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TAX SECTION
STATE BAR OF TEXAS

www.texastaxsection.org

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Dear Fellow Tax Section Members:

We are near the end of our fiscal year and the Tax Section is busy, busy. The Section continues to offer a wide variety of programs, events, committees and publications for the benefit of its amazing members. Here is a recap of a few recent and pending developments.

Tax Section Annual Meeting

The Tax Section Annual Meeting is June 13 and 14, 2019 in Austin, TX at the JW Marriot. If you have not already registered, you may do so on our website at https://www.texasbar.com. The Annual Meeting is a great opportunity to network with other tax lawyers throughout the state of Texas and to catch up on recent developments in the tax law. We will host a networking happy hour on Thursday, June 13, 2019, at the Austin JW Marriott, from 5:00 p.m.–7:00 p.m. The happy hour is open to all Tax Section members, and I look forward to seeing many of you there. This year **Bill Elliot** will interview Tax Legend **Larry Campagna** of Chamberlain Hrdlicka. For this year's Annual Meeting we have an outstanding lineup of speakers for you including former IRS Commissioner Larry Gibbs, Tax Court Judge Elizabeth Copeland, and our first ever Federal Income Tax update with Professor Bruce McGovern and Professor Cass Brewer. We hope to see you all at our Annual Meeting!

Pro Bono Committee

Thank you for all you do during the Tax Court Calendar Calls and for teaching those individuals on the army bases how to help the soldiers prepare their individual income tax returns.

Committee on Governmental Submissions

The Committee on Governmental Submissions had some quality comments this year. Committees on General Tax, Partnership and Real Estate and Corporate Tax are working on another comment on Opportunity Zones. Thank you to **Chris Goodrich**, **Brandon Jones**, **Nathan Smithson**, and **Jeff Blair** for working on that comment. The Pro Bono Committee recently received some press on their Limited Appearance Tax Court Procedure comment. Thank you to, **Bob Probasco**, **Jason Freeman**, **Rachael Rubenstein**, **Juan Vasquez, Jr.**, and **Richard Hunn** for their work on the Tax Court Procedure Comment . Thank you to COGS Chairs **Henry Talavera**, **Jeff Blair**, **Ira Lipstet**, and **Jason Freeman**. Thank you to all those who participated on the committee.

CLE This Year

I continue to receive positive feedback from folks on the "**First Wednesday Tax Update**" webcast series. The webcasts are offered the first Wednesday of each month (barring a holiday) and always focus on Recent Developments in Federal Income Taxation, and are presented by **Bruce McGovern**, Professor of Law and Director, Tax Clinic, South Texas College of Law Houston (and may occasionally include other guest speakers).

We had another successful Property Tax Seminar in Austin Texas thanks to the hard work of **Braden Metcalf** and **Danny Smith** who have endless energy and knowledge of their field. The Tax Section offered another important Advanced Tax Workshop Program, un-taped, in depth, interactive seminar focusing on one topic. This year the Tax Section partnered with the Texas Comptroller, private practitioners, and industry leaders to present a deep dive into *South Dakota v. Wayfair*. Many thanks to **Dan Baucum** for his leadership in putting together another Advanced Tax Law Seminar this year. Dan Baucum had help from **Christi Mondrik** and **Charolette Noel**.

Outstanding Texas Tax Lawyer

Each year the Tax Section issues the Outstanding Texas Tax Lawyer Award to tax attorneys whose achievements demonstrate satisfaction of the rigorous substantive standards specified in our by-laws. **William Caudill** of Norton Rose Fulbright and Professor **William P. Streng** of the University of Houston Law Center who were both nominated by many fellow attorneys, were both selected by the Officers and Council this year. We will present their awards at the Annual Meeting Speakers' Dinner on June 13, 2019 in Austin, Texas. Please congratulate Bill Caudill and Professor Bill Streng on this honor if you see either of these outstanding gentlemen.

Scholarship Recipients

Each year the Tax Section issues several scholarships to deserving law students who are selected from among qualifying candidates. The deadline for submitting scholarships was April 6, 2019. The Law School Liaison Task Force received 19 applications from students at 10 law schools. Recipients of the scholarships will be recognized at the Annual Meeting Speakers' Dinner on June 13, 2019 in Austin, Texas. Many thanks to **Stephen Long** for his hard work and dedication to this fantastic program. Many thanks to the graders of the applications. Congratulations to our winners this year who are: Kathryn Torres, Cody Wilson, Luis Leos, and Stephanie Grissom.

Leadership Academy

I am excited to report the Tax Section has a wonderful leadership class for this 2019/2020 year. These bright up-and-coming tax professionals are: Ira Aghai, Aaron P. Borden, Shannon R. Brandt, Carolyn Chachere, Brian A. Clark, Stuart H. Clements, Blair M. Green, Christopher Wayne James, Julio Mendoza-Quiroz, Mark A. McMillan, Adrian Ochoa, Ryan D. Phelps, John D. Portnow, Joshua D. Prywes, John B. Reyna, Jameson Sauseda, Austen L. Unzeitig, Joshua S. Veith, Hersh M. Verma, and Sarah Woodberry. Many thanks to **Rob Morris** for leading the new recruits and thank you to all the speakers for their time in supporting the program.

Special Thanks

As my tenure as Chair of the Tax Section comes to an end, I would like to recognize and give special thanks to the many outstanding tax lawyers who make the Tax Section great. I would like to thank **Stephanie Schroepfer** and all the partners of Norton Rose Fulbright for graciously hosting the Tax Section meetings this year. We are so grateful for your hospitality. Thank you so much for the support and wisdom of **Elizabeth Copeland**, **Alyson Outenreath, Tina Green, Mary McNulty,** the Officers, **Charolette Noel**, **Christi Mondrik**, **Lora Davis**, and **Dan Baucum,** Council Members, Committee Chairs and Vice Chairs, project leaders, and everyone else involved with the Tax Section who tirelessly give their time, energy and resources to the various activities of the Tax Section. I would also like to thank **Gwen Fulcher**, **Jesse Gustin**, and **Anthony Airola** of Norton Rose Fulbright who were essential supporters of all our meetings this year. I look forward to recognizing many of the Tax Section's outstanding leaders at the Tax Section Annual Meeting on June 14, 2019. I would also like to thank **Anne Schwartz**, the Tax Section Administrator, and **Tracy Nuckols** from the State Bar for their endless help this year.

Join a Committee

We have an active set of committees, both substantive and procedural. Our substantive committees are: Corporate Tax, Employee Benefits, Energy and Natural Resources, Estate and Gift Tax, General Tax Issues, International Tax, Partnership and Real Estate, Property Tax, Solo and Small Firm, State and Local Tax, Tax Controversy, Tax- Exempt Finance, and Tax-Exempt Organizations. In addition, our procedural committees include: the Committee on Governmental Submissions, Annual Meeting Planning Committee, Continuing Legal Education Committee, Newsletter Committee, Tax Law in a Day Committee, Law School Outreach and Sponsorship Committee.

Any members interested in joining a committee may do so by visiting our website at www.texastaxsection.org.

Contact Information

Below is my contact information as well as the contact information for our Tax Section Administrator, Anne Schwartz, if anyone would like additional information:

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Thank you to **Michelle Spiegel** for all the patience she shows to all of us in putting together this publication three times a year!

Outstanding Texas Tax Lawyer Award 2019

William H. Caudill

William H. Caudill has been one of Texas's leading tax attorneys for decades. A fourth-generation Texan and partner at Norton Rose Fulbright since 1986, Bill is an expert in a wide variety of tax topics, including partnerships, oil and gas, real estate, and tax-exempt organizations just to name a few.

Bill received his J.D. with high honors from the University of Texas at Austin, where he was on Law Review, a chancellor, and a member of the Order of the Coif. He received his Masters degree in public accounting from the University of Texas at Austin Graduate School of Business (Dean's Award for Academic Excellence), and his B.S.B.A. with high honors from the University of Arkansas. Bill is also a Certified Public Accountant.

A prodigious speaker and writer, Bill has spoken at dozens of events and authored many articles over his career. He has given significantly of his time to the tax profession, and is a member of an elite group of three attorneys who have served as both Chair of the Section of Taxation of the American Bar Association (2016-2017) and Chair of the State Bar of Texas Tax Section (1991-1992).

Bill has been tirelessly devoted to the Houston community through involvement with his church, the Boy Scouts of America, the Mary Christian Burleson House Preservation and Development Foundation, and as outside general counsel to the Greater Houston Community Foundation, among other activities.

Bill has a warmth and ease about him that he extends to his clients as well as the attorneys he has mentored over the years. His partners have referred to him as "a guru of partnership tax," and as Tax Legend and former Outstanding Texas Tax Lawyer Award recipient Charles W. Hall has said, "Bill Caudill is particularly well-known for his tax expertise regarding tax exempt organizations, oil and gas, and partnerships. His expertise goes beyond that, though. He has an incredible breadth of knowledge across the entire spectrum of tax law, and also he has a great knowledge of law generally beyond tax. More importantly, he is a splendid human being and a wonderful friend."

Thank you, Bill for your significant contributions to our field. We are grateful for all you have done and continue to do for our practice. Congratulations on this well-deserved honor!

Outstanding Texas Tax Lawyer Award 2019

William P. Streng

Bill Streng grew up in Iowa, but he has left a lasting mark on Texas and the nation. Bill graduated from Northwestern University School of Law in 1962. He served as an Attorney-Advisor in the Office of the Assistant Secretary for Tax Policy (Office of Tax Legislative Counsel) in United States Department of the Treasury. He began his career in academia as a faculty member with tenure at the Southern Methodist University School of Law. Bill then became of counsel at Bracewell & Patterson and remained affiliated with that firm for sixteen years. He moved to the University of Houston Law Center as a tenured professor of law in 1985. Bill has been instrumental in guiding tax law at UHLC from that point until his retirement from UHLC this year.

Bill Streng was one of the first co-authors with Boris Bittker, and he has authored or co-authored leading treatises in the areas of estate planning, corporate taxation, and international taxation. Few academics have published on as broad a spectrum of the tax law as Bill Streng. His reputation as a leading academic in tax law is internationally recognized. He was a Fulbright Scholar in 1993, and he has been invited to speak or teach throughout Europe in the Netherlands, Sweden, and other countries. In Asia, he has regularly taught in tax programs in Taiwan, Hong Kong, and New Zealand. Bill Streng has been a non-European member of the European Association of Tax Law Professors since 2002, and he has been a member of the American Law Institute since 1982. He has been a U.S. Branch Council Member of the International Fiscal Association since 1977.

Bill Streng has left a lasting mark on the tax profession in this state. He has educated tax professionals in this state since 1973, and literally thousands of tax professionals have been impacted by his mentorship and teaching over that period of time. Countless students indicate and recall fondly how Bill Streng was instrumental in their entering the tax profession. He has been a leading educator in taxation for many of the tax professionals in this state. In addition, Bill's generosity is well-known and legendary. Bill has always been generous both in terms of his time and in providing resources to other teachers, educators, and professionals around this state. He has also been an active force for providing continuing education lectures in Texas for forty-six years. He is a true Texas legend.

TAX SECTION
STATE BAR OF TEXAS

2019 Annual Meeting
Austin, June 14, 2019
CLE Hours 6.5. Course # 174046503
CPE Hours 7.5 • Sponsor ID #135
Wifi Network: SBOT2019 • Password: CapitalOne

8:00-8:30 **Registration and Breakfast**

8:30-9:15 **Section Membership Meeting and Awards**

9:15-10:00 **The United States of America, Our National Debt, Our Annual Deficits and the Increasing Risks They Pose and What Can Be Done About Them?** *.75 hour*

Lawrence B. Gibbs, *Washington, D.C.*
Senior Council – Miller & Chevalier; Former IRS Commissioner

10:00-10:15 **Break**

10:15–11:15 **Federal Tax Update** *1 hour*

Prof. Cassady V. (Cass) Brewer, *Atlanta, GA*
Georgia State University College of Law

Prof. Bruce McGovern, *Houston*
South Texas College of Law

11:15-12:00 **Penalties Above 20%: What Are They, When Are They Applied, and How Do You Defend?**
.75 hour

Hon. Elizabeth A. Copeland, *Washington, D.C.*
U.S. Tax Court

12:00--12:30 **Buffet Luncheon Served** (Ticket Required)

12:30 -1:30 **Lunch Session: Interview of Larry A. Campagna** *1 hour*

William D. (Bill) Elliott, *Dallas*
Elliott Thomason & Gibson

1:30-1:45 **Break**

1:45-2:45 **It Still Takes A Village: Balancing Professionalism, Privileges and Advocacy in Tax Controversies**
1 hour

Larry A. Campagna, *Houston*
Chamberlain Hrdlicka

2:45-3:45 **South Dakota V. Wayfair Where Are We Now?**
1 hour

Nancy L. Prosser, *Dallas*
Chief Counsel for the Texas Comptroller of Public Accounts

Sam Megally, *Dallas*
Partner, K&L Gates, LLP

3:45- 4:00 **Break (Mid Afternoon Snack)**

4:00-5:00 **The Latest and the Greatest in Property Tax**
1 hour

Moderator:

Braden W. Metcalf, *Dallas*
Jackson, Dillard, Hager & Smith

Panelists:

Marya Crigler, *Austin*
Chief Appraiser of Travis County Appraisal District Office

John Brusniak, Jr., *Dallas*
Brusniak, Turner Fine LLP
Former Chair, Texas Tax Section

THOMPSON & KNIGHT LLP
Q&AS RELATED TO THE
NEW QUALIFIED OPPORTUNITY ZONE
PROPOSED REGULATIONS

BY: KATHLEEN GERBER AND JANA B. WIGHT

The Tax Cuts and Jobs Act of 2017 (the "TCJA") added two new provisions in the Internal Revenue Code of 1986, as amended (the "Code"), which together create federal tax incentives for investing in economically distressed areas referred to as "qualified opportunity zones" or "QOZs".[1] An initial set of Proposed Regulations providing further guidance on these rules was released on October 19, 2018. These Proposed Regulations provided much needed guidance, but also created additional questions and uncertainties. On April 17, 2019, a second set of Proposed Regulations was issued, addressing additional issues and also modifying certain aspects of the first set of Proposed Regulations. The Q&As that follow this brief introduction to the QOZ rules address some of the most common questions asked about how this new tax incentive program works and the answers provided in the recently published second set of Proposed Regulations.

