

Agenda

- **RMD Planning under the SECURE Act**
- **Other Planning Opportunities under the Consolidated Appropriations Act of 2020**
- **Planning under the Final 199A Regulations**
- **Basis Adjustment Planning for Estate Planning Clients**
- **Preparing for the New OT Rule**

Consolidated Appropriations Act of 2020

Consolidated Appropriations Act of 2020

- **Extensions of credits and deductions that had expired in prior years, as well as some that were scheduled to expire in 2019**
- **Repeal of the TCJA changes to the kiddie tax rules**
- **New disaster relief tax provisions**

Consolidated Appropriations Act of 2020

- **Permanent repeal of the "Cadillac Tax" on high cost employer sponsored health insurance and two other healthcare taxes**
- **Expansion of Section 529 plans**
- **Major changes to some retirement-related tax provisions**

December 20, 2019

- **Two year-end spending packages signed into law**
 - **Consolidated Appropriations Act**
 - **Further Consolidated Appropriations Act**
 - **Comprehensive retirement reform package (“SECURE Act”)**
 - **Disaster relief and new health and welfare provisions**

New Provisions Affecting Employer Plans and IRAs

- **Age when RMDs required to begin increased from age 70-1/2 to 72**
- **Non-spouse beneficiaries required to distribute inherited amounts within 10 years**

Exceptions to 10 Year Rule

- **Disabled individuals,**
- **Certain chronically ill individuals,**
- **Beneficiaries whose age is within 10 years of the decedent's age,**
- **Minors (they would begin a 10-year payout period upon reaching the age of majority), and**
- **Recipients of certain annuitized payments begun before enactment of the SECURE Act.**

Other New Rules

- **Distribution within 1 year of birth or adoption of individual incapable of self-support**
 - Exempt from 10% early distribution penalty
 - Limited to \$5,000
- **“Difficulty of care” payments treated as eligible compensation for retirement plan funding**

IRAs Only

- Taxpayers with earned income can make Traditional IRA contributions at any age, not just for years before reaching age 70½
- Certain stipend, fellowship, and similar payments to graduate and postdoctoral students treated as earned income for IRA contribution purposes

Planning Around the 10 Year Payout

- **Can still leave IRA outright to beneficiaries (except for spouse the payout will simply be shorter)**
- **Trusts with payouts based on RMDs will need to be reviewed**
- **Conduit trusts may no longer work**
- **Accumulation trusts still work, but need to plan for how the tax will be paid**

Planning Around the 10 Year Payout

- Roth conversions will need to be considered more often by IRA owners, particularly where the IRA owner is in a lower bracket than expected of the beneficiary – as often would be the case where a trust is the beneficiary
- CRTs may have more appeal where the IRA owner desires to leave a lifetime stream of income instead of a 10 year payout

More Flexibility for IRA Contributions

- Taxpayers with earned income can make Traditional IRA contributions at any age, not just for years before reaching age 70¹/₂
- Certain stipend, fellowship, and similar payments to graduate and postdoctoral students will be treated as earned income for IRA contribution purposes

New Eligible Expenses for 529 Plans

- **May make tax-free 529 plan distributions to pay for registered apprenticeships**
- **May also distribute up to \$10,000 in order to make repayments of student loans for a 529 plan beneficiary—or a beneficiary’s sibling**

Incentives to Establish or Enhance Employer Plans

- Employers can more easily participate in a MEP or a new variant, a “pooled employer plan,” or PEP
- Employers may establish a qualified plan—such as a profit sharing or pension plan—as late as their business tax filing deadline, including extensions
- Small employer retirement plan startup tax credit increases from \$500 to a maximum of \$5,000 per year, available to cover startup costs for the first three years that the plan is in effect

Incentives to Establish or Enhance Employer Plans

- Annual tax credit is \$500 for each of the first three years that a plan with an automatic enrollment feature is maintained
- Employers that make nonelective safe harbor plan contributions may amend up to 30 days before the end of a plan year or amend by the close of the following plan year if the plan is also amended to require a four percent nonelective safe harbor contribution

