Recent Developments in Federal Income Taxation

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To obtain today's outline and slides:
https://tinyurl.com/outline-mar18-fwtu

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Selected Highlights—Bipartisan Budget Act of 2018

- Depreciation and amortization
  - Racehorses placed in service in 2017 have a 3-year recovery period [p.2]
  - Motorsports entertainment complexes placed in service in 2017 have a 7-year recovery period [pp.2-3]
  - Taxpayers can treat 50% of cost of qualified advanced mine safety equipment as a deductible if placed in service in 2017. [p.3]

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Employee Retention Credit
2017 Disaster Relief Act (9/29/17)
Outline: item F.1, page 3

- The Disaster Relief and Airport and Airway Extension Act of 2017, § 503, Pub. L. No. 115-63 (9/29/17) provides:
  - "Eligible employer" can include "Hurricane Harvey employee retention credit" among components of general business credit under § 38(b).
- Credit is 40 percent of "qualified wages" for each "eligible employee."
  - Cap on qualified wages is $6,000, so maximum credit is $2,400/employee.
- *Eligible employer*: one that operated an active trade or business in a Harvey/Irma/Maria disaster zone if, because of damage from hurricane, it became inoperable after a specified date and before 1/1/18.
  - Specified dates: 8/23/17 (Harvey), 9/4/17 (Irma), 9/16/17 (Maria).
- *Eligible employee*: principal place of employment (PPE) was in the relevant disaster zone on the relevant specified date.
- *Qualified wages*: wages paid or incurred by eligible employer with respect to eligible employee from date the PPE became inoperable through date the business resumed significant operations at PPE.

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Employee Retention Credit
Bipartisan Budget Act of 2018 (2/9/18)
Outline: item F.1.a, page 3

- The Bipartisan Budget Act of 2018, § 20103, Pub. L. No. 115-123 (2/9/18) provides:
  - "Eligible employer" can include "California wildfire employee retention credit" among components of general business credit under § 38(b).
- Credit is 40 percent of "qualified wages" for each "eligible employee."
  - Cap on qualified wages is $6,000, so maximum credit is $2,400/employee.
- *Eligible employer*: one that operated an active trade or business in a California wildfire disaster zone if, because of damage from the wildfires, it became inoperable after 10/8/17 and before 1/1/18.
- *Eligible employee*: principal place of employment (PPE) was in the California wildfire disaster zone on 10/8/17.
- *Qualified wages*: wages paid or incurred by eligible employer with respect to eligible employee from date the PPE became inoperable through date the business resumed significant operations at PPE.

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Use of Retirement Funds by Hurricane Survivors
2017 Disaster Relief Act (9/29/17)
Outline: item B.1.a, page 5

- The Disaster Relief and Airport and Airway Extension Act of 2017, § 502, Pub. L. No. 115-63 (9/29/17), provides special rules for distributions and loans from qualified employer plans (and distributions from IRAs) to victims of Harvey, Irma, and Maria.
- "Qualified hurricane distributions"
  - Up to $100,000 not subject to normal 10% penalty for early withdrawal.
  - Income is reported ratably over 3 years unless taxpayer elects otherwise.
  - Can be recontributed to an eligible plan or IRA within 3 years (i.e., rollover)
    - See IRS Form 8930 and its instructions for guidance.
  - Are not subject to normal 20% withholding that applies to rollovers.
  - Defined as distributions from an eligible retirement plan before 1/1/19 and on or after 8/23/17 to an individual whose principal place of abode on 8/23 was in the Hurricane Harvey disaster area and who sustained an economic loss by reason of Hurricane Harvey.
    - Similar definitions for Irma (9/4/17) and Maria (9/16/17).

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Use of Retirement Funds by Hurricane Survivors 2017 Disaster Relief Act (9/29/17)

Outline: item B.1.a, page 5

- Distributions for Home Not Constructed or Purchased. Section 502(b) of the legislation:
  - Permits an individual who received a "qualified distribution" to recontribute it from 8/23/17 to 2/28/18 to a qualified employer plan or IRA
    - "Qualified distribution" is one received after 2/28/17 and before 9/21/17 that was to be used to construct or purchase a principal residence in the Harvey/Irma/Maria disaster area that was not constructed or purchased on account of the hurricanes.
- Loans. Section 502(c) of the legislation:
  - For a "qualified individual"
    - Increases the limit on retirement plan loans to lesser of $100,000 or 100% of present value for loans made from 9/29/17 through 12/31/18.
    - Extends due date for payments due by 12/31/18 on outstanding loans.
  - "Qualified individual:" principal place of abode on a specified date was in Hurricane Harvey/Irma/Maria disaster area and sustained economic loss from the hurricane.