OVERVIEW OF THE OPPORTUNITY ZONE RULES

A QOZ is an economically distressed census tract that (i) meets the requirements of Section 1400Z-1 of the Code, (ii) has been duly nominated by a Governor of the state within which the census tract lies (or, in the case of census tracts within Washington, D.C., by the mayor of Washington, D.C.), and (iii) is certified by the Treasury Department. After the enactment of the TCJA, U.S. governors and the mayor of Washington, D.C. were given until April 2018 to nominate qualifying census tracts in their jurisdictions for QOZ certification. To date, approximately 8,700 QOZs have been certified by the Treasury Department. A list of the QOZs is available at: https://www.cdfifund.gov/pages/opportunity-zones.aspx.

Investors gain several tax benefits if they elect to rollover capital gains realized after December 31, 2017 into a qualified opportunity fund (a "QO Fund"). To qualify for these tax benefits, all or a portion of the realized capital gain must be invested in a QO Fund within 180 days of the date the gains are realized (subject to certain exceptions for gains realized through a partnership or S corporation and gains treated as capital gain under Section 1231 of the Code). The federal tax benefits available to taxpayers that invest in QO Funds are:

i) A deferral of tax on the invested capital gains until the earlier of December 31, 2026 or the date the taxpayer sells or exchanges the QO Fund investment;
ii) A reduction of tax on the invested capital gains if the taxpayer holds the QO Fund investment for a set period of time; and
iii) The elimination of tax on any gains realized from an investment in a QO Fund (*i.e.*, in excess of the deferred capital gains) if the investment is held for ten or more years.

[1] *See* Sections 1400Z-1 and 1400Z-2 of the Code.

To qualify as a QO Fund, at least 90% of a QO Fund's assets must be qualified opportunity zone property ("Qualified Opportunity Zone Property"). This is commonly referred to as the "90% Test". Qualified Opportunity Zone Property includes both direct interests in qualified opportunity zone business property, as defined in Section 1400Z-2(d)(2)(D) ("Qualified Opportunity Zone Business Property"), and indirect interests in such property through ownership of qualified opportunity zone stock, as defined in Section 1400Z-2(d)(2)(B) of the Code ("Qualified Opportunity Zone Business Stock") or qualified opportunity zone business partnership interests, as defined in Section 1400Z-2(d)(2)(C) of the Code ("Qualified Opportunity Zone Business Partnership Interests"). Qualified Opportunity Zone Business Property is tangible property used in a trade or business of a QO Fund if (i) the property was acquired by the QO Fund by purchase after December 31, 2017, (ii) the original use of such property in the QOZ commences with the QO Fund or the QO Fund substantially improves the property, and (iii) during substantially all of the QO Fund's holding period for such property, substantially all of the use of such property was in a QOZ.[2]

a. Direct Investment by a QO Fund

If a QO Fund chooses to own and develop Qualified Opportunity Zone Business Property directly, the property will qualify as Qualified Opportunity Zone Business Property as long as the QO Fund uses the properties in a trade or business, the QO Fund meets the original use or substantial improvement requirement, and during all of the QO Fund's holding period in such properties substantially all of it is located in a QOZ.

b. Indirect Investment by a QO Fund

A QO Fund may instead invest in Qualified Opportunity Zone Business Property indirectly through its ownership of stock or a partnership interest in a Qualified Opportunity Zone Business.[3] A Qualified Opportunity Zone Business is a trade or business that meets the following three requirements: (i) substantially all of the tangible property owned or leased by the business is Qualified Opportunity Zone Business Property; (ii) the trade or business satisfies the requirements of Section 1397C(b)(2), (4), and (8) of the Code; and (iii) the trade or business is not one of the prohibited "sin" businesses described in Section 144(c)(6)(B) of the Code.

For purposes of the first requirement, the Proposed Regulations provide that the "substantially all" requirement is satisfied if at least 70% of the tangible property owned or leased by the trade or business is Qualified Opportunity Zone Business Property (the "70% Test").

For purposes of the second requirement, Section 1397C(b)(2), (4), and (8) of the Code require that: (i) at least 50% of the total gross income be derived from the active conduct of the QOZ trade or business (the "50% Test"); (ii) a substantial portion of the intangible property be used in the active conduct of such trade or business; and (iii) less than 5% of the average of the aggregate unadjusted bases of the property of the trade or business can be attributable to nonqualified financial property (the "NQFP Limit"). Section 1379C of the Code defines

[2] Section 1400Z-2(d)(2)(D) of the Code.

[3] The Proposed Regulations clarify that a Qualified Opportunity Fund can invest in a business that is organized as a limited liability company and is treated as a corporation or a partnership for U.S. federal income tax purposes.

nonqualified financial property as including debt, stock, partnership interests, options, futures contracts, forward contracts, warrants, notional principal contracts, annuities, and other similar property but excluding reasonable amounts of working capital held in cash, cash equivalents, or debt instruments with a term of 18 months or less. Solely for purposes of applying the NQFP Limit, Prop. Reg. Section 1.1400Z-2(d)-1(d)(5)(iv) provides a safe harbor that expands the definition of reasonable working capital to include amounts designated in writing for the acquisition, construction, and/or substantial improvement of tangible property in a QOZ if (i) there is a written schedule consistent with an ordinary start-up of a trade or business for the expenditure of the working capital assets; (ii) the working capital assets are expended within 31 months of the receipt by the business of such assets under that schedule; and (iii) the working capital assets are actually used in a manner consistent with such written designation and schedule. Further, Prop. Reg. Section 1.1400Z-2(d)-1(d)(5)(v), (vi), and (vii) provide that (i) any gross income received from amounts treated as reasonable working capital under this safe harbor will be treated as gross income that counts toward the satisfaction of the 50% Test; (ii) intangible property will be treated as being used in the trade or business during any period in which the business is proceeding to expend working capital pursuant to the schedule permitted under the working capital safe harbor; and (iii) if some financial property is treated as reasonable working capital under the safe harbor, and if the tangible property being improved is expected to satisfy the substantial improvement requirement, then the tangible property is not treated as failing to satisfy the substantial improvement requirement solely because the scheduled consumption of the working capital is not yet complete.

For purposes of the third requirement, the prohibited "sin" businesses listed in Section 144(c)(6)(B) of the Code are: (i) private or commercial golf courses or country clubs; (ii) massage parlors; (iii) hot tub facilities; (iv) suntan facilities; (v) racetracks or other gambling facilities; and (vi) any store the principal business of which is the sale of alcoholic beverages for consumption off premises.

Q&As

1. What does "substantially all" mean in each of the various places where it appears in Section 1400Z-2 of the Code?

The definition of "substantially all" is used in multiple places within Section 1400Z-2 of the Code and is critical to establishing when property qualifies as Qualified Opportunity Zone Business Property, Qualified Opportunity Business Stock or Qualified Opportunity Business Partnership Interest. For example, substantially all of the tangible property owned or leased by a Qualified Opportunity Zone Business must be Qualified Opportunity Zone Business Property. The first set of Proposed Regulations clarified that for these purposes "substantially all" means at least 70%. To qualify as Qualified Opportunity Zone Business Property, substantially all of such property must be used in a trade or business in a QOZ. The second set of Proposed Regulations provide that for these purposes "substantially all" means at least 70% of the use of such property must be in a QOZ.[4] During substantially all of a QO Fund's holding period in Qualified Opportunity Zone Business Property, such property must qualify as such, and during substantially

[4] Prop. Reg. Section 1.1400Z2(d)-1(c)(6).

all of a QO Fund's holding period in a Qualified Opportunity Zone Business, such business must qualify as such. The second set of Proposed Regulations provides that for purposes of these holding period requirements, "substantially all" means 90%.[5] The preamble to the second set of Proposed Regulations explains that the reasoning for the higher threshold for holding period purposes was due to the fact that a taxpayer has the ability to "control and determine the period for which they hold property."

2. How has the "original use" requirement been modified by the second set of Proposed Regulations?

Generally, the "original use" of tangible property acquired by purchase commences on the date when that acquirer or any prior owner first places the property in service in a QOZ for depreciation or amortization purposes.[6] Thus, if tangible property located in a QOZ was previously depreciated by a taxpayer other than the QO Fund or Qualified Opportunity Zone Business, the original use requirement cannot be satisfied. Instead, a QO Fund or Qualified Opportunity Zone Business must substantially improve the property.

Notwithstanding this general rule, Prop. Treas. Reg. Section 1400Z2(d)-1(c)(7) permits buildings or structures that were previously placed in service within a QOZ to be disregarded for purposes of the original use requirement if the building or structure has not been utilized for five years or has been abandoned for five years.

Land is treated as Qualified Opportunity Zone Business Property only if it is treated as used in a trade or business within the meaning of Section 162 of the Code by a QO Fund or a Qualified Opportunity Zone Business. The preamble to the Proposed Regulations acknowledges that this provision can be abused if a QO Fund or Qualified Opportunity Zone Business does not invest any new capital or increase the economic activity or output of the land. Thus, an anti-abuse provision in Prop. Treas. Reg. Section 1.1400Z2(f)-1 will apply in such situations to treat the acquisition of the land as an acquisition of non-qualifying property for Section 1400Z-2 purposes.

3. When will leased tangible property satisfy the requirements of the 90% Test?

Leased tangible property meeting certain criteria may be treated as Qualified Opportunity Zone Business Property for purposes of satisfying the 90% Test. To satisfy the 90% Test, the leased tangible property must be acquired under a lease entered into after December 31, 2017[7] and substantially all of the use of the leased tangible property must be in a QOZ during substantially all of the period for which the trade or business leases the property.[8]

Each lease which a QO Fund or Qualified Opportunity Zone Business acquires with respect to tangible property must be a "market rate lease."[9] Further if the lessor and lessee are related, the

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[5] Prop. Reg. Section 1.1400Z2(d)-1(c)(5).
[6] Prop. Reg. Section 1.1400Z2(d)-1(c)(7)(i).
[7] Prop. Reg. Section 1.1400Z2(d)-1(c)(4)(B)(1).
[8] Prop. Reg. Section 1.1400Z2(d)-1(c)(4)(D).
[9] Prop. Reg. Section 1.1400Z2(d)-1(c)(4)(B)(2).

Proposed Regulations do not permit leased tangible property to be treated as Qualified Opportunity Zone Business Property if, in connection with the lease, a QO Fund or Qualified Opportunity Zone Business at any time makes a prepayment to the lessor (or a person related to the lessor) relating to a period of use of the leased tangible property that exceeds twelve months.[10]

4. When is the 50% of gross income requirement satisfied?

A Qualified Opportunity Zone Business must derive at least 50% of its total gross income from the active conduct of a business within a QOZ. The second set of Proposed Regulations provide three safe harbors and a facts and circumstances test to determine whether sufficient gross income is derived from a trade or business within a QOZ. The safe harbors and facts and circumstances test are set out in the Proposed Regulations as follows:

i) Based on the hours spent by the employees and independent contractors, 50% of the services performed for such trade or business by its employees and independent contractors are performed within the QOZ.[11]
ii) Based on the amounts paid for the services performed by the employees and independent contractors, 50% of the services performed for the business by its employees or independent contractors are performed within the QOZ.[12]
iii) The tangible property of the trade or business that is in the QOZ and the management or operational functions performed for the business in the QOZ are each necessary to generate 50% of the gross income of h trade or business.[13]
iv) Based on the facts and circumstances, at least 50% of the gross income of a trade or business is derived from the active conduct of a trade or business in the QOZ.[14]

5. How are Section 1231 gains treated under Section 1400Z-2 of the Code?

Prop. Treas. Reg. Section 1.1400Z2(a)-1(b)(2)(iii) provides that gain treated as long-term capital gain pursuant to Section 1231 of the Code is eligible gain for purposes of Section 1400Z-2 of the Code. Section 1231 of the Code provides that if a taxpayer realizes a net gain from sales or exchanges of depreciable property used in a trade or business held over one year ("Section 1231 Property") during the taxable year, such gain is treated as long-term capital gain, and if a taxpayer realizes a net loss from sales or exchanges of Section 1231 Property during the taxable year, such loss is treated as ordinary loss. Since a taxpayer cannot know whether a gain realized from a single sale or exchange of Section 1231 Property will qualify for long-term capital gain treatment under Section 1231 of the Code until all such gains and losses are netted at the end of the tax year, the

[10] Prop. Reg. Section 1.1400Z2(d)-1(c)(4)(B)(3), (4) and (5). Furthermore, if the original use of leased tangible personal property in a QOZ does not commence with the lessee, the property is not Qualified Opportunity Zone Business Property unless, the lessee becomes the owner of tangible property that is Qualified Opportunity Zone Business Property having a value not less than the value of that leased tangible personal property.
[11] Prop. Reg. Section 1.1400Z2(d)-1(d)(5)(i)(A).
[12] Prop. Reg. Section 1.1400Z2(d)-1(d)(5)(i)(B).
[13] Prop. Reg. Section 1.1400Z2(d)-1(d)(5)(i)(C).
[14] Prop. Reg. Section 1.1400Z2(d)-1(d)(5)(i)(D).

Proposed Regulations provide that the 180-day period to re-invest such amounts will not begin until the last day of the taxable year.

6. Do cash and cash equivalents contributed to a QO Fund immediately count as non-qualifying assets for purposes of the 90% Test?

No. The second set of Proposed Regulations allow a QO Fund to apply the 90% Test without taking into account any investments received in the preceding six months, provided that such newly contributed assets are held in cash, cash equivalents or debt instruments with term 18 months or less.[15]

7. How are mixed investments in a QO Fund treated?

The Proposed Regulations acknowledge the need for regulations surrounding mixed funds investments in a QO Fund when a partner contributes tangible property to a QO Fund with a value in excess of its basis or cash in excess of the person's eligible gain under Section 1400Z-2 or where a person receives a partnership interest in exchange for services. Section 1400Z-2(e)(1) of the Code provides that only the portion of investment in a QO Fund to which an election under Section 1400Z-2(a) of the Code is in effect is treated as a qualifying investment. Under this rule, the share of gain attributable to the excess investment and/or the service component of the interest in the QO Fund is not eligible for the various benefits afforded to the qualifying investments under Code Section 1400Z-2.

The Proposed Regulations provide that generally a partner holding mixed funds investment will be treated as holding a single partnership interest with a single basis and capital account for all partnership purposes. However, solely for purposes of Section 1400Z-2 of the Code, the mixed funds partner will be treated as holding two interests, and all partnership items, such as income and debt allocations and property distributions, will be allocated between those two interests based on the relative percentages of each interest.

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[15] Prop. Reg. Section 1.1400Z2(d)-1(b)(4).

U.S. Supreme Court to hear *Kaestner* trust tax nexus case

INSIGHT ARTICLE | February 19, 2019

The U.S. Supreme Court will revisit state tax nexus for the second year in a row after granting North Carolina's petition for certiorari in *North Carolina Department of Revenue v. The Kimberley Rice Kaestner 1992 Family Trust* (Docket No. 18-457). Recall that last summer, the Court issued its opinion in *South Dakota v. Wayfair*, which eliminated the physical presence nexus requirement set forth in *Quill v. North Dakota*. In *Wayfair*, the Court found that a more than de minimis economic presence, based on volume or value of sales to in-state customers, was enough to satisfy the "substantial nexus" requirement of the four-part Commerce Clause test established under *Complete Auto Transit, Inc. v. Brady*.