New Ways to Save More in Employer Plans

- **Some 401(k) plans meet nondiscrimination requirements through automatic enrollment and automatic deferral increases. These qualified automatic contribution arrangements (QACAs) will now have a maximum 15 percent deferral rate instead of 10 percent**
- **Defined contribution plans must provide, at least annually, a projected lifetime income stream that a participant's accrued benefit could generate**

New Ways to Save More in Employer Plans

- Employees who have three consecutive 12-month periods of 500 hours of service and who satisfy the plan's minimum age requirement must be allowed to make elective deferrals in an employer's 401(k) plan
- The current, more restrictive, eligibility rules could continue to be applied to other contribution sources (e.g., matching contributions) and to ADP/ACP safe harbor plans
- Employers may also exclude such part-time employees from coverage, nondiscrimination, and top-heavy test rules

Other Provisions Affecting Employer Plans

- May distribute a 403(b) custodial account “in kind” to a participant or beneficiary when the employer is terminating the 403(b) plan
- Participants in a qualified plan, 403(b) plan, or governmental 457(b) plan may roll over lifetime income investments to an IRA or another retirement plan without a traditional distribution triggering event if their plan no longer permits such investments

Other Provisions Affecting Employer Plans

- Retirement plan loans enabled through a credit card will be treated as distributed from the plan and subject to taxation
- Employers sponsoring defined contribution plans that have the same trustee, administrator, fiduciaries, plan year, and investment options may file a common Form 5500

Higher Penalties for Plan Reporting Failures

- **Form 5500 -- \$250 per day, up to a maximum of \$150,000**
- **Form 8955-SSA (deferred benefit reporting) -- \$10 per day, up to a maximum of \$50,000 for failing to file; \$10 per day, up to a maximum of \$10,000 for failing to file a notification of change**
- **Withholding notices -- \$100 per failure, up to a maximum of \$50,000 for all such failures during any calendar year**

Tax Extenders

- **The Further Consolidated Appropriations Act extends three dozen expired and expiring deductions and tax credits**
- **All but a few of the provisions had expired at the end of 2017 and were extended retroactively to December 31, 2017**
- **Amended 2018 tax returns and revisions to previously calculated 2019 tax liabilities may be warranted**

Tax Extenders - Examples

- **Exclusion from Gross Income of Discharge of Qualified Principal Residence Indebtedness**
- **Treatment of Mortgage Insurance Premiums as Qualified Residence Interest**
- **Deduction of Qualified Tuition and Related Expenses**
- **Reduction in Medical Expense Deduction Floor**
- **Employer Credit for Paid Family and Medical Leave**

Modification of Kiddie Tax Rules

- **The Act eliminates the kiddie tax calculation that was enacted in the Tax Cuts and Jobs Act of 2017**
- **Thus, estate and trust tax rates are no longer used to calculate a child's tax on unearned income**
- **The Act also eliminates the reduced AMT exemption amount for a child to whom the kiddie tax applies**

Repeal of the "Cadillac Tax"

- **The Act permanently repeals the excise tax on high cost employer sponsored health insurance for tax years beginning after December 31, 2019**
- **As a result, the so-called "Cadillac Tax" has been repealed nearly a decade after its original enactment without ever having gone into effect**

Planning under the Final 199A Regulations

199A Refresher

An individual is allowed a deduction up to the lesser of:

- “Qualified business income”, or
- 20% of taxable income less net capital gains and qualified dividends

Qualified Business Income

- The net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business (“QTOB”)
- A QTOB means any business other than:
 - A “specified service trade or business” (“SSTB”)
 - Performing services as an employee
- An SSTB includes all traditional professions other than architecture and engineering

Section 199A(b)(2)(A) Limitation

- **Deduction limited to 20% of QBI**
- **Covers around 75% of all business owners eligible for the deduction**