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Use of Retirement Funds by Wildfire Survivors Bipartisan Budget Act of 2018 (9/29/17)

Outline: item B.1.b, page 6

- The Bipartisan Budget Act of 2018, § 20103, Pub. L. No. 115-123 (2/9/18) provides special rules for distributions and loans from qualified employer plans (and distributions from IRAs) to those affected by California wildfires.
- "Qualified wildfire distributions"
  - Up to $100,000 not subject to normal 10% penalty for early withdrawal.
  - Income is reported ratably over 3 years unless taxpayer elects otherwise.
  - Can be recontributed to an eligible plan or IRA within 3 years (i.e., rollover)
    - See IRS Form 8930 and its instructions for guidance.
  - Are not subject to normal 20% withholding that applies to rollovers.
  - Defined as distributions from an eligible retirement plan before 1/1/19 and on or after 10/8/17 to an individual whose principal place of abode during any period from 10/8/17 through 12/31/17 was in the California wildfire disaster area and sustained an economic loss by reason of the wildfires.

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Use of Retirement Funds by Wildfire Survivors Bipartisan Budget Act of 2018 (2/9/18)
Outline: item B.1.b, page 6

- Distributions for Home Not Constructed or Purchased. Section 20102 of the legislation:
  - Permits an individual who received a "qualified distribution" to recontribute it from 8/23/17 to 2/28/18 to a qualified employer plan or IRA
    - "Qualified distribution" is one received after 3/31/17 and before 1/15/18 that was to be used to construct or purchase a principal residence in the California wildfire disaster area that was not constructed or purchased on account of the wildfires.
- Loans. Section 20102 of the legislation:
  - For a "qualified individual"
    - Increases the limit on retirement plan loans to lesser of $100,000 or 100% of present value for loans made from 2/9/19 through 12/31/18.
    - Extends due date for payments due by 12/31/18 on outstanding loans.
  - "Qualified individual:" principal place of abode during any period from 10/8/17 through 12/31/17 was in the California wildfire disaster area and sustained an economic loss by reason of the wildfires.

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Section 139F
Outline: item B.1, page 7

- The Protecting Americans from Tax Hikes Act of 2015 ("2015 PATH Act"), § 304 (12/18/15):
  - Added § 139F to the Code
    - Section 139F excludes from the gross income of an individual who is convicted of a criminal offense under federal or state law and *wrongfully incarcerated* any civil damages, restitution, or other monetary award relating to the individual's incarceration.
  - *In re Elkins*, 117 A.F.T.R.2d 2016-2124 (Bankr. N.D. Ohio 6/14/16). The exclusion of § 139F is available only to the wrongfully incarcerated individual, not to other persons, such as family members.
  - *Recent Development*: the Bipartisan Budget Act of 2018 extends through 12/31/18 the time within which claims for refund based on § 139F can be filed.

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Selected Highlights—Bipartisan Budget Act of 2018

- Discharge of qualified principal residence indebtedness
  - The legislation retroactively extended through 2017 the § 108(a)(E) exclusion for the discharge of qualified principal residence indebtedness. [item 2, p.7]

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Casualty Losses of Hurricane Survivors 2017 Disaster Relief Act (9/29/17) *Outline: item D.1, page 8*

- The Disaster Relief and Airport and Airway Extension Act of 2017, § 504(b), Pub. L. No. 115-63 (9/29/17), provides special rules for disaster losses in specified areas attributable to Harvey, Irma, or Maria.
- A "net disaster loss"
  - Is deductible only to extent it exceeds $500 (rather than normal $100)
  - Is deductible without regard to normal 10% of AGI threshold.
  - Is deductible by those who do not itemize—standard deduction increased
- Example:
  - Individual has AGI of $90,000, loss from theft of car of $10,000 (not disaster-related), and $50,000 net disaster loss from hurricane.
  - Theft loss deductible is $900 ($10,000 less $100 less 10% of AGI)
  - Net disaster loss deductible is $49,500 ($50,000 less $500)
- Net disaster loss: amount by which "qualified disaster-related personal casualty losses" exceed personal casualty gains
  - Generally, a casualty loss attributable to the hurricane that arises in the disaster area on or after 8/23 (Harvey), 9/4 (Irma), or 9/16 (Maria)