While *Wayfair* provided some clarity on state tax nexus under the Commerce Clause of the U.S. Constitution, it did not address or eliminate the purposeful availment requirement of the Due Process Clause. In 1992, *Quill* found that due process concerns of fairness are satisfied when the out-of-state taxpayer "purposely avails itself" of the benefits of the forum state. On appeal to the U.S. Supreme Court, *Kaestner* asks whether due process prohibits states from taxing trusts based on the in-state residency of a nonresident trust beneficiary.

Background

In 1992, Joseph Lee Rice, III, a New York resident, established a trust as the settlor (creator) under New York law for the benefit of his descendants. The trustee was also a New York resident at the time the trust was created, and a Connecticut resident during the tax periods at issue. The trust was subsequently divided into three separate share trusts, one of which was the Kimberley Rice Kaestner 1992 Family Trust (the Trust). The Trust's beneficiary, Kimberley Rice Kaestner (daughter to the settlor), had no connection to North Carolina until she moved to the state in 1997.

Throughout the periods at issue, Ms. Kaestner received no distributions from the Trust and was not aware of its existence until after moving to the state. Additionally, no funds were distributed during the periods, and she had no right to withdraw assets because distributions were at the sole discretion of the trustee. All the Trust's assets were located outside North Carolina, while the custodian of those assets resided in Boston, Massachusetts. All of the business of the Trust took place in New York, where the tax returns and accountings were prepared. The beneficiaries had no role in the management or investment decisions of the Trust. The only connection between the Trust and North Carolina was that Ms. Kaestner resided in the state for the periods in question.

The challenge

During tax years 2005 through 2008, North Carolina taxed all the worldwide income of the Trust on the basis that Ms. Kaestner, the sole beneficiary of the Trust, was a resident of the state. Under North Carolina law, the tax imposed on a trust is computed on the amount of taxable income of the trust that is for the benefit of a resident of North Carolina (see N.C. Gen. Stat. section 105-160.2), regardless of whether any of that income is actually distributed to North Carolina beneficiaries. The Trust subsequently sought a $1.3 million refund from the North Carolina Department of Revenue. The department denied the refund request, and the Trust filed a complaint in the Wake County Superior Court, alleging that the tax was unconstitutional. The Trust prevailed in that court, and again on appeal to an appellate court, both of which found that the tax as applied to the Trust was unconstitutional under the Due Process Clause.

On appeal to the North Carolina Supreme Court, the state argued that the Trust had the requisite minimum contacts with North Carolina through the residency of the beneficiary, Ms. Kaestner, sufficient to satisfy the Due Process Clause of the U.S. and State Constitutions. The Court, in explaining due process as applied to taxation, noted that there must be some definite link, some minimum connection, between a state and the person, property or transaction (the Trust in this case) it seeks to tax. Accordingly, the Court found that a beneficiary living in the state did not create the necessary minimum contacts required under due process solely based on a beneficiary availing themselves of the benefits and protections of North Carolina law to subject the Trust to tax.

It should be noted that section 105-160.2 was not ruled unconstitutional on its face, and that the decision was limited to its application to the facts of the case. Although the lowermost court also found the provision violated the Commerce Clause, neither the appellate court nor the state Supreme Court addressed those claims.

On Jan. 11, 2019, the U.S. Supreme Court granted the state's petition for certiorari. Argument is scheduled for April 16, 2019.

Added complexity

The Minnesota Department of Revenue recently petitioned the U.S. Supreme Court to hear another due process-related trust taxation issue in *Fielding v. Commissioner of Revenue*. In *Fielding*, the Minnesota Supreme Court held that Minnesota's grantor-domicile rule, as applied to trusts that had only "extremely tenuous" contacts with Minnesota, was unconstitutional under the Due Process Clause. That Court found that the relevant Minnesota connections were to the trustee, not to the

Minnesota grantor who established the trust at an earlier time. The U.S. Supreme Court may decide to combine *Fielding* with *Kaestner* to address the due process issues simultaneously.

Takeaways

Kaestner and *Fielding* could have significant implications on the state taxation of trusts. Nonresident trust taxation jurisdiction provisions are not limited to North Carolina and Minnesota, as a number of states impose taxes on a trust based upon one or more of these factors:

- The residency of the grantor of the trust at the time the trust became irrevocable (like the Minnesota law)
- The residency of the beneficiary or beneficiaries of the trust (like the North Carolina law)
- The residency of the trustee or trustees of the trust
- The location where the trust is being administered

It is possible, particularly in light of the U.S. Supreme Court's recent state tax decisions, that one or more of these provisions could be found to be unconstitutional and/or the Court could set out a unified jurisdictional standard. In the near term, trustees should review their trust residency decisions, and should prepare for the Kaestner decision, as well as the possibility of a U.S. Supreme Court decision in Fielding. A decision in Kaestner is expected by the end of June.

Finally, all multistate taxpayers should prepare for the potential wider-ranging impacts of a U.S. Supreme Court decision regarding how the Due Process Clause applies to state taxes. Particularly given the Court's repudiation of the Quill Commerce Clause analysis and nonstate tax oriented Due Process Clause decisions over the last eight years, it is possible that there could be some broader clarification of the Quill due process minimum contacts approach.

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U.S. Supreme Court hears arguments in Kaestner trust tax nexus case

TAX ALERT | April 19, 2019

ORIGINAL ARTICLE — Feb. 19, 2019: US Supreme Court to hear Kaestner trust tax nexus case

UPDATE — April 19, 2019:

On April 16, 2019, the U.S. Supreme Court heard oral argument in North Carolina Department of Revenue v. The Kimberley Rice Kaestner 1992 Family Trust, the challenge to North Carolina's tax on the undistributed income of a trust earned for the benefit of an in-state resident. The Court, tasked with reviewing a state tax nexus case for the second year in a row, was asked to consider whether the Due Process Clause of the U.S. Constitution prohibited a state from taxing a trust based on a beneficiary's state of residency.

RSM was onsite early to attend in person. While interest in the argument may not have resulted in long lines like last year's historic *South Dakota v. Wayfair*, the courtroom was full of state tax and trust professionals, accountants and attorneys eager to hear the Court explore the multistate taxation of a trust. While fewer attendees were turned away than *Wayfair*, the impact of *Kaestner* could have similarly far-reaching implications to all of state tax.

Oral argument highlights

The North Carolina Solicitor General began the arguments. He asserted that the state's tax on the beneficiary's pro-rata interest in the trust satisfied due process because of all the benefits and protections that states extend to their residents. Justice Ginsburg quickly posed the first question, leading to a lengthy discussion on whether, and how, the beneficiary is sufficiently connected to the trust to support taxing the accumulating trust income. Recall that in this case, the trust beneficiary was a North Carolina resident who received no trust distributions and exercised no control over the trust assets for the period in question.

Several Justices expressed concern that there was no guarantee that the beneficiaries would receive any distribution from the trust as it was based entirely on the trustee's discretion. Justice Breyer noted that "there could be something wrong" with a state taxing the accumulated income of the trust based on a resident beneficiary who may not receive any distribution. Justice Breyer continued questioning the imposition of the tax based on the pro-rata share of beneficiaries residing in the state. He noted that the proportion of beneficiaries in the state may not be representative of the value of the eventual distribution, if any, to the beneficiary.

The Solicitor General reiterated that the state's taxing scheme was fair because trust beneficiaries have true ownership of the accumulating assets, and that the state residents avail themselves of all the services, benefits and protections a state provides to its resident citizens. Later in the argument, Justice Kagan expressed that it did not "make a whole lot of sense" that, between North Carolina and Connecticut (where the trustee resided), the taxing authority for the undistributed growth of the trust should be in a state where no one was benefiting from the income growth, *i.e.*, the trustee was not benefiting from the trust's growth. The Justice indicated that she thought North Carolina had the greater interest in taxation because the beneficiary, who was accumulating wealth in the trust during the periods in question, resided there.

Throughout the hour-long session, a number of other arguments and issues were raised, including counsel for the taxpayer highlighting that the beneficiary had no control over management of the trust's assets. The beneficiary did not have the right to demand trust distributions, while the trustee exercised most, if not all of the control over the trust.

The Justices challenged counsel for both the taxpayer and the state, appearing to express uncertainty over the state's law. However, like most arguments before the Court, there was no clear consensus on how the decision may come down.

Takeaways

Kaestner provides the Court an opportunity to revisit the application of the Due Process Clause in the context of state taxation, the first significant opportunity to do so since *Quill Corp. v. North Dakota* in 1992. Although the challenge is within the context of a state's authority to tax the income of a trust, a broad decision by the Court could have significant implications to other state taxes, including corporate and individual income taxes, and sales and use taxes.

With oral argument complete, a decision is anticipated by the end of June. A transcript of the oral argument is available here.

A similar due process-related trust taxation decision out of Minnesota, *Fielding v. Commissioner of Revenue*, rejected a rule that taxed the trust based on the location of the grantor. *Fielding* is currently on petition to the Court.

For more information on *Kaestner*, please read our article, U.S. Supreme Court to hear Kaestner trust tax nexus case, and reach out to your tax adviser to discuss steps you can take now, before the decision comes down.

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IRS Provides Additional Guidance on Investing in Qualified Opportunity Funds

By Jeffry M. Blair[1]

On December 23, 2017, President Donald Trump signed into law the Tax Cuts and Jobs Act of 2017 (the "TCJA"). Included in the TCJA were Sections 1400Z-1 and 1400Z-2 of the Internal Revenue Code of 1986, as amended (the "Code")[2] that sought to encourage economic growth and investment in designated distressed communities (qualified opportunity zones) by providing Federal income tax benefits to taxpayers who invest new capital in businesses located within qualified opportunity zones through qualified opportunity funds ("QOFs").

Section 1400Z-1 of the Code provides procedural rules for designating qualified opportunity zones and related definitions. Section 1400Z-2 of the Code provides two main tax incentives to encourage investment in qualified opportunity zones. The first incentive allows for certain gains to be deferred from the inclusion in gross income to the extent that a taxpayer elects to invest a corresponding amount in a QOF. [3] The second incentive allows a taxpayer to elect to exclude from gross income the post-acquisition gain on investments in a QOF held for at least 10 years.

Initially, there was great excitement over these new tax incentives. However, due at least in part to a lack of clarity with respect to several aspects of this new tax incentive program, these new tax provisions were not generating the economic growth and investment initially anticipated. On October 29, 2018, in an attempt to clarify some aspects of this program, the Department of Treasury ("Treasury") and the Internal Revenue Service ("IRS") responded by publishing proposed Treasury Regulations under Section 1400Z-2 of the Code to provide additional guidance with respect to investing in qualified opportunity funds (the "2018 Proposed Regulations"). The 2018 Proposed Regulations were very helpful but there were several items that required additional clarification. A public hearing was held on February 14, 2019 and 25 individuals spoke to Treasury and the IRS regarding portions of the 2018 Proposed Regulations that needed clarification or correction. In addition, Treasury and the IRS received several written comments from practitioners and other taxpayers. Treasury and the IRS continues to consider the comments received, including those provided at the public hearing.

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2 All Section references are to the Internal Revenue Code of 1986, as amended (the "Code") unless otherwise indicated.

3 In addition, §1400Z-2 provides that a portion of the deferred gain may be permanently excluded if the corresponding investment in the QOF is held for five or seven years.

On April 17, 2019, Treasury and the IRS issued proposed Treasury Regulations (the "2019 Proposed Regulations") that amend, clarify and provide additional guidance with respect to the Sections 1400Z-1 and 1400Z-2 of the Code and to the 2018 Proposed Regulations. As more fully explained below, the 2019 Proposed Regulations provide additional guidance and clarifications with respect to many aspects of this new qualified opportunity zone tax incentive program, including the qualification of and investment in QOFs, certain aspects of the deferral election, and the type of events that cause the inclusion of deferred gain.[4]

I. Qualified Opportunity Zone Business Property

a. *Definition of Substantially All for Purposes of Sections 1400Z-2(d)(2) and (d)(3)*

To qualify as a QOF, an investment vehicle must: (i) be organized as a corporation or as a partnership for the purpose of investing in qualified opportunity zone property (other than another QOF) and (ii) holds at least 90% of its assets in qualified opportunity zone property.[5] Qualified opportunity zone property includes any qualified opportunity zone stock, qualified opportunity zone partnership interest or qualified opportunity zone business property.[6] Qualified opportunity zone business property is defined as tangible property used in a trade or business of the QOF if: (I) the property was acquired by the qualified opportunity zone business by purchase (as defined in Section 179(d)(2) of the Code) after December 31, 2017, (II) the original use of the property in the qualified opportunity zone began with the QOF or the QOF substantially improved the property, and (III) during substantially all of the QOF's holding period for the property substantially all of the use of the property was in a qualified opportunity zone.[7] Although Code

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4 The 2018 Proposed Regulations used a numbering format for Section references using two dashes (e.g. Proposed Treasury Regulations §1.1400Z-2(a)-1(e)). The 2019 Proposed Regulations changed that numbering format slightly by using only one dash (e.g. Proposed Treasury Regulations §1.1400Z2(s)-1(b)). It's hard to determine why Treasury and the IRS changed the numbering format. The slight change in format may have been intended to distinguish the 2019 Proposed Regulations from the 2018 Proposed Regulations, in which case practitioners must hope that there are not too many more rounds of proposed regulations, each with a slightly different numbering format. It brings to mind thoughts of an episode from the TV series *Mash* when Captain Hawkeye Pierce, in trying to explain to a Colonel what Corporal Radar was doing with Captain Pierce and Captain Honeycutt in the officer's club (wearing corporal stripes on his sleeves and borrowed captain bars on his hat). Captain Pierce told the Colonel "We're experimenting with a new rank 'Corporal Captain.' We're down here making a survey seeing if everyone likes it." If the IRS is taking a survey as to whether practitioners like multiple numbering formats for proposed regulations involving the same sections of the Code, you can put my vote down as a no.

5 §1400Z-2(d)(1).

6 §1400Z-2(d)(2)(A).

7 §1400Z-2(d)(2)(D)(i). Section 179(d)(2) of the Code generally defines "purchase" as any acquisition of property but has three exceptions. The first exception excludes the property acquired from a related person as determined under the loss disallowance rules of Section 267 or 707(b) of the Code. The second exception excludes property acquired from a component member of a controlled group from another member of a controlled group. The third exception excludes property acquired in a transaction where the tax basis of the property acquired was acquired in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired, or under Section 1014(a) of the Code (relating to property acquired from a decedent.