Section 199A(b)(2)(B) Limitation

Deduction limited to the greater of:

- 50% of W-2 wages
- 25% of W-2 wages plus 2.5% of the aggregate unadjusted basis immediately after acquisition (“UBIA”) of the business’s qualified property

“Phase-in Ranges”

- A range within which another limitation on the 199A deduction phases in
- \$100,000 from threshold for married filing jointly
- \$50,000 from threshold for all others

2019 Threshold for Phase-in Range

- **\$321,400 or married individuals filing jointly**
- **\$160,725 for married individuals filing separately**
- **\$160,700 for single filers and heads of households**

Section 199A(b)(3)(B)

- **Owners of QTOBs and SSTBs may receive 199A deductions through the phase-in range**
- **Owners of SSTBs may receive a lesser deduction within the phase-in range**
- **Owners of SSTBs receive no deduction if their taxable income exceeds the phase-in range**

Final 199A Regulations – Effective Date

- **2018 - - allowed choice between proposed and final regulations**
- **Must use final regulations for tax years ending after February 8, 2019**

Final 199A Regulations – Aggregation

Proposed Regs – may, but not obligated to, aggregate if:

1. Same person or group owns 50% or more of each trade or business for majority of tax year
2. Businesses use same tax year
3. None of the businesses is an SSTB

Final 199A Regulations – Aggregation

4. At least two of the following:
- a) Same products or services (or commonly offered together)
 - b) Share facilities, personnel or other business resources
 - c) Operate in coordination with, or reliance upon, each other (e.g., supply chain interdependencies)

Final 199A Regulations – Aggregation

Proposed Regs -- Other Requirements:

- Taxpayer combining trades or business must do so consistently in all future years unless there is a change in circumstances
- Must attach a statement to return with certain identifying information about each business

Final 199A Regulations – Aggregation

Final Regs – permit a relevant pass-through entity (“RPE”) to aggregate trades or businesses at the entity level

- Must attach a statement to each owner’s K-1
- Must compute QBI, W-2 wages and UBIA on an aggregated basis
- All owners bound by decision but can aggregate other businesses if conditions met

Final 199A Regulations – Aggregation

Other changes made by final regs:

- Attribution rules apply to 50% ownership test
- Can aggregate an SSTB with gross receipts below the de minimis threshold
- First aggregation factor now includes products, property or services

Final 199A Regulations – Aggregation

Other changes made by final regs:

- Taxpayers that fail to aggregate in one year can aggregate in a subsequent year
- May not amend a prior return to aggregate
- Disaggregated businesses can be aggregated after three years

Final 199A Regulations – Di Minimis Rule

Proposed Regs:

- Business with gross receipts of \$24 million or less isn't an SSTB if less than 10% of its gross receipts are from the performance of services in the specified field
- If gross receipts exceed \$25 million, the percentage is reduced to 5%

Final 199A Regulations – Di Minimis Rule

Final Regs:

- Eliminate “cliff effect”
- Must establish that businesses are separate
- Result is that the income of the non-SSTB can be treated as QBI

Final 199A Regulations – Antiabuse

- Proposed regs eliminated “crack and pack” strategy by providing that an SSTB includes any business with 50% or more common ownership that provides 80% or more of its property or services to the SSTB
- **Final Regs:**
 - Eliminate 80% threshold
 - Include a 5% de minimis rule

Final 199A Regulations – Like Kind Exchanges

Proposed Regs:

- UBIA of property received in 1031 like kind exchange is adjusted basis of relinquished property
- Takes into account depreciation deductions

Final 199A Regulations – Like Kind Exchanges

Final Regs:

- UBIA of property received in 1031 like kind exchange is UBIA of relinquished property
- Adjusted down for excess of any money or property (i.e., “boot”) received over the appreciation in the relinquished property
- Adjusted up for any additional taxpayer investment