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Casualty Losses of Wildfire Survivors
Biparisan Budget Act of 2018 (2/9/18)
Outline: item D.1.c, page 9

- The Bipartisan Budget Act of 2018, § 20104(c), Pub. L. No. 115-123 (2/9/18), provides special rules for disaster losses in specified areas attributable to California wildfires.
- A "net disaster loss"
  - Is deductible only to extent it exceeds $500 (rather than normal $100)
  - Is deductible without regard to normal 10% of AGI threshold.
  - Is deductible by those who do not itemize—standard deduction increased
- Example:
  - Individual has AGI of $90,000, loss from theft of car of $10,000 (not disaster-related), and $50,000 net disaster loss from hurricane.
  - Theft loss deductible is $900 ($10,000 less $100 less 10% of AGI)
  - Net disaster loss deductible is $49,500 ($50,000 less $500)
- <u>Net disaster loss</u>: amount by which "qualified disaster-related personal casualty losses" exceed personal casualty gains
  - Generally, a casualty loss attributable to the wildfires arose in the disaster area on or after 10/8/17.

Use of Prior-Year Earned Income for EITC and CTC
2017 Disaster Relief Act (9/29/17)
Outline: item D.2, page 9

- The Disaster Relief and Airport and Airway Extension Act of 2017, § 504(c), Pub. L. No. 115-63 (9/29/17):
  - Permits a "qualified individual" to elect to use prior-year earned income for purposes of determining eligibility for the earned income tax credit (§ 32) and child tax credit (§ 24) .
- Available to qualified individuals whose earned income for the tax year that includes a specified date is lower than the preceding year.
  - Specified dates are 8/23/17 (Harvey), 9/4/17 (Irma), 9/16/17 (Maria)
- Election applies to both credits (cannot choose)
- Election is available to joint filers if either spouse is a qualified individual
  - In this case, prior-year earned income is combined earned income.
- <u>Qualified individual</u>: individual whose principal place of abode on 8/23/17 was (1) in Hurricane Harvey disaster *zone*, or (2) outside disaster zone, but within Hurricane Harvey disaster *area* if was displaced by the hurricane. (Similar definitions apply for Irma and Maria.)

Use of Prior-Year Earned Income for EITC and CTC Bipartisan Budget Act of 2018 (2/9/18) *Outline: item D.2.a, page 9*

- The Bipartisan Budget Act of 2018, § 20104(c), Pub. L. No. 115-123 (2/9/18):
  - Permits a "qualified individual" to elect to use prior-year earned income for purposes of determining eligibility for the earned income tax credit (§ 32) and child tax credit (§ 24) .
- Available to qualified individuals whose earned income for the tax year that includes any portion of period from 10/8/17 through 12/32/17 is lower than the preceding year.
- Election applies to both credits (cannot choose)
- Election is available to joint filers if either spouse is a qualified individual
  - In this case, prior-year earned income is combined earned income.
- <u>Qualified individual</u>: individual whose principal place of abode during any period from 10/8/17 through 12/31/17 was (1) in the California wildfire disaster *zone*, or (2) outside disaster zone, but within California wildfire disaster *area* if was displaced by the wildfires.

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Selected Highlights—Bipartisan Budget Act of 2018

- Mortgage insurance premiums
  - The legislation retroactively extended through 2017 the § 163(h)(3)(E) deduction for mortgage insurance premiums [item 3, p.10]
- Qualified tuition and related expenses
  - The legislation retroactively extended through 2017 the § 222 above the line deduction for qualified tuition and related expenses [item 4, p.10]
- Retroactive extension through 2017 of credits for energy efficiency [item 5, pp.10-11]

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Selected Highlights of the Tax Cuts and Jobs Act

- Partnerships
  - Three-year holding period for carried interests **[p. 11, B.1]**
    - Notice 2018-38 (3/1/18) – "Corporations" does not include S corporations.

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Other Developments

- T.D. 9829 [page 15]
- Fees for installment agreements [page 16]
- Camara v. Commissioner, 149 T.C. No. 13 (9/28/17) [page 18]
- Withholding guidance [pages 19-20]
- Martin v. Commissioner, 140 T.C. No. 12 (9/27/17) [page 20]

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