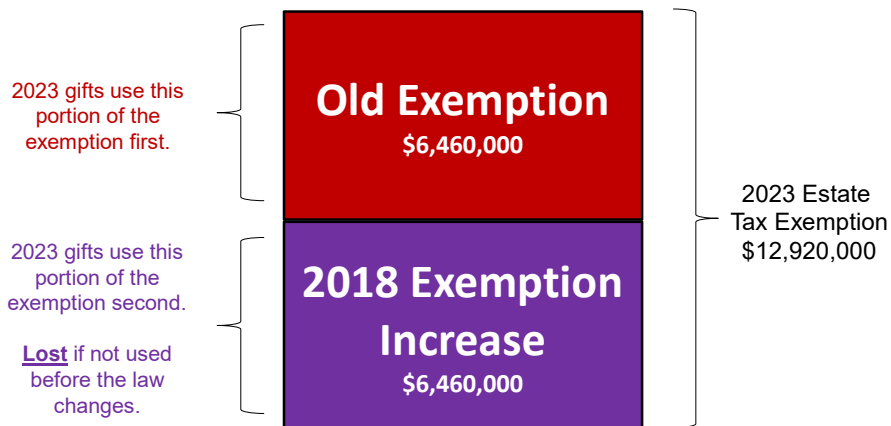
Estate & GST Taxes

Estate Tax Exemption - Past & Projected



Estate & Gift Taxes

Exemption Reduction Math: "Use It or Lose It"



Basis Basics

- Donee's basis for computing gain is the same as the donor's basis
- Donee's basis for computing loss is the lesser of—
 - Donor's basis, or
 - FMV of property on date of gift (Reg. § 1.1015-1(a))

Basis Basics

- The basis calculated in the previous slides is increased by all or a portion of the federal gift tax paid with respect to the gift.
- The increase is the amount of gift tax attributable to the net appreciation in the value of the gift

$$= \frac{\text{Basis increase} \times (\text{gift tax paid}) \times (\text{net appreciation})}{\text{amount of gift}}$$

Basis Basics

- Basis is generally FMV on date of decedent's death or, if elected, the alternate valuation date (IRC § 1014(a))
- Appreciated assets receive a "step-up" in basis at death – saves income tax when the property is sold by "heirs"
- Depreciated assets receive a "step-down" in basis – deprives "heirs" of the income tax benefit of claiming a loss when the property is sold
 - Less common than stepped-up basis because taxpayers have an incentive to realize losses during life

What is the Value of a Step-up?

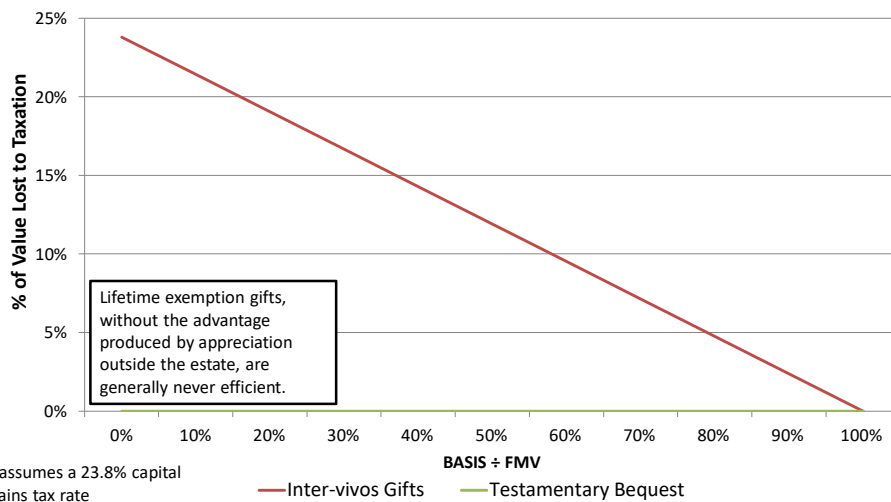
Tax savings

- Federal Capital Gains Tax
- Federal Net Investment Income Tax
- State Capital Gains Tax