Section 1400Z-2(d)(2)(D) did provide a definition for the term "substantially improved"[8] neither the Code nor the 2018 Proposed Regulations provided specific guidance on what constituted "substantially all" of the use of the property or "substantially all" of the QOF's holding period under Code Section 1400Z-2(d)(2)(D). The 2018 Proposed Regulations did reserve a spot for a proposed meaning of the phrase "substantially all" as used in Code Section 1400Z-2(d)(2).[9] In addition, the 2018 Proposed Regulations did define the phrase "substantially all" to mean at least 70% with respect to whether a business met the requirements of being a qualified opportunity zone business under Code Section 1400Z-2(d)(3)(A)(i).[10]

The 2019 Proposed Regulations provide that for purposes of determining whether the use of qualified opportunity zone business property in a qualified opportunity zone, as required in Code Section 1400Z-2(d)(2)(D)(i)(III), the term "substantially all" in the context of "use" is seventy percent (70%).[11]

However, the 2019 Proposed Regulations took a different position with respect to the term "substantially all" as used in the holding period context. Treasury and the IRS noted that since the language of Code Section 1400Z-2(d)(2)(D)(i)(III) had a compounded use of the phrase "substantially all" (i.e. substantially all of the use and substantially all of the holding period) that this should be interpreted as Congress intending a higher threshold in order to preserve the integrity of the statute and for the purpose of focusing investment in designated qualified opportunity zones. Accordingly, the 2019 Proposed Regulations provide that the term "substantially all" as used in the holding period context should be ninety percent (90%).[12]

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8 §1400Z-2(d)(2)(D)(ii) states that tangible property used in a QOF's trade or business is treated as substantially improved by the QOF only if, during any 30-month period beginning after the date of acquisition of such tangible property, additions to basis with respect to such tangible property in the hands of the QOF exceed an amount equal to the adjusted basis of such tangible property at the beginning of such 30-month period in the hands of the QOF.

9 *See* 2018 Proposed Regulations §1.1400Z-2(d)-1(c)(6) *Substantially all of the usage of tangible property by a QOF in a qualified opportunity zone – [Reserved]*.

10 §1400Z-2(d)-2(d)(3)(A)(i) and 2018 Proposed Regulations §1.1400Z-2(d)-1(d)(1)(i) requires "substantially all" of the tangible property owned or leased by the taxpayer to be qualified opportunity zone business property in order for the trade or business to be treated as a qualified opportunity zone business. Proposed 2018 Regulations §1400Z-2(d)-1(d)(3)(i) states that a trade or business of an entity is treated as satisfying the requirement of §1400Z-2(d)-1(d)(1)(i) if at least 70 percent of the tangible property owned or leased by the trade or business is qualified opportunity zone business property.

11 2019 Proposed Regulations §1.1400Z2(d)-1(c)(6). The Preamble to the Proposed 2019 Regulations indicate that Treasury and the IRS received numerous questions and comments on the threshold limits of "substantially all" for purposes of §1400Z-2(d)(2)(D)(i)(III). Many commentators suggesting that a lower threshold for the use requirement would allow a variety of businesses to benefit from qualifying investments in QOFs. Other commentators suggested that too low a threshold would negatively impact the low-income communities that §1400 is intended to benefit, because the tax-incentivized investment would not be focused sufficiently on these communities. Although not getting into the relative merits of both sides, Treasury and the IRS apparently just went with consistency at least as it applied to the "use" test.

12 2019 Proposed Regulations §1.1400Z2(d)-1(c)(5).

b. *Original Use of Tangible Property Acquired by Purchase*

For tangible property to be treated as qualified opportunity zone business property, the "original use" of such property in the qualified opportunity zone must commence with the QOF or the QOF must substantially improve the property.[13] The 2019 Proposed Regulations, Treasury Regulations state that the original use of tangible property in a qualified opportunity zone commences on the date any person first places the property in service in the qualified opportunity zone for purposes of depreciation or amortization (or first uses it in a manner that would allow depreciation or amortization if that person were that property's owner).[14] Under the 2019 Proposed Regulations, tangible property located in the qualified opportunity zone that is being depreciated or amortized by a taxpayer other than the QOF or qualified opportunity zone business would not satisfy the original use requirement. Conversely, tangible property (other than land) located in the qualified opportunity zone that has not yet been depreciated or amortized by a taxpayer other than the QOF or qualified opportunity zone business would satisfy the original use requirement.

Treasury and the IRS also reviewed how to handle property that was currently not being used or vacant. Several commentators suggested that a vacancy period of at least one year should be required. The 2019 Proposed Regulations take the position that if property has been unused or vacant for an uninterrupted period of at least 5 years, original use in the qualified opportunity zone commences on the date after that period when any person first so uses or places the property in service in the qualified opportunity zone.[15]

With respect to used property, the 2019 Proposed Regulations state that used tangible property satisfies the original use requirement if the property has not been previously so used or placed in service in the qualified opportunity zone.[16] If tangible property has previously been used or placed in service in a qualified opportunity zone has been used or placed in service in the qualified opportunity zone before it was acquired by purchase, it must be substantially improved in order to satisfy the requirements of Code Section 1400Z-2(d)(2)(D)(i)(II).[17]

A taxpayer's improvements to leased property may satisfy the original use requirement and be considered purchased property for the amount of the unadjusted cost basis of such improvements as determined in accordance with Code Section 1012.[18]

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13 §1400Z-2(d)(2)(D)(i)(II).

14 2019 Proposed Regulations §1.1400Z2(d)-1(c)(7)(i).

15 The Preamble to the 2019 Proposed Regulations indicates that the five year period was chosen to prevent current owners of buildings in qualified opportunity zones from intentionally letting the buildings lay idle for a short period in order to increase their marketability to potential purchasers after 2017.

16 2019 Proposed Regulations §1.1400Z2(d)-1(c)(7)(i).

17 *Id.*

18 2019 Proposed Regulations §1.1400Z2(d)-1(c)(7)(ii).

The 2019 Proposed Regulations also looked at the proper treatment of land under the original use requirement. In general, the 2019 Proposed Regulations and Revenue Ruling 2018-29 take the position that if land that is within a qualified opportunity zone is acquired by purchase (within the meaning of Code Section 1400Z-2(d)(2)(D)(i)(I)), then the original use requirement of Code Section 1400Z-2(d)(2)(D)(i)(II) does not apply to the land, regardless of whether the land is improved or unimproved.[19] In addition, unimproved land that is within a qualified opportunity zone and acquired by purchase in accordance with Code Section 1400Z-2(d)(2)(D)(i)(I) is not required to be substantially improved within the meaning of Code Sections 1400Z-2(d)(2)(D)(i)(II) and 1400Z-2(d)(2)(D)(ii).[20] However, Treasury and the IRS recognized that in certain instances, the treatment of unimproved land as qualified opportunity zone business property could lead to tax results inconsistent with the purposes of Code Section 1400Z-2. Accordingly, the 2019 Proposed Regulations contain an anti-abuse provision that could apply to prevent a taxpayer from acquiring unimproved land to receive an inappropriate tax result.[21]

c. *Safe Harbor for Testing Use of Inventory in Transit*

Code Section 1400Z-2(d)(2)(D)(i)(III) provides that qualified opportunity zone business property means tangible property used in a trade or business of the QOF if, during substantially all of the QOF's holding period for such property, substantially all of the use of such property was in a qualified opportunity zone. Some commentators expressed concern over how inventory that was in transit on the last day of the taxable year of a QOF would be counted in determining whether the QOF has met the ninety percent (90%) ownership requirement found in Code Section 1400Z-2(d)(1). The 2019 Proposed Regulations clarify that inventory (including raw materials) of a trade or business does not fail to be used in a qualified opportunity zone solely because the inventory is in transit from a vendor to a facility of the trade or business that is in a qualified opportunity zone, or from a facility of the trade or business that is in a qualified opportunity zone to customers of the trade or business that are not located in a qualified opportunity zone.[22]

II. Treatment of Leased Tangible Property

a. *Status as Qualified Opportunity Zone Business Property*

Treasury and the IRS believe that given the purpose of Code Sections 1400Z-1 and 1400Z-2 to facilitate increased business activity and economic investment in qualified opportunity zones, the 2019 Proposed Regulations should not discriminate against and should provide greater parity among diverse types of business models. Accordingly, the 2019 Proposed Regulation take the position that in general leased property should be able to be treated as qualified opportunity zone

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19 *See* Rev. Rul. 2018-29, 2018 I.R.B. 45; 2019 Proposed Regulations §1.1400Z2(d)-1(d)(4)(ii).

20 2019 Proposed Regulations §§1.1400Z2(d)-1(c)(8)(ii)(D), -1(d)(4)(ii)(B).

21 2019 Proposed Regulations §1.1400Z2(f)-1(c)(1).

22 2019 Proposed Regulations §1.1400Z2(d)-1(c)(4)(iii).

business property.[23] Under the 2019 Proposed Regulations, leased tangible property meeting certain criteria may be treated as qualified opportunity zone business property for purposes of satisfying the ninety percent (90%) asset test under Code Section 1400Z-2(d)(1) and the substantially all requirement under Code Section 1400Z-2(d)(3)(A)(i). The following two general criteria must be satisfied. First, leased tangible property must be acquired under a lease entered into after December 31, 2017. Second, substantially all of the use of the leased tangible property must be in a qualified opportunity zone during substantially all of the period for which the business leases the property.[24]

The 2019 Proposed Regulations do not impose an original use requirement with respect to leased tangible property.[25] Furthermore, the 2019 Proposed Regulations do not require leased tangible property to be acquired from a lessor that is unrelated (within the meaning of Code Section 1400Z-2(e)(2)) to the QOF or qualified opportunity zone business that is the lessee under the lease. Alternatively, the 2019 Proposed Regulations require in all cases where a QOF or qualified opportunity zone business acquires rights with respect to any leased tangible property, the lease must be must be a "market rate lease" (i.e. the terms of the lease must reflect common, arms-length market practice in the locale that includes the QOF, as determined under Code Section 482 and the Treasury Regulations issued thereunder).[26] In addition, in order to maintain greater parity between decisions to lease or own tangible property, while also limiting abuse, the 2019 Proposed Regulations provide two limitations. First, if the lessor and lessee are related, leased tangible property will not be treated as qualified opportunity zone business property if, in connection with the lease, a QOF or qualified opportunity zone business at any time makes a prepayment to the lessor (or a person related to the lessor within the meaning of Code Section 1400Z-2(e)(2)) relating to a period of use of the leased tangible property that exceeds 12 months.[27] Second, if the lessor and lessee are related, then leased tangible personal property shall not be treated as qualified opportunity zone business property unless the lessee becomes the owner of the tangible property that is qualified opportunity zone business property and that has a value not less than the value of the leased personal property.[28] This acquisition must occur during the period that begins on the

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[23] *See, e.g.,* 2019 Proposed Regulations §1.1400Z2(d)-1(b)(2) (including the value of each asset owned or leased by the QOF to determine whether the QOF satisfies the ninety percent (90%) asset test of Section 1400Z-2(d)(1) of the Code.

[24] Preamble to the 2019 Proposed Regulations, Section II Treatment of Leased Property, Subsection A Status as Qualified Opportunity Zone Property.

[25] The Preamble to the 2019 Proposed Regulations states that in most circumstances, leased tangible property held by a lessee cannot be placed in service for deprecation or amortization purposes because the lessee does not own the tangible property for Federal income tax purposes. In addition, in many instances, leased tangible property may have been previously leased to other lessees or previously used in the qualified opportunity zone. Furthermore, taxpayers general do not have a basis in leased property that can be depreciated. Based on these reasons, the 2019 Proposed Regulations do not impose an "original use" requirement on lessees. In addition and for similar reasons, the Preamble to the 2019 Proposed Regulations indicates that no requirement for a lessee to "substantially improve leased tangible property.

[26] 2019 Proposed Regulations §1.1400Z2(d)-1(c)(4)(i)(B)(2).

[27] 2019 Proposed Regulations §1.1400Z2(d)-1(c)(4)(i)(B)(3)-(4).

[28] 2019 Proposed Regulations §1.1400Z2(d)-1(c)(4)(i)(B)(3), (B)(5).

date that the lessee receives possession of the property under the lease and ends on the earlier of the last day of the lease or the end of the 30-month period beginning on the date that the lessee receives possession of the property under the lease. Furthermore, there must be substantial overlap of zones(s) in which the owner of the property so acquired used it and the zone(s) in which that person uses the leased property.

The 2019 Proposed Regulations also include an anti-abuse rule to prevent the use of leases to circumvent the substantial improvement requirement for purchases of real property (other than unimproved land). In the case of real property (other than improved land) that is leased by a QOF, if, at the time the lease is entered into, there was a plan, intent or expectation for the real property to be purchased by the QOF for an amount of consideration other than the fair market value of the real property determined at the time of the purchase without regard to any prior lease payments, the leased real property is not qualified opportunity zone business property at any time.[29]

b. *Valuation of Leased Tangible Property*

The 2019 Proposed Regulations provide two methodologies (the "applicable financial statement valuation method" and the "alternative valuation method") for valuing leased tangible property for purposes of satisfying the ninety percent (90%) test and the substantially all test.[30] Once a QOF or qualified opportunity zone business selects one of those valuation methods for the taxable year, it must apply that method consistently to all leased tangible property valued with respect to the taxable year.

Under the applicable financial statement valuation method, the value of leased tangible property of a QOF or qualified opportunity zone business is the value of that property as reported on the applicable financial statement for the relevant reporting period.[31] A QOF or qualified opportunity zone business may select this method only if the applicable financial statement is prepared according to U.S. generally accepted accounting principles and requires an assignment of value to the lease of the tangible property.

Under the alternative valuation method, the value of tangible property this is leased by a QOF or a qualified opportunity zone business is determined based on a calculation of the sum of the present values of the payments to be made under the lease for such tangible property (using a discount rate equal to the applicable federal rate under Code Section 1274(a)(1)).[32] The value of the leased tangible property is calculated at the time the lease for such property is entered into.

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29 Preamble to the 2019 Proposed Regulations, Section II Treatment of Leased Property, Subsection A Status as Qualified Opportunity Zone Property.

30 §1400Z-2(d)(1) requires that at least 90% of a QOF's assets must be "qualified opportunity zone property." §1400-2(d)(3)(A)(i) requires substantially all of the tangible property owned or leased by a trade or business to be qualified opportunity zone business property in order for the trade or business to be a qualified opportunity zone business.

31 2019 Proposed Regulations §1.1400Z2(d)-1(b)(2).

32 2019 Proposed Regulations §1.1400Z2(d)-1(b)(3).