Final 199A Safe Harbor for Rental Real Estate

- **Rev. Proc. 2019-38 issued by IRS on September 24, 2019**
- **Finalizes rules proposed by the IRS on January 18, 2019, in Notice 2019-07**
- **IRS and Treasury made few changes when finalizing the guidance**

Final 199A Safe Harbor for Rental Real Estate

Two methods for treating net rental profit as QBI:

- Claim that the rentals are trades or businesses under existing law, or
- Use the new safe-harbor rules

Final 199A Safe Harbor for Rental Real Estate

- **Rental Real Estate Enterprise:**
 - Group properties as commercial, residential, triple-net or mixed use, or
 - Treat each as a separate enterprise
- **Residential may not be combined with commercial**

Final 199A Safe Harbor for Rental Real Estate

Mixed use:

- May be treated as a single rental real estate enterprise or it may be bifurcated into separate residential and commercial
- If treated as a single rental real estate enterprise, may not be treated as part of the same enterprise as other residential, commercial, or mixed-use property

Final 199A Safe Harbor for Rental Real Estate

- **Once a taxpayer or RPE chooses to treat similar properties as a single rental real estate enterprise, it must continue to do so in future years (including when it acquires new properties)**
- **A taxpayer or RPE that has chosen to treat its interests as separate enterprises, however, may choose to treat its interests in similar commercial or similar residential properties as single rental real estate enterprises in a future year**

Final 199A Safe Harbor for Rental Real Estate

- **Determination to use the safe harbor must be made annually**
- **Rental real estate enterprise treated as a single trade or business if the requirements are satisfied during the taxable year**
- **Each rental real estate enterprise that satisfies the requirements of this safe harbor is treated as a separate trade or business for purposes of applying section 199A**

Final 199A Safe Harbor for Rental Real Estate

Safe harbor Factors:

- Maintain separate books and records reflecting income and expenses
- Perform 250 or more hours of “rental services” during the tax year
- Any 3 out of 5 years okay if in existence more than 4 years

Final 199A Safe Harbor for Rental Real Estate

Safe harbor Factors:

- Maintain contemporaneous records
 - hours of all services performed;
 - description of all services performed;
 - dates on which such services were performed; and
 - who performed the services

Final 199A Safe Harbor for Rental Real Estate

- **Attach statement to return:**
 - A description (including the address and rental category) of all properties included in the enterprise,
 - A description (including the address and rental category) of rental real estate properties acquired or disposed of during the taxable year, and
 - A representation that the requirements of the revenue procedure have been satisfied.
- **Final rule eliminates the “under penalty of perjury” affirmation required by the proposed revenue procedure**

Examples of rental services that qualify:

- Advertising to rent or lease the real estate
- Negotiating and executing leases
- Verifying information contained in the prospective tenant applications
- Collection of rent
- Daily operation, maintenance, and repair of the property, *including the purchase of materials and supplies*
- Management of the real estate
- Supervision of employees and independent contractors

Examples of activities that do not count as rental services:

- **Arranging financing**
- **Procuring property**
- **Studying and reviewing financial statements or reports on operations**
- ***Improving property under § 1.263(a)-3(d)* (proposed safe harbor said "planning, managing, or constructing long-term capital improvements")**
- **Hours spent traveling to and from the real estate**

Excluded from the Safe Harbor:

- Real estate used by the taxpayer (including an owner or beneficiary of an RPE) as a residence
- Real estate rented or leased under a triple net lease
- Real estate rented to a trade or business conducted by a taxpayer or an RPE which is commonly controlled
- The entire real estate interest if any portion of the interest is treated as an SSTB

199A Restructuring: Self-Employment Tax

- **Self-employment tax (“SET”) is a key issue in 199A restructuring**
- **IRC 1401(a)(13) provides that limited partners don’t owe SET on their shares of limited partnership income**
- **Prop. Reg. 1.1402(a)-2 issued on January 13, 1997, but never finalized or withdrawn**