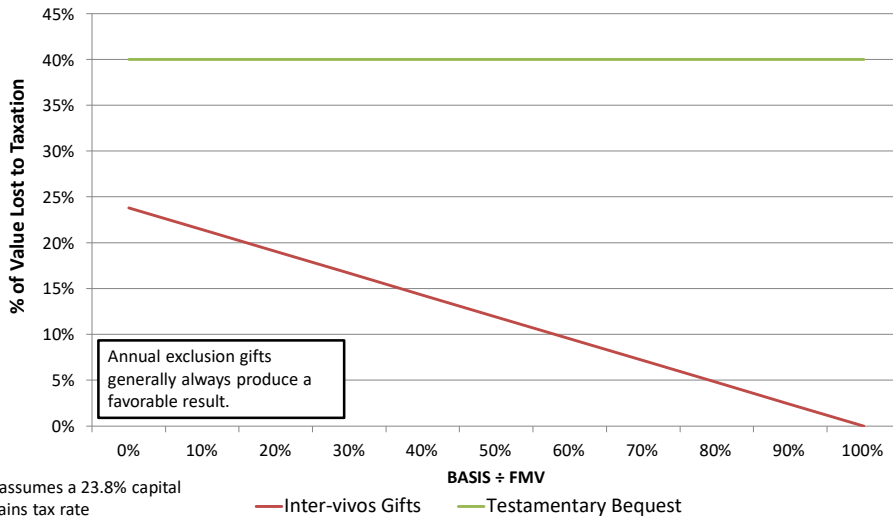
Basis Basics

Lifetime Exemption Gifting / Asset Value Constant / Grantor Lives 3+ Years



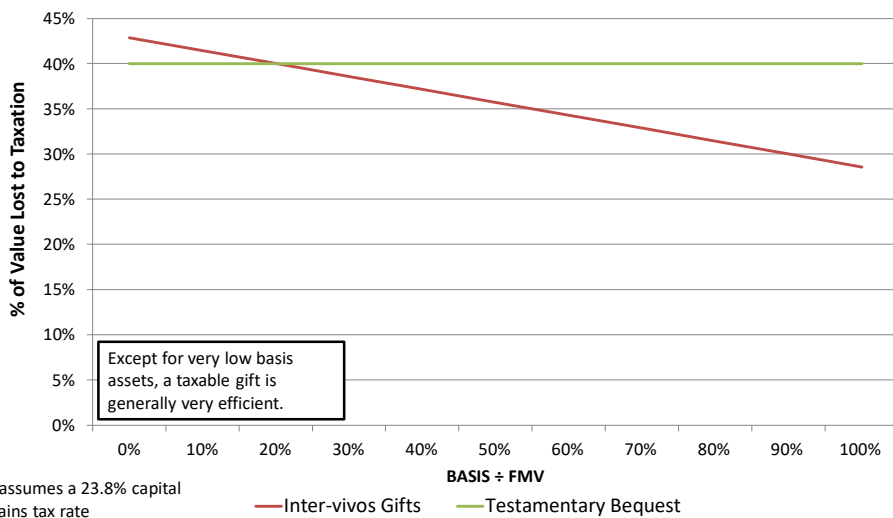
Basis Basics

Annual Exclusion Gifting / Asset Value Constant / Grantor Lives 3+ Years



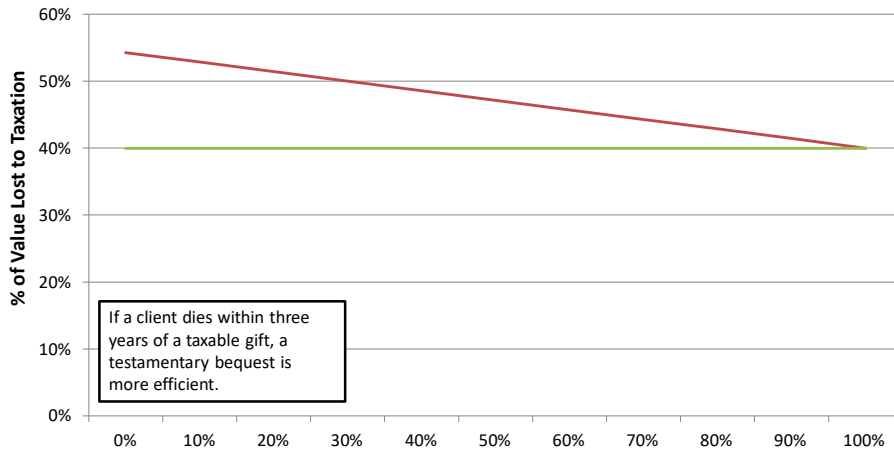
Basis Basics

Gift Tax Paid / Asset Value Constant / Grantor Lives 3+ Years



Basis Basics

Gift Tax Paid / Asset Value Constant / Grantor Dies within 3 Years



If a client dies within three years of a taxable gift, a testamentary bequest is more efficient.