Once calculated, this calculated value is used as the value for such asset for all testing dates for purposes of the "substantially all of the use" requirement and the ninety percent (90%) asset test.

III. Qualified Opportunity Zone Businesses

a. *Real Property Straddling a Qualified Opportunity Zone*

For purposes of determining whether a trade or business is a "qualified opportunity zone business, Code Section 1400Z-2(d)(3)(A)(ii) incorporates the requirements of Code Section 1397C(b)(2)(, (4) and (8) related to Empowerment Zones. Code Section 1397C(f) provides rules with respect to real property that is partially within and partially outside of an Empowerment Zone. The 2019 Proposed Regulations adopt a rule similar to the rule in Code Section 1397(f) with respect to Qualified Opportunity Zones. Accordingly, if the unadjusted cost of real property located within the qualified opportunity zone is greater than the unadjusted cost of the real property outside the zone and the real property is contiguous to the part of all of the real property inside the zone, then all of the property is deemed to be located in a qualified opportunity zone.[33]

b. *50 Percent of Gross Income of a Qualified Opportunity Zone Business*

One of the requirements of being a "qualified business entity" with respect to a taxable year, the entity must derive at least 50 percent of its total gross income "from the active conduct of such business."[34] In response to concerns from commentators with respect to how the IRS will determine whether this 50% gross income requirement is satisfied, the 2019 Proposed Regulations provide three safe harbors and a facts and circumstances test. Businesses only need to meet one of these safe harbors to satisfy the test.[35]

A trade or business meets the first safe harbor if at least 50 percent of the services performed (based on hours) for the business by its employees and independent contractors (and employees of independent contractors) are performed within the qualified opportunity zone. A trade or business meets the second safe harbor if at least 50 percent of the services performed for the business by its employees and independent contractors (and employees of independent contractors) are performed in the qualified opportunity zone, based on amounts paid for the services performed. A trade or business meets the third safe harbor if the tangible property of the trade or business that is located in a qualified opportunity zone and the management or operational functions performed in the qualified opportunity zone are each necessary to generate at least 50 percent of the gross income of the trade or business. If a trade or business does not meet any of the three safe harbors, it will still be treated as meeting the 50% of total gross income test if, based on all the facts and circumstances, at least 50 percent of the gross income of a qualified opportunity zone business is derived from the active conduct of a trade or business in the qualified opportunity zone.

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[33] 2019 Proposed Regulations §1.1400Z2(d)-1(d)(4)(i)(B)(2).

[34] §1397C(b)(2).

[35] 2019 Proposed Regulations §1.1400Z2(d)-1(d)(5)(i).

c. *Use of Intangibles*

One of the requirements that a qualified opportunity zone business must satisfy is Code Section 1397C(b)(4). As applied to a qualified opportunity zone business, Code Section 1397C(b)(4) requires that, with respect to any taxable year, a substantial portion of the intangible property of the trade or business must be used in the active conduct of a trade or business in the qualified opportunity zone. Code Section 1397C does not define what constitutes a "substantial portion" for purposes of this requirement. The 2019 Proposed Regulations provide that for purposes of determining whether a substantial portion of intangible property of a qualified opportunity zone business is used in the active conduct of a trade or business, the term "substantial potion" means at least 40 percent.[36]

d. *Active Conduct of a Trade or Business*

A qualified opportunity zone business must also satisfy Code Section 1397(b)(2). As applied to a qualified business entity, Code Section 1397(b)(2) requires at least 50 percent of the total gross income of the entity to be derived from the active conduct of a trade or business within a qualified opportunity zone. The 2018 Proposed Regulations did not define what constitutes the active conduct of a trade or business for purposes of this requirement. In response to requests for guidance from commentators, the 2019 Proposed Regulations defined a trade or business for purposes of satisfying this requirement as a trade or business within the definition of Code Section 162.[37] Although Treasury and the IRS reserved for a later date issuing additional rules for determining if a trade or business is actively conducted, the Preamble to the 2019 Proposed Regulations also indicated that the ownership and operation (including leasing, provided the lease is not a triple net lease) of real property used in a trade or business qualifies as the active conduct of a trade or business.

e. *Working Capital Safe Harbor*

As applied to a qualified opportunity zone business, Code Section 1397(b)(8) requires the less than 5 percent of the average of the aggregate unadjusted bases of the asset of the business must be attributable to "nonqualified financial property." The 2018 Proposed Regulations excluded from "nonqualified financial property, a reasonable amount of working capital held in cash, cash equivalents or debt instruments with a term of 18 months or less.[38] The 2018 Proposed Regulations also provided a safe harbor indicating that working capital assets are treated as reasonable in amount if the amounts are designated in writing for the acquisition, construction and/or substantial improvement of tangible property in a qualified opportunity zone, there is a written schedule consistent with the ordinary start-up of a trade or business for the expenditure of the working capital assets that calls for working capital assets to be spent within 31 months of the

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[36] 2019 Proposed Regulations §1.1400Z2(d)-1(d)(5)(ii)(A).

[37] 2019 Proposed Regulations §1.1400Z2(d)-1(d)(5)(ii)(B)(3).

[38] 2018 Proposed Regulations §1.1400Z-2(d)-1(d)(5)(iii).

receipt by the business of the assets, and the working capital assets are actually used in a manner that is substantially consistent with the prior two requirements.[39]

The 2019 Proposed Regulations made two changes to this safe harbor. First, the written designation for planned use of working capital now includes the development of a trade or business in the qualified opportunity zone as well as acquisition, construction, and/or substantial improvement of tangible property.[40] Second, exceeding the 31-month period does not violate the save harbor if the delay is attributable to waiting for government action and the application for which is completed during the 31-month period. [41]

IV. <u>Special Rules for Section 1231 Gains</u>

The 2018 Proposed Regulations clarified that only gain that is treated as capital gain is eligible for deferral under Code Section 1400Z-2(a)(1).[42] In general, gain or loss from the sale or exchange of real property or depreciable property used in a trade or business and held for more than one year is treated as "Section 1231 gain" or "Section 1231 loss," as applicable. Code Section 1231(a)(1) provides that if the Section 1231 gains for any taxable year exceed the Section 1231 losses, such gain shall be treated as long-term capital gain. Accordingly, the 2019 Proposed Regulations provide that only this gain shall be treated as an eligible gain for purposes of the deferral under Code Section 1400Z-2(a)(1).[43] In addition, the 2019 Proposed Regulations state that the 180-day period by which gain must be reinvested in a qualified opportunity fund with respect to any Section 1231 capital gain begins on the last day of the taxpayer's taxable year, not when the Section 1231 gain is recognized.[44]

V. <u>Relief with Respect to the 90-Percent Test</u>

a. *Relief for Newly Contributed Assets*

Under the so called 90% Asset Test, at least 90% of a QOF's assets must be qualified opportunity zone property (the "90% Asset Test").[45] A QOF must meet the 90% Asset Test every six months. In order to provide some relief to a QOF that receives a large investment shortly before one of its sic month testing dates, the 2019 Proposed Regulations allow a QOF to apply the

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39 2018 Proposed Regulations §1.1400Z-2(d)-1(d)(5)(iv).

40 2019 Proposed Regulations §1.1400Z2(d)-1(d)(5)(iv)(A).

41 2019 Proposed Regulations §1.1400Z2(d)-1(d)(5)(iv)(C).

42 2018 Proposed Regulations §1.1400Z-2(a)-1(b)(2)(i)(A).

43 2019 Proposed Regulations §1.1400Z2(a)-1(b)(2)(iii).

44 *Id.* This change was based on the fact that since a taxpayer's net Section 1231 gain or net Section 1231 loss cannot be determined until the last day of the taxpayer's taxable year, the 180-day period for investing such capital gain income in a QOF shouldn't begin prior to that day.

45 §1400Z-2(d)(1).

90% Asset Test without taking into account any investments received in the preceding 6 months.[46] The QOF's ability to do this, however, is dependent on those new assets being continuously held in cash, cash equivalents, or debt instruments with a term of 18 months or less.

b. ***QOF Reinvestment Rule***

In response to commentators requests for guidance on reinvestment proceeds, the 2019 Proposed Regulations provide that proceeds received by a QOF from the sale or disposition of (1) qualified opportunity zone business property, (2) qualified opportunity zone stock, and (3) qualified opportunity zone partnership interests are treated as qualified opportunity zone property for purpose of the 90% Asset Test so long as the QOF reinvests the proceeds received by the QOF from the sale of such property during the 12-month period beginning on the date of such distribution, sale or disposition.[47] Prior to reinvestment, the proceeds must be held in cash, cash equivalents and debt instruments with a term of 18 months or less.

This rule is intended to allow a QOF a reasonable amount of time to reinvest such proceeds without failing to meet the 90% Asset Test. The 2019 Proposed Regulations did not, however, provide that the reinvestment deferred the recognition of gain on the sale or disposition of the property by the QOF. Whether or not the QOF is taxed on the gain from the sale or disposition of the QOF's property depends on whether or not the transaction is an "Inclusion Event" as defined in and subject to the rules provided in the 2019 Proposed Regulations. Inclusion Events are discussed in more detail in Section VII of this article.

VI. Amount of an Investment for Purposes of Making a Deferral Election

Code Section 1400Z-2(e) requires that where a taxpayer makes an investment in a QOF in part with gains for which a deferral election was made and in part with other funds, these two types of QOF investments must be treated as separate investments (a qualified investment and a non-qualifying investment). In that case, only the "deferred gain" portion of the QOF investment is eligible for the benefits of QOF regime.

a. ***Interests for Services***

If a taxpayer receives an interest in a QOF in exchange for services rendered to the QOF, that interest is treated as a non-qualifying investment under the 2019 Proposed Regulations.[48] Accordingly carried interests in a QOF are ineligible for any tax exemption under the QOF regime upon a later sale.

b. ***Interests for Cash***

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[46] 2019 Proposed Regulations §1.1400Z2(d)-1(b)(4).

[47] Preamble to the 2019 Proposed Regulations, Section V.B.

[48] 2019 Proposed Regulations §1.1400Z2(a)-1(b)(9)(ii).

If a taxpayer makes a Code Section 1400Z-2(a)(1)(A) investment in a QOF by transferring cash to the QOF in exchange for the interest in the QOF, then the 2019 Proposed Regulations treat the amount of the taxpayer's Code Section 1400-2(a)(1)(A) investment as being equal to the amount of cash transferred.[49]

c. ***Interests for Property***

The 2019 Proposed Regulations clarify that a taxpayer may make an investment in a QOF for purposes of making a deferral election under Code Section 1400Z-2(a) by transferring cash or other property to a QOF, regardless of whether the transferor would recognize gain or loss on the property transferred.[50] Under these rules, a taxpayer can transfer property to a QOF in a taxable transaction (e.g. a transfer to a QOF corporation in an exchange that does not meet the requirements of Code Section 351) or in a nontaxable transaction (e.g. a contribution to a partnership in an exchange qualifying under Code Section 721) in exchange for an eligible interest in the QOF. The amount of the investment treated as eligible for purposes of making a deferral election depends upon whether a taxpayer transfers property in a carryover basis transaction (in whole or in part) or a taxable transaction.

If a taxpayer transfers property (other than cash) in exchange for an interest in a QOF in a carryover basis transaction (e.g. a contribution to a QOF partnership in exchange for an eligible interest in the QOF in a transaction within Code Section 721(a)), the amount of the taxpayer's qualifying investment for federal income tax purposes is equal to the lesser of (1) the taxpayer's basis in the QOF investment without regard to the special zero basis rule in Code Section 1400Z-2(b)(2)(B), or (2) the fair market value of the eligible interest received, both determined immediately after the contribution.[51] This rule is applied separately to each piece of property contributed to the QOF.

The contribution of appreciated property with unrecognized gain by a taxpayer to a QOF in exchange for a QOF interest will result in a mixed-funds investment (i.e. a qualifying investment and a non-qualifying investment).[52] The taxpayer's basis in the non-qualifying investment is equal

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[49] 2019 Proposed Regulations §1.1400Z2(a)-1(b)(10)(i)(A).

[50] 2019 Proposed Regulations §1.1400Z2(a)-1(b)(9)(i).

[51] 2019 Proposed Regulations §1.1400Z2(a)-1(b)(10)(i)(B)(1).

[52] 2019 Proposed Regulations §1.1400Z2(a)-1(b)(10)(i)(B)(2). It should be noted that the current language in this section of the 2019 Proposed Regulations appears to be incorrect. The current language in 2019 Proposed Regulations §1.1400Z2(a)-1(b)(10)(i)(B)(2) indicates that when the fair market value of the eligible interest received exceeds the taxpayer's adjusted basis in the eligible interest received in the transaction, (without regard to the zero basis rule), then the amount of the taxpayer's non-qualifying investment is equal to the excess of the "fair market value of the investment to which Section 1400Z2-2(e)(1)(A)(i) applies; over the taxpayer's adjusted basis therein, determined without regard to section 1400Z-2(b)(2)(B)." The "investment to which Section 1400Z2-2(e)(1)(A)(i) applies" is the qualifying investment. As currently written, the language would have you calculate the amount of a taxpayer's non-qualifying investment as the difference between the fair market value of the taxpayer's qualifying investment and the adjusted basis in that investment without taking into account the zero basis rule. This appears to be incorrect. As correctly calculation in Example 1 in the relevant section of the 2019 Proposed Regulations), the amount of a taxpayer's non-qualifying investment should be the excess of the fair market value of the eligible interest

to the taxpayer's basis in all QOF interests received (determined without regards to the zero basis rule of Code Section 1400Z-2(b)(2)(B)), less the taxpayer's basis in the qualifying investment (determined without regards to the zero basis rule of Code Section 1400Z-2(b)(2)(B)).

If there is a transfer of built-in loss property to a corporation in a transaction covered in whole or in part by Section 362 of the Code, then there is a special rule that deems the contributing taxpayer to have made a Code Section 362(e)(2)(C) election (related to the transfer of built-in loss property in a Code Section 351 transaction).[53]

If the taxpayer transfers property other than cash to a QOF in exchange for an interest in the QOF in a taxable transaction, the amount of the qualifying investment in the QOF is the fair market value of the transferred property, determined immediately prior to the transfer.[54]

VII. Events that Cause Inclusion of Deferred Gain (Inclusion Events)

Code Section 1400Z-2(b)(1) provides that the amount of gain that is deferred if a taxpayer makes an equity investment in a qualifying investment (as described in Code Section 1400Z-2(e)(1)(A)(i)) will be included in the taxpayer's income in the taxable year that includes the earlier of: (A) the date on which the qualifying investment is sold or exchange, or (B) December 31, 2026. By using the terms "sold" or "exchanged," Code Section 1400-2(b)(1) does not directly address non-sale or exchange dispositions, such as gifts, bequests, devises, charitable contributions, and abandonments of qualifying investments.

The 2019 Proposed Regulations contain detailed rules concerning the types of transfers of qualifying investments that will trigger the deferred gains (referred to as "inclusion events"). The 2019 Proposed Regulations define 21 inclusion events and note that each of those transactions would reduce or terminate the QOF investor's direct or indirect interest in the QOF. Among the other types of transfers described as inclusion events are transfers by gift, (whether outright or in trust and regardless of whether the transfer is a completed gift for federal gift tax purposes), a distribution of a QOF partnership, a distribution of property with respect to stock in a QOF corporation to the extent it is treated as gain from the sale or exchange of property under Code Section 301(c)(3) and certain transfers of interests in an S corporation or partnership that are themselves a direct investment in a QOF. Transfers by reason of death (to the decedent's estate or from the estate to the decedent's heirs) are not inclusion events.

VIII. Consolidated Return Provisions

The 2019 Proposed Regulations note that the consolidated return regulations and the opportunity zone program are based on incompatible principles and rules. Accordingly, the 2019 Proposed

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received over the taxpayer's adjusted basis in the interest without regard to the special zero basis rule in Code Section 1400Z-2(b)(2)(B). *See* Lisa M Starczewski, *INSIGHT: The Second Set of Proposed Opportunity Zone Regulations: Where Are We Now? – Part I,* Daily Tax Report (April 23, 2019).

53 2019 Proposed Regulations §1.1400Z2(a)-1(b)(10)(i)(B)(3).

54 2019 Proposed Regulations §1.1400Z2(a)-1(b)(10)(i)(C).

Regulations provide (1) that a QOF C corporation owned by members of a consolidated group is not a member of a consolidated and (2) various other rules related to QOFs and consolidated groups.

IX. Holding Period and Other Tacking Rules

The 2019 Proposed Regulations provide if an investor disposes of its interest in a QOF and reinvests in another QOF, the investor's holding period begins on the date of its investment in the second QOF, not the first QOF. However, the 2019 Proposed Regulations also provide for exceptions for certain mergers and acquisitions of QOF investments that allow for the tacking of a holding period in the initial investment in a QOF.

X. General Anti-Abuse Rule

The 2019 Proposed Regulations provide for a general anti-abuse rules stating the qualified opportunity zone rules must be applied in a manner consistent with the purposes of Code Section 1400Z-2. Accordingly, if a significant purpose of a transaction is to achieve a tax result that is inconsistent with the purposes of Code Section 1400Z-2, the Commissioner can recast the transaction (or series of transactions) for federal income tax purposes as appropriate to achieve tax results that are consistent with the purposes of Code Section 1400Z-2. This determination is done on a facts and circumstances basis.

The 2019 Proposed Regulations, like the 2018 Proposed Regulations, represent much needed guidance with respect to the implementation of the incentive program as described in Sections 1400-1 and 1400-2 of the Code. Investors and the tax practitioners advising them certainly welcome this guidance and, hopefully, even more guidance in the months ahead as Treasury, the IRS and taxpayers all hope to be able to use this new tax incentive to help achieve its goals of providing additional capital to businesses located in qualified opportunity zones.

RECENT DEVELOPMENTS IN FEDERAL INCOME TAXATION

"Recent developments are just like ancient history, except they happened less long ago."

By

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I. ACCOUNTING

A. Accounting Methods

1. A genuine issue of material fact existed as to whether a C corporation (that eventually changed to an S corporation) adopted the deposit, in lieu of the deferral, method of accounting. Thrasys, Inc. v. Commissioner, 116 T.C.M. (CCH) 531, 2018 T.C.M. (RIA) ¶ 2018-199 (12/4/18). The issue in this case was whether taxpayer, Thrasys, Inc., could, in its 2008 tax year, properly account for a $15 million payment received from its customer, Siemens, under the deferral method allowed by Rev. Proc. 2004-34. The Tax Court (Judge Lauber) dismissed the Service's motion for summary judgment and concluded that genuine issues of material fact existed as to whether the taxpayer had adopted the "deposit" method of accounting in 2008. The Service argued in its motion for summary judgment that the taxpayer could not switch from the "deposit" method of accounting—which the Service argued the taxpayer had adopted for this type of payment through its accounting treatment—to the deferral method because it never received the Service's consent to make that switch. Section 446(a) provides that "[t]axable income shall be computed under the method of accounting on the basis of which the taxpayer regularly computes his income in keeping his books." Under Reg. § 1.446-1(e)(1), "[a] taxpayer filing his first return may adopt any permissible method of accounting in computing taxable income for the taxable year covered by such return." Section 446(e) provides that "a taxpayer who changes the method of accounting on the basis of which he regularly computes his income in keeping his books shall, before computing his taxable income under the new method, secure the consent of the Secretary." Moreover, according to the court, under § 446(a) and (e), "an accounting treatment constitutes a 'method of accounting' if the taxpayer 'regularly computes his income' using it." The court denied the Service's motion for summary judgment, **first**, because the taxpayer treated only one customer payment (the 2008 $15 million payment from Siemens) as a deposit for book or federal income tax purposes (and then shifted the $15 million to the deferred revenue category on its Form 1120S in 2009). Therefore, "[a] question of material fact exists as to whether [taxpayer's] 'deposit' treatment displayed the consistency required to constitute a method of accounting on the basis of which Thrasys 'regularly compute[d]' its income." And, **second**, the Tax Court noted that a change in the taxpayer's "method of accounting does not include 'a change in treatment resulting from a change in underlying facts'" under Reg. § 1.446-1(e)(2)(ii)(b). Thrasys (and its auditor) "may reasonably have believed that treating the $15 million payment as a deposit was a required 'change in treatment resulting from a change in underlying facts'" because "Thrasys treated the $15 million payment differently from [other] customer payments received during 2005 to 2007," which were treated as advance payments and unearned, deferred revenue on its financial statements. The $15 million treatment as a deposit was based on the adjustments an independent auditor had made to taxpayer's 2008 financial statements (i.e., potentially a change in treatment due to a change in underlying facts). Therefore, the Tax Court found that genuine issues of material fact existed regarding whether Thrasys in 2008 actually "adopted the 'deposit' method as a method of accounting for customer payments," and accordingly the Tax Court denied the Service's motion for summary judgment.

B. Inventories

C. Installment Method

D. Year of Inclusion or Deduction

II. BUSINESS INCOME AND DEDUCTIONS

A. Income

B. Deductible Expenses versus Capitalization

1. Up in Smoke: the deductions of this medical marijuana business were disallowed by § 280E and could not be capitalized under the uniform capitalization rules of § 263A. Patients Mutual Assistance Collective Corp. v. Commissioner, 151 T.C. No. 11 (11/29/18). The taxpayer, a subchapter C corporation engaged in the medical marijuana business in California, argued that its deductions for business expenses were not subject to disallowance under § 280E. Section 280E disallows any deduction or credit otherwise allowable if such amount is paid or incurred in connection with a trade or business "if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances …." In a lengthy opinion by Judge Holmes, the Tax Court rejected the taxpayer's argument that the words "consists of" in § 280E mean that the statute applies only to businesses that exclusively or solely engage in trafficking controlled substances and does not apply to businesses, like the taxpayer's, that also engage in other activities such as offering acupuncture services and group sessions for yoga and tai chi. Judge Holmes noted that the court had "cursorily rejected" a nearly identical argument in *Olive v. Commissioner*, 139 T.C. 19 (2012), *aff'd*, 792 F.3d 1146 (9th Cir. 2015), but given the importance of the issue to the industry, explained the court's reasoning at greater length. The court further held that the taxpayer had only one trade or business. Accordingly, § 280E applied to disallow the taxpayer's deductions. The court also considered whether the taxpayer was required to determine cost of goods sold under the rules of § 471 or instead the rules of § 263A. Section 263A provides that both resellers as well as producers of property must include indirect costs in cost of goods sold and broadens the indirect costs that must be included. The court concluded that the rules of § 263A did not apply to the taxpayer because of the flush language of § 263A(a)(2), which provides:

> Any cost which (but for this subsection) could not be taken into account in computing taxable income for any taxable year shall not be treated as a cost described in this paragraph.

The court analyzed the regulations that interpret this provision and concluded that the statute's meaning is that "if something wasn't deductible before Congress enacted section 263A, taxpayers cannot use that section to capitalize it." The court rejected several arguments of the taxpayer to the contrary. Because the rules of § 263A did not apply, only the rules of § 471 did. (Unlike § 263A, § 471 was in place when Congress enacted § 280E.) The rules of § 471 distinguish between resellers and producers of property. Under Reg. § 1.471-3(b), resellers must use as their cost of goods sold the price they pay for inventory plus any "transportation or other necessary charges incurred in acquiring possession of the goods." The court concluded that the taxpayer was a reseller and therefore, pursuant to the regulations under § 471, could not include indirect costs in determining cost of goods sold. Finally, the court rejected the taxpayer's argument that the government was barred by *res judicata* from pursuing the case because of the government's prior decision to abandon a civil forfeiture action against the taxpayer.

C. Reasonable Compensation

D. Miscellaneous Deductions

1. Tax Court blows out the flame on California medical marijuana dispensary's deductions. A related subchapter S corporation's deductions also were disallowed. Alternative Health Care Advocates v. Commissioner, 151 T.C. No. 13 (12/20/18). A California medical marijuana dispensary claimed deductions under § 162 for business expenses. The dispensary was organized as a C corporation (Alternative) that operated the dispensary and a subchapter S corporation (Wellness) that handled daily operations for Alternative, including paying employee wages and salaries. The Tax Court (Judge Pugh) agreed with the IRS that the deductions claimed by both Alternative and Wellness were disallowed by § 280E. Section 280E disallows any deduction or credit otherwise allowable if such amount is paid or incurred in connection with a trade or business "if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances …." Judge Pugh concluded that Alternative had only one trade or business because its nonmarijuana activities "were only ancillary" to its primary activity of operating a marijuana dispensary. Therefore, Alternative could not allocate its expenses between a trafficking business and a non-trafficking business and § 280E operated to disallow all of Alternative's claimed deductions. With respect to the subchapter S corporation, Wellness, the court concluded that "Wellness employees were directly involved in the provision of medical marijuana to the patient members of Alternative's dispensary." Further, according to the court, Wellness employees were engaged in the purchase and sale of marijuana on behalf of Alternative and this activity was the primary business of Wellness. Accordingly, although Wellness never took title to marijuana, the court held that Wellness was engaged in trafficking in controlled substances. Therefore, § 280E disallowed deductions claimed by Wellness, which resulted in additional income flowing to the shareholders of Wellness. The court also held that Alternative could not add direct and indirect costs of inventory to its cost of goods sold under § 263A because, by virtue of § 263A(a)(2), "[s]ection 263A puts into COGS only expenses otherwise deductible." (The court previously had reached this conclusion and applied it to a medical marijuana business in Patients Mutual Assistance Collective Corp. v. Commissioner, 151 T.C. No. 11 (11/29/18).) The court held that Alternative was not a producer, but rather a reseller of marijuana products, and therefore could not increase its cost of goods sold under § 471 beyond what the IRS had allowed for the taxable years at issue. Finally, the Tax Court held that Alternative was liable for the § 6662(a) accuracy-related penalty for the taxable years at issue due to substantial understatements of income tax for those years.

E. Depreciation & Amortization

F. Credits

G. Natural Resources Deductions & Credits

H. Loss Transactions, Bad Debts, and NOLs

I. At-Risk and Passive Activity Losses

1. No passivity here; taxpayer's active and involved management of multiple rental properties establishes her as a real estate professional for purposes of § 469. Birdsong v. Commissioner, 116 T.C.M. (CCH) 274, 2018 T.C.M. (RIA) ¶ 2018-148 (9/10/18). The taxpayers were a married couple. The Tax Court (Judge Vasquez) concluded that the wife's activities indicated that she was a real estate professional under § 469(c)(7)(B) and materially participated and thus did not have a passive activity loss under § 469(c)(2). Section 469(a) generally disallows passive activity losses. Under § 469(c)(1) a passive activity is any trade or business in which the taxpayer does not materially participate. A rental activity is generally treated as a per se passive activity regardless of whether the taxpayer materially participates pursuant to § 469(c)(2), but the rental activities of a taxpayer who qualifies as a real estate professional are not per se passive activities according to § 469(c)(7). Instead such activities are treated as a trade or business subject to the material participation requirements of § 469(c)(1). A taxpayer is a real estate professional if: "(i) more than one-half of the personal services performed in trades or businesses by the taxpayer during such taxable year are performed in real property trades or businesses in which the taxpayer materially participates, and (ii) such taxpayer performs more than 750 hours of services during the taxable year [in such real property trades or businesses]." § 469(c)(7)(B). The Tax Court cited Reg. § 1.469-5T(f)(4) for the requirements to establish the taxpayer's hours of participation. This provision states in part that the "extent of an individual's participation in an activity may be established by any reasonable means. Contemporaneous daily time reports, logs, or similar documents are not required if the extent of such participation may be established by other reasonable means." Moreover, Judge Vasquez noted that other Tax Court decisions "have held that the regulations do not allow a post-event, 'ballpark guesstimate'" (citing *Bailey v. Commissioner*, T.C. Memo. 2001-296; *Goshorn v. Commissioner*, T.C. Memo. 1993-578). With that in mind, the Tax Court found the taxpayers' narrative summary alongside the "thorough time logs," which indicated the wife spent 1,136.25 hours managing the rental properties in 2014, "convincing because [taxpayers] owned numerous rental units that [the] wife operated alone" (citing *Hailstock v. Commissioner*, T.C. Memo. 2016-146, at *21 for its holding that the "taxpayer's credible testimony regarding time spent operating multiple properties alone satisfied the section 469(c)(2) requirements."). Thus, the Tax Court held that the wife "materially participated and is a real estate professional" (meeting both requirements under § 469(c)(7)(B)), and accordingly held that the taxpayers' "loss attributable to their rental real estate [was] not limited by the passive activity loss rules of section 469," which meant that the taxpayers had no tax underpayment and no accuracy-related penalty.

III. INVESTMENT GAIN AND INCOME

IV. COMPENSATION ISSUES

V. PERSONAL INCOME AND DEDUCTIONS

A. Rates

B. Miscellaneous Income

1. Taxpayers feel the pain after this Tax Court decision, and that pain is not on account of any physical injury or physical sickness. Smith v. Commissioner, 116 T.C.M. (CCH) 154, 2018 T.C.M. (RIA) ¶ 2018-127 (8/3/18). The taxpayers were Dr. Georgia Lakner—a doctor, psychiatrist, and U.S. Army colonel—and his wife, Martha Smith. They failed to report income on their 2007 to 2011 joint tax returns, including their receipt of a $328,000 settlement from the Veterans Administration (VA). The Tax Court (Judge Lauber) held that the taxpayers could not exclude the settlement payment from gross income under § 104(a)(2) because the payment did not constitute damages received on account of personal, physical injury. Section 104(a)(2) provides that "gross income does not include damages received on account of personal physical injuries or physical sickness," but emotional distress is not treated as a physical injury or physical sickness for this purpose. The Tax Court noted that Dr. Lakner's EEOC complaints alleged that the VA Medical Center in Loma Linda, California fired him "because of his Jewish ancestry and religion and as reprisal for his advocacy on behalf of veterans with psychological illness." Moreover, the Tax Court pointed out that the original and amended EEOC complaints were filed in 2002, and thus "did not mention (nor could they possibly have mentioned) [an] injury he sustained in 2003" while deployed in Bosnia. In general, the EEOC complaints did not allege any physical injury. Instead the VA settlement agreement made clear that the VA settled the case in consideration of Dr. Lakner's "agreement to withdraw 'all discrimination complaints' he had made." The Tax Court focused on the intent of the payor, the VA, and found that under the terms of the settlement agreement the VA intended to settle and settled Dr. Lakner's claims of discrimination based on religion, national origin, and reprisal. Therefore, the court held that the "$328,000 VA settlement payment was not received 'on account of personal physical injuries or physical sickness' and therefore was not excludable from gross income under section 104(a)(2)." The Tax Court also held that the taxpayers could not take certain deductions and upheld late-filing penalties under §6651(a)(1) and accuracy-related penalties under § 6662(a) for underpayment of tax due to negligence.

C. Hobby Losses and § 280A Home Office and Vacation Homes

D. Deductions and Credits for Personal Expenses

1. Has the federal deduction for your high property or state income taxes made them easier to bear? Brace yourself! The deduction for state and local taxes not paid or accrued in carrying on a trade or business or an income-producing activity is limited to $10,000. The 2017 Tax Cuts and Jobs Act, § 11042, amended Code § 164(b) by adding § 164(b)(6). For individual taxpayers, this provision generally (1) eliminates the deduction for foreign real property taxes, and (2) limits to $10,000 ($5,000 for married individuals filing separately) a taxpayer's itemized deductions on Schedule A for the aggregate of state or local property taxes, income taxes, and sales taxes deducted in lieu of income taxes. This provision applies to taxable years beginning after 2017 and before 2026. The provision does *not* affect the deduction of state or local property taxes or sales taxes that are paid or accrued in carrying on a trade or business or an income-producing activity (i.e., an activity described in § 212) that are properly deductible on Schedules C, E, or F. For example, property taxes imposed on residential rental property will continue to be deductible. With respect to income taxes, an individual can deduct only *foreign* income taxes paid or accrued in carrying on a trade or business or an income-producing activity. As under current law, an individual cannot deduct state or local income taxes as a business expense even if the individual is engaged in a trade or business as a sole proprietor. *See* Reg. § 1.62-1T(d).

a. The Service is not going to give blue states a pass on creative workarounds to the new $10,000 limitation on the personal deduction for state and local taxes. Notice 2018-54, 2018-24 I.R.B. 750 (05/23/18). In response to new § 164(b)(6), many states—including Connecticut, New Jersey, and New York—have enacted workarounds to the $10,000 limitation. For instance, New Jersey reportedly has enacted legislation giving property owners a special tax credit against otherwise assessable property taxes if the owner makes a contribution to charitable funds designated by local governments. Connecticut reportedly has enacted a new provision that taxes the income of pass-through entities such as S corporations and partnerships, but allows the shareholders or members a corresponding tax credit against certain state and local taxes assessed against them individually. Notice 2018-54 announces that the Service and Treasury are aware of these workarounds and that proposed regulations will be issued to "make clear that the requirements of the Internal Revenue Code, informed by substance-over-form principles, govern the federal income tax treatment of such transfers." In other words, blue states, don't bank on a charitable contribution or a flow-through income tax substituting for otherwise assessable state and local taxes to avoid new § 164(b)(6). The authors predict that this will be an interesting subject to watch over the coming months.

b. And like Rameses II in The Ten Commandments, Treasury says, "So let it be written; so let it (finally!) be done." REG-112176-18, Contributions in Exchange for State and Local Tax Credits, 83 F.R. 43563 (8/27/18). Moving swiftly, Treasury has published proposed regulations under § 170 that purport to close the door on any state-enacted workarounds to new § 164(b)(6). Prop. Reg. § 1.170A-1(h)(3) generally requires taxpayers to reduce the amount of any federal income tax charitable contribution deduction by the amount of any corresponding state or local tax *credit* the taxpayer receives or expects to receive. The proposed regulations further provide that a corresponding state or local tax *deduction* normally will not reduce the taxpayer's federal deduction provided the state and local deduction does not exceed the taxpayer's federal deduction. To the extent the state and local charitable deduction exceeds the taxpayer's federal deduction, the taxpayer's federal deduction is reduced. Finally, the proposed regulations provide an exception whereby the taxpayer's federal charitable contribution deduction is not reduced if the corresponding state or local credit does not exceed 15 percent of the taxpayer's federal deduction. Three examples illustrate the application of the proposed regulation:

- *Example 1*. A, an individual, makes a payment of $1,000 to X, an entity listed in section 170(c). In exchange for the payment, A receives or expects to receive a state tax credit of 70% of the amount of A's payment to X. Under paragraph (h)(3)(i) of this section, A's charitable contribution deduction is reduced by $700 (70% × $1,000). This reduction occurs regardless of whether A is able to claim the state tax credit in that year. Thus, A's charitable contribution deduction for the $1,000 payment to X may not exceed $300.

- *Example 2*. B, an individual, transfers a painting to Y, an entity listed in section 170(c). At the time of the transfer, the painting has a fair market value of $100,000. In exchange for the painting, B receives or expects to receive a state tax credit equal to 10% of the fair market value of the painting. Under paragraph (h)(3)(vi) of this section, B is not required to apply the general rule of paragraph (h)(3)(i) of this section because the amount of the tax credit received or expected to be received by B does not exceed 15% of the fair market value of the property transferred to Y. Accordingly, the amount of B's charitable contribution deduction for the transfer of the painting is not reduced under paragraph (h)(3)(i) of this section.

- *Example 3*. C, an individual, makes a payment of $1,000 to Z, an entity listed in section 170(c). In exchange for the payment, under state M law, C is entitled to receive a state tax deduction equal to the amount paid by C to Z. Under paragraph (h)(3)(ii)(A) of this section, C is not required to reduce its charitable contribution deduction under section 170(a) on account of the state tax deduction.

The proposed regulation is effective for charitable contributions made after August 27, 2018.

- *On the other hand* . . . . The looming trouble spot here is how taxpayers and the Service discern the difference between abusive "workarounds" enacted in response to new § 164(b)(6) and legitimate state and local tax credit programs such as the Georgia Rural Hospital Tax Credit that preceded TCJA. The Georgia Rural Hospital Tax Credit program was enacted in 2017 to combat the closure of many rural hospitals in Georgia due to financial difficulties. Under the program, individuals and corporations making contributions to designated rural hospitals receive a 90% dollar-for-dollar tax credit against their Georgia state income tax liability. Is the Georgia Rural Hospital Tax Credit program adversely affected by proposed regulations under § 164(b)(6)? In our view, the answer is "yes" and a Georgia taxpayer's federal charitable contribution deduction for a donation to a Georgia rural hospital is reduced by 90 percent. This follows because the proposed regulations do not condition the reduction in a taxpayer's federal charitable contribution deduction on whether the taxpayer's state and local deduction otherwise would exceed the $10,000 cap of new § 164(b)(6). We note, however, that it may be possible under state or local law for a taxpayer to waive any corresponding state or local tax credit and thereby claim a full charitable contribution for federal income tax purposes. *See* Rev. Rul. 67-246, 1967-2 C.B. 104.

c. Speaking of looming trouble spots: The availability of a business expense deduction under § 162 for payments to charities is not affected by the recently issued proposed regulations, says the Service. IRS News Release IR-2018-178 (9/5/18). This news release clarifies that the availability of a deduction for ordinary and necessary business expenses under § 162 for businesses that make payments to charities or government agencies and for which the business receives state tax credits is not affected by the proposed regulations issued in August 2018 that generally disallow a federal charitable contribution deduction under § 170 for charitable contributions made by an individual for which the individual receives a state tax credit. See REG-112176-18, Contributions in Exchange for State and Local Tax Credits, 83 F.R. 43563 (8/27/18). Thus, if a payment to a government agency or charity qualifies as an ordinary and necessary business expense under § 162(a), it is not subject to disallowance in the manner in which deductions under § 170 are subject to disallowance. This is true, according to the news release, regardless of whether the taxpayer is doing business as a sole proprietor, partnership or corporation. According to a "frequently asked question" posted on the Service website, "a business taxpayer making a payment to a charitable or government entity described in § 170(c) is generally permitted to deduct the entire payment as an ordinary and necessary business expense under § 162 if the payment is made with a business purpose."

d. More about trouble spots: The Service must be thinking, "Will this ever end?" Rev. Proc. 2019-12, 2019-04 I.R.B. 401 (12/29/18). Notwithstanding the above guidance, Treasury and the Service obviously have continued to receive questions regarding the deductibility of business expenses that may indirectly bear on the taxpayer's state and local tax liability. In response, Rev. Proc. 2019-12 provides certain safe harbors. For C corporations that make payments to or for the use of § 170(c) charitable organizations and that receive or expect to receive corresponding tax credits against state or local taxes, the C corporation nevertheless may treat such payment as meeting the requirements of an ordinary and necessary business expense for purposes of § 162(a). A similar safe harbor rule applies for entities other than C corporations, but only if the entity is a "specified passthrough entity." A specified passthrough entity for this purpose is one that meets four requirements. First, the entity must be a business entity other than a C corporation that is regarded for all federal income tax purposes as separate from its owners under Reg. § 301.7701-3 (i.e., it is not single-member LLC). Second, the entity must operate a trade or business within the meaning of § 162. Third, the entity must be subject to a state or local tax incurred in carrying on its trade or business that is imposed directly on the entity. Fourth, in return for a payment to a § 170(c) charitable organization, the entity receives or expects to receive a state or local tax credit that the entity applies or expects to apply to offset a state or local tax imposed upon the entity. The revenue procedure applies to payments made on or after January 1, 2018.

- *C corporation example state and local income tax credit:* A, a C corporation engaged in a trade or business, makes a payment of $1,000 to a § 170(c) charitable organization. In return for the payment, A receives or expects to receive a dollar-for-dollar state tax credit to be applied to A's state corporate income tax liability. Under the revenue procedure, A may treat the $1,000 payment as meeting the requirements of an ordinary and necessary business expense under § 162.

- *C corporation example state and local property tax credit:* B, a C corporation engaged in a trade or business, makes a payment of $1,000 to a § 170(c) charitable organization. In return for the payment, B receives or expects to receive a tax credit equal to 80 percent of the amount of this payment ($800) to be applied to B's local real property tax liability. Under the revenue procedure, B may treat $800 as meeting the requirements of an ordinary and necessary business expense under § 162. The treatment of the remaining $200 will depend upon the facts and circumstances and is not affected by the revenue procedure. (In other words, the $200 could be a charitable contribution deductible under § 170, or the $200 could be a business expense deductible under § 162.)

- *Specified passthrough example state and local excise tax credit:* P is a limited liability company (LLC) classified as a partnership for federal income tax purposes under Reg. § 301.7701-3 and is owned by individuals A and B. P is engaged in a trade or business within the meaning of § 162 and makes a payment of $1,000 to a § 170(c) charitable organization. In return for the payment, P receives or expects to receive a dollar-for-dollar state tax credit to be applied to P's state excise tax liability incurred by P in carrying on its trade or business. Under applicable state law, the state's excise tax is imposed at the entity level (not the owner level). Under the revenue procedure, P may treat the $1,000 payment as meeting the requirements of an ordinary and necessary business expense under § 162.

- *Specified passthrough example state and local property tax credit:* S is an S corporation engaged in a trade or business and is owned by individuals C and D. S makes a payment of $1,000 to a § 170(c) charitable organization. In return for the payment, S receives or expects to receive a state tax credit equal to 80 percent of the amount of this payment ($800) to be applied to S's local real property tax liability incurred by S in carrying on its trade or business. Under applicable state and local law, the real property tax is imposed at the entity level (not the owner level). Under the revenue procedure, S may treat $800 of the payment as meeting the requirements of an ordinary and necessary business expense under § 162. The treatment of the remaining $200 will depend upon the facts and circumstances and is not affected by this revenue procedure. (In other words, the $200 could be a charitable contribution deductible under § 170 by the owners of the specified passthrough entity, or the $200 could be a business expense deductible at the entity level under § 162.)

E. Divorce Tax Issues

F. Education

G. Alternative Minimum Tax

VI. CORPORATIONS

A. Entity and Formation

B. Distributions and Redemptions

C. Liquidations

D. S Corporations

1. ♪♬"Oh when will they ever learn, oh when will they ever learn?"♪♬ Debt of an S corporation to third parties does not increase the basis of shareholders. Hargis v. Koskinen, 893 F.3d 540 (8th Cir. 6/22/18). The taxpayers, a married couple, bought and operated nursing homes through several entities. Some of the entities were subchapter S corporations, of which the husband was the sole shareholder, that operated the nursing homes. The others were limited liability companies classified as tax partnerships in which the wife had an interest. The LLCs owned the nursing homes and leased them to the S corporations. The Service disallowed losses of the S corporations and the LLCs on the ground that the husband and wife had insufficient basis in their interests to deduct the losses. The S corporations had borrowed money from commercial lenders, from the LLCs, and from each other. The husband was a co-borrower or guarantor on the loans. The taxpayers acknowledged that the loans made to the S corporations were not indebtedness of the S corporations to the husband. Nevertheless, they argued that the husband had made an "economic outlay" that entitled him to a basis increase because, among other reasons, the husband was co-borrower on at least some of the loans. Citing *Selfe v. United States*, 778 F.2d 769 (11th Cir. 1985), they also argued that the lenders looked primarily to the husband for repayment of the loans, and therefore the loans should be treated as having been made to him followed by his contribution of the proceeds to the S corporations. In an opinion by Judge Benton, the U.S. Court of Appeals for the Eighth Circuit rejected all of these arguments:

> None of the other facts demonstrates that, in substance, [the husband] borrowed the funds and subsequently advanced them to the Operating Corporations. The lenders advanced the funds directly to the Operating Corporations; they directly paid the lenders; and [the husband] did not pledge any personal assets as collateral.