199A Restructuring: Self-Employment Tax

- **Under the Prop. Reg., limited partner if:**
 - Lack contract signing authority,
 - Work 500 or fewer hours, and
 - Not personally liable for partnership debt
- **Prop. Reg. doesn't apply to professional partnerships**

199A Restructuring: Self-Employment Tax

- **Can still avoid SET if any of the 3 tests is not met if partnership agreement provides for both of the following:**
 - A manager class, all of whose members are also managers
 - An investor class in which a safe harbor amount of 20% of the partners meet the 3 tests

Basis Adjustment Planning for Estate Planning Clients

Basis Adjustment Planning

- **Make distributions to the beneficiary pursuant to:**
 - Discretionary distribution standard
 - Non-fiduciary, nontaxable power of appointment
- **Careful that granting an inter vivos power of appointment exercisable during the settlor's lifetime might cause trust to be a grantor trust**

Basis Adjustment Planning

- **Have someone grant a general power of appointment to the beneficiary**
- **Consider including a broad exculpatory clause and/or providing that they have no authority to grant the power until requested to consider doing it by some designated person or class of persons**

Basis Adjustment Planning

- Use a formula general power of appointment based on the lesser of the individual's remaining GST exemption or applicable exclusion amount
- Give a non-adverse party the power to modify the power to add flexibility

Basis Adjustment Planning

Trigger the Delaware tax trap by the exercise of a nontaxable special power of appointment to appoint the assets into a trust of which a beneficiary has a presently exercisable general power of appointment.

Delaware Tax Trap

The basic question is whether the second power of appointment (the one created through the exercise of the original special power of appointment) has the effect of restarting the Rule Against Perpetuities. If so, then the Delaware Tax Trap is sprung and the assets are included in the estate of the person exercising the original special power of appointment.

Delaware Tax Trap

To limit the possible “inappropriate” exercise of the special power of appointment, consider:

- Granting a testamentary power that some independent person has the ability to remove before the powerholder dies or to revise
- Specify that the power is exercisable only with the consent of some other non-adverse party (not the grantor)
- Limit the permissible appointees

Basis Adjustment Planning

- **Swap or purchase of grantor trust assets**
- **Watch out for IRC 1014(e)**
- **Example:**
 - Transfer low basis assets intended to pass to children rather than surviving spouse

Preparing for the New OT Rule

Preparing for the New OT Rule

- **Beginning January 1, 2020, businesses have to comply with a new overtime rule**
- **The new rule requires that exempt salaried employees must be paid at least \$684 per week, or \$35,568 annually**
- **Employees who do not meet this salary level must be classified as non-exempt, and be paid overtime for all hours worked over 40 in a workweek**

Preparing for the New OT Rule

Employers have two compliance options:

- **Raise Salary.** Employers can raise an employee's salary to satisfy the new rule. Under this scenario the employee will remain exempt from overtime pay requirements. For example, if the employee was making \$455 per week, the company would have to provide a raise of \$229 per week.
- **Convert to Non-Exempt.** Some employers will choose to begin paying hourly wages and overtime rather than paying a higher salary. Under this scenario the employer must begin tracking hours so that the company can accurately compensate for all time worked, and all overtime due. (If the job requires more than 40 hours of work in a week, the company might choose to divide responsibilities among multiple employees to limit overtime liabilities).

Preparing for the New OT Rule

Remember that to qualify for exemption from FLSA's overtime requirements, an employee must:

- Be paid the salary level AND
- Perform the appropriate exempt duties

Preparing for the New OT Rule

To satisfy the exempt duties test, work must be:

- **Executive** – Primary duty is management of two or more full-time employees.
- **Administrative** – Primary duty is office or non-manual work related to business operation.
- **Professional** – Primary duty is performance of work requiring advanced knowledge.
- **Computer Related** – Primary duty is computer or program design.
- **Outside Sales** – Primary duty is selling products or services at the customer's place of business or home.

The End