*assumes a 23.8% capital gains tax rate

BASIS ÷ FMV

— Inter-vivos Gifts — Testamentary Bequest

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Single Client Age 92 – Gift versus Death Analysis Simple Breakeven

Size of Estate	\$ 25,000,000	\$ 25,000,000	\$ 25,000,000
Size of Gift	\$ 10,000,000	\$ 10,000,000	\$ 10,000,000
Basis of Gift	\$ 1,000,000	\$ 6,000,000	\$ 10,000,000
Built-in Gain	\$ 9,000,000	\$ 4,000,000	0
Built-in Gain taxed @ 25%	\$ 2,250,000	\$ 1,000,000	0
Appreciation needed to overcome value of step-up	\$ 5,625,000 ¹	\$ 2,500,000 ²	0 ³
% of Appreciation	56.25%	25%	N/A

1. $\$2,250,000 / 40\% = \$5,625,000$ 2. $\$1,000,000 / 40\% = \$2,500,000$ 3. 40% Estate tax exceeds 25% Income tax

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Single Client Age 92 – Gift versus Death Analysis *Interrelated Breakeven*

Size of Estate	\$ 25,000,000	\$ 25,000,000	\$ 25,000,000
Size of Gift	\$ 10,000,000	\$ 10,000,000	\$ 10,000,000
Basis of Gift	\$ 1,000,000	\$ 6,000,000	\$ 10,000,000
Built-in Gain	\$ 9,000,000	\$ 4,000,000	0
Built-in Gain taxed @ 25%	\$ 2,250,000	\$ 1,000,000	0
Appreciation needed to overcome value of step-up	\$ 15,000,000 ¹	\$ 6,666,667 ²	0 ³
% of Appreciation	150.00%	66.67%	N/A

1. $\$2,250,000 / (40\% - 25\%) = \$15,000,000$ 2. $\$1,000,000 / (40\% - 25\%) = \$6,666,667$ 3. 40% Estate tax exceeds 25% Income tax

Simplified Sunset Case Study

- Client is single
- Net worth: \$20,000,000
- Overall basis: \$10,000,000 (1/2)
- Assume net worth is stagnant over the analysis period (25'-26')
- Estate tax rate: 40% (fed only)
- Capital gains tax rate: 30% (fed+state)
- 2025 estate tax exclusion: \$14,000,000
- 2026 estate tax exclusion: \$7,500,000

2025 Funding -> 2025 Death

Option 1 - Fund Intervivos Trust		Option 2 - Do Nothing	
Gift	\$ 14,000,000	Gift	\$ -
Built-in Gain	7,000,000		
Future Income Tax Liability	2,100,000		
Assets at Death	6,000,000	Assets at Death	20,000,000
+ Prior Gifts	14,000,000	+ Prior Gifts	-
- BEA	<u>(14,000,000)</u>	- BEA	<u>(14,000,000)</u>
Taxable Estate	6,000,000	Taxable Estate	6,000,000
Estate Tax	2,400,000	Estate Tax	2,400,000
Total Tax Liability	\$ 4,500,000	Total Tax Liability	\$ 2,400,000

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Experts. Single. Clients.

2025 Funding -> 2026 Death

Option 1 - Fund Intervivos Trust		Option 2 - Do Nothing	
Gift	\$ 14,000,000	Gift	\$ -
Built-in Gain	7,000,000		
Future Income Tax Liability	2,100,000		
Assets at Death	6,000,000	Assets at Death	20,000,000
+ Prior Gifts	14,000,000	+ Prior Gifts	-
- BEA (clawback adj)	<u>(14,000,000)</u>	- BEA	<u>(7,500,000)</u>
Taxable Estate	6,000,000	Taxable Estate	12,500,000
Estate Tax	2,400,000	Estate Tax	5,000,000
Total Tax Liability	\$ 4,500,000	Total Tax Liability	\$ 5,000,000

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Trust Gifting for Sunset

- Consider the significant impact of income tax basis and recognize capturing the disappearing exemption has cost
- Prepare to fund now, but delay actual funding to an opportune time (i.e. fall of 2025 under current law)

CONCLUSION