The court also held that the wife had failed to prove that she had sufficient basis in her interests in the LLCs to deduct her share of the LLCs' losses.

E. Mergers, Acquisitions and Reorganizations

F. Corporate Divisions

G. Affiliated Corporations and Consolidated Returns

H. Miscellaneous Corporate Issues

VII. PARTNERSHIPS

VIII. TAX SHELTERS

IX. EXEMPT ORGANIZATIONS AND CHARITABLE GIVING

A. Exempt Organizations

1. The eleven-factor facts and circumstances test for political campaign activity by tax exempts set forth in Rev. Rul. 2004-6 is neither unconstitutionally vague nor overbroad, at least on its face. Freedom Path, Inc. v. Internal Revenue Service, 120 A.F.T.R. 2d 2017-5125 (N.D. Tex. 7/7/17). In this unreported decision from the U.S. District Court for the Northern District of Texas, Judge Fitzwater upheld Rev. Rul. 2004-6, 2004-1 C.B. 328, as being neither unconstitutionally vague nor overbroad on its face for purposes of determining impermissible political campaign activity by a § 501(c)(4) organization. Rev. Rul. 2004-6 sets forth an eleven-factor facts and circumstances test used by the Service to determine whether certain activity by tax-exempt § 501(c)(3) or (c)(4) organizations is impermissible political campaign activity. The Service preliminarily denied exempt § 501(c)(4) status to Freedom Path, Inc. on the basis that its proposed activities were primarily political in nature. Freedom Path then sued Lois Lerner and the Service before the Service even issued a final negative determination letter to Freedom Path. The opinion in this case is the fourth ruling issued by Judge Fitzwater in a series of claims made in this ongoing lawsuit against the Service and former Exempt Organizations Director Lois Lerner alleging that conservative § 501(c)(4) groups had been targeted for denial of tax-exempt status during the 2011-2012 election cycle. The specific issue in this case was whether Rev. Rul. 2004-6 was unconstitutional on its face under either the First Amendment (free speech) or Fifth Amendment (due process) for being vague or overbroad. Judge Fitzwater held that it was not. The next and fifth ruling in this case almost certainly will be whether the eleven-factor test in Rev. Rul. 2004-6 was applied in an unconstitutional manner by the Service to preliminarily deny § 501(c)(4) exempt status to Freedom Path, Inc. Stay tuned . . . .

a. Meanwhile, prompted by the Service, the Fifth Circuit has another idea how to resolve the issue of the facial challenge to Rev. Rul. 2004-6. Freedom Path, Inc. v. Internal Revenue Service, 913 F.3d 503 (5th Cir. 1/16/19), *vacating and remanding* 120 A.F.T.R. 2d 2017-5125 (N.D. Tex. 7/7/17). On appeal of the narrow issue regarding whether Rev. Rul. 2004-6 is unconstitutional on its face, the Fifth Circuit, in an opinion written by Judge Southwick, decided Freedom Path lacked standing to sue. Freedom Path had made the same arguments before the Fifth Circuit as it had made before Judge Fitzwater. Cleverly, though, the Service argued before the Fifth Circuit that Rev. Rul. 2004-6 technically was not applied to deny Freedom Path's application for exempt status under § 501(c)(4). (The Service had not made this argument before Judge Fitzwater.) Rather, the Service pointed out that the facts and circumstances test described in Rev. Rul. 2004-6 was considered by the Service, along with other authorities, as part of the decision to deny (c)(4) status to Freedom Path, but the actual application of Rev. Rul. 2004-6 by its terms relates to determining an exempt organization's tax liability (if any) under § 527 (political organizations). Furthermore, argued the Service, Freedom Path has no tax liability under § 527. Thus, the Service concluded, Rev. Rul. 2004-6 is not the source of the alleged injury to Freedom Path. The Fifth Circuit agreed with the Service's analysis and determined that Freedom Path did not have standing because its claim (i.e., denial of (c)(4) status) was not "fairly traceable" to the text of Rev. Rul. 2004-6. Therefore, the Fifth Circuit vacated Judge Fitzwater's opinion (which had considered but rejected Freedom Path's constitutional challenge to Rev. Rul. 2004-6) and remanded the case to be dismissed for lack of jurisdiction. As noted above, Freedom Path's claim that it was unconstitutionally denied (c)(4) status (as opposed to its claim that Rev. Rul. 2004-6 is unconstitutional on its face) remains subject to challenge by Freedom Path and likely will be the next chapter in this story.

2. Oh goody! Changes to the UBTI rules too! The 2017 Tax Cuts and Jobs Act, §§ 13702 and 13703, also made certain changes to the determination of unrelated business taxable income ("UBTI") with respect to tax-exempt organizations. Most tax-exempt organizations are subject to federal income tax at regular rates (corporate rates for exempt corporations and trust rates for exempt trusts) on net income (i.e., after permissible deductions) from a trade or business, regularly carried on, that is unrelated to the organization's exempt purpose (other than its need for revenue). Exceptions exist for most types of passive, investment income as well as for narrow categories of other types of income (e.g., thrift store sales). *See* §§ 511-514. The rationale behind the changes to the UBIT rules was to put tax-exempt organizations on par with taxable organizations with respect to certain types of compensation and fringe benefits. Because, however, disallowing deductions for fringe benefits such as parking and transportation expenses (which is what the 2017 Tax Cuts and Jobs Act, § 13304(c), did by adding § 274(a)(4)) does not work for exempt organizations which do not normally pay tax, Congress did something weird. Specifically, Congress decided to arbitrarily increase an exempt organization's unrelated business income (even if such income was otherwise zero) by the value of the fringe benefits the organization provides to employees. Sounds like a simple solution, right? *Wrong! See below.*

Stop using good UBI money to chase bad UBI money! Under pre-TCJA law, if an exempt organization had unrelated business income ("UBI") from one activity, but unrelated losses from another activity, then the income and losses could offset, meaning that the organization would report zero or even negative UBI. Congress apparently doesn't like this result, so under new § 512(a)(6) income and losses from separate unrelated businesses no longer may be aggregated. This new UBI provision is effective for taxable years beginning after 2017, thus giving fiscal year nonprofits some time to plan. Moreover, under a special transition rule, unrelated business income net operating losses arising in a taxable year beginning before January 1, 2018, that are carried forward to a taxable year beginning on or after such date, are not subject to § 512(a)(6).

Congress doesn't like using UBI to help fund fringe benefits, so when your organization's highly-compensated employees are pumping iron at the charity's free gym, you can pump up your UBI too. Under new § 512(a)(7), an organization's unrelated business taxable income is increased by the amount of any expenses paid or incurred by the organization that are not deductible because of the limitations of § 274 for (i) qualified transportation fringe benefits (as defined in § 132(f)); (ii) a parking facility used in connection with qualified parking (as defined in § 132(f)(5)(C)); or (iii) any on-premises athletic facility (as defined in § 132(j)(4)(B)). New § 512(a)(7) is effective for amounts paid or incurred after 2017, so affected tax-exempt organizations need to deal with this change immediately. The Service has granted some relief, though, in the form of Notice 2018-100, 2018-52 I.R.B. 1074 (12/10/18), discussed further below. Moreover, Notice 2018-100 clarifies that with respect to on-premises athletic facilities UBI is increased under § 512(a)(7) only if the benefits provided discriminate in favor of highly-compensated employees.

Perhaps worth noting here: Because the TCJA reduced the top federal income tax rate on C corporations to 21 percent, it likewise reduced to 21 percent the top rate on UBI of tax-exempt organizations formed as nonprofit corporations, which are the vast majority. So, the news for tax-exempts is not all bad.

a. A tax law oxymoron: nonprofit trades or businesses. Huh? Notice 2018-67, 2018-36 I.R.B. 409 (8/21/18). Organizations described in §§ 401(a) (pension and retirement plans) and 501(c) (charitable and certain other entities) generally are exempt from federal income taxation. Nevertheless, §§ 511 through 514 impose federal income tax upon the "unrelated business taxable income" ("UBTI") of such organizations including for this purpose state colleges and universities. The principal sources of UBTI are §§ 512 and 513 "unrelated trade or business" gross income (minus deductions properly attributable thereto) and § 514 "unrelated debt-financed income" (minus deductions), including a partner's allocable share of income from a partnership generating UBTI. Prior to TCJA, exempt organizations could aggregate income and losses from unrelated trades or businesses before determining annual UBTI potentially subject to tax. Excess losses (if any) after aggregating all UBTI-related items of an exempt organization created a net operating loss subject to the rules of § 172. [See Reg. § 1.512(a)-1(a) prior to enactment of TCJA. After TCJA, § 172 permits only carryforwards.] Effective for taxable years beginning after 2017, however, TCJA added new § 512(a)(6) to disaggregate unrelated trades or businesses of exempt organizations for purposes of determining UBTI. Specifically, new § 512(a)(6) provides that for any exempt organization with more than one unrelated trade or business: (1) UBTI must be computed separately (including for purposes of determining any net operating loss deduction) for each such unrelated "trade or business;" and (2) total annual UBTI is equal to (i) the sum of positive UBTI from each such separate "trade or business" minus (ii) the specific $1,000 deduction allowed by § 512(b)(12). Under a special transition rule, unrelated business income net operating losses arising in a taxable year beginning before January 1, 2018 and carried forward to a taxable year beginning on or after such date, are not subject to new § 512(a)(6).

Now we get to the crux of the matter. The logical result of new § 512(a)(6) is that every exempt organization must segregate its unrelated trade or business income and losses for purposes of determining its annual UBTI. Yet, Treasury and Service have never defined separate "trades or businesses" for this purpose or, frankly, for any other federal income tax purpose. Further complicating matters, TCJA also enacted a related subsection, new § 512(a)(7), that increases an exempt organization's UBTI by expenses for which a deduction is disallowed under certain provisions of §§ 274 and 132 (specified transportation, parking, and athletic facility fringe benefits) *unless* the expense is "directly connected with an unrelated trade or business which is regularly carried on by the organization." Thus, new § 512(a)(7) also requires identification of each unrelated "trade or business" of an exempt organization, but § 512(a)(7) has the further deleterious effect of potentially creating UBTI for an exempt organization that otherwise has no unrelated trade or business. In Notice 2018-

67, Treasury and Service take the first step toward providing guidance with respect to both § 512(a)(6) and (7) and delineating separate trades or businesses for UBIT purposes.

What's in the Notice? Aside from requesting comments, Notice 2018-67 is lengthy (36 pages) and contains thirteen different "SECTIONS," ten of which address substantive, technical aspects of new § 512(a)(6) and (7). The high points are summarized below, but Notice 2018-67 is a must read for tax advisors to § 501(c) organizations, state colleges and universities, and § 401(a) pension and retirement plans, especially where those entities have UBTI from partnership interests they hold as investments. To summarize:

1. *General Rule.* Until proposed regulations are published, all exempt organizations affected by the changes to § 512(a)(6) and (7) may rely upon a "reasonable, good-faith interpretation" of §§ 511 through 514, considering all relevant facts and circumstances, for purposes of determining whether the organization has more than one unrelated trade or business. Because of the way § 512(a)(6) operates, exempt organizations will be inclined to conclude that they have only one unrelated trade or business, but that is not easy to do given the so-called "fragmentation" principle of § 513(c) and Reg. § 1.513-1(b). For example, advertising income earned by an exempt organization (e.g., National Geographic) from ads placed in the organization's periodical is UBTI even if subscription income is not UBTI. For an exempt organization this general rule includes using a reasonable, good-faith interpretation when determining: (a) whether to separate debt-financed income described in §§ 512(b)(4) and 514; (b) whether to separate income from a controlled entity described in § 512(b)(13); and (c) whether to separate insurance income earned through a controlled foreign corporation as described in § 512(b)(17). The use of the 6-digit code North American Industry Classification System ("NAICS") for segregating trades or businesses will be considered a reasonable, good-faith interpretation until regulations are proposed.

2. *Partnership Interests*. In general, partnership activities are attributable to partners such that holding a partnership interest can result in multiple lines of UBTI being considered allocable to an exempt organization partner. Until proposed regulations are issued, however, exempt organizations (other than § 501(c)(7) social clubs) may rely upon either of two rules for aggregating multiple lines of UBTI from a partnership, including UBTI attributable to lower-tier partnerships and unrelated debt-financed income:

    - The "interim rule" that permits the aggregation of multiple lines of UBTI from an exempt organization's interest in a single partnership if the partnership meets either a "de minimis test" or a "control test." The de minimis test generally is met if the exempt organization partner holds a 2 percent or less capital and profits interest in a partnership. The control test generally is met if the exempt organization partner holds a 20 percent or less capital interest in a partnership and does not have "control or influence" over the partnership. Control or influence over a partnership is determined based upon all relevant facts and circumstances. For purposes of determining an exempt organization's percentage interest in a partnership under the interim rule, partnership interests held by disqualified persons (as defined in § 4958), supporting organizations (as defined in § 509(a)(3)), and controlled entities (as defined in § 512(b)(13)(D)) must be considered.

    - The "transition rule" that permits the aggregation of multiple lines of UBTI from an exempt organization's interest in a single partnership if the interest was acquired prior to August 21, 2018. For example, if an organization has a 35 percent interest in a partnership [acquired] prior to August 21, 2018, it can treat the partnership as being in a single unrelated trade or business even if the partnership's investments generated UBTI from various lower-tier partnerships that were engaged in multiple types of trades or businesses (or, presumably, from debt-financed income).

3. *IRC § 512(a)(7)*. Income under § 512(a)(7) [i.e., the UBIT increase for expenses not directly connected with an unrelated trade or business regularly carried on by the organization and for which a deduction is disallowed under certain provisions of §§ 274 and 132 (specified transportation, parking, and athletic facility fringe benefits)] is not income from a trade or

business for purposes of § 512(a)(6). Thus, such UBIT appears to be entirely separate from § 512(a)(6) income and therefore not offset by any deductions or losses.

4. *GILTI*. An exempt organization's inclusion of global intangible low-taxed income ("GILTI") under § 951A is treated as a dividend which is not UBTI (pursuant to § 512(b)(1)) unless it is debt-financed (and thus included in UBIT under § 512(b)(4)).

b. Guidance on determining the increase to UBTI for employer-provided parking. Notice 2018-99, 2018-52 I.R.B. 1067 (12/10/18). In this notice, the Service announced that Treasury and the Service will issue proposed regulations under §§ 274 and 512 that will include guidance on determining the calculation of increased unrelated business taxable income (UBTI) of tax-exempt organizations that provide qualified transportation fringes (and also the nondeductible parking expenses and other expenses for qualified transportation fringes provided by non-tax-exempt employers). Until further guidance is issued, employers that own or lease parking facilities where their employees park can rely on interim guidance provided in the notice to determine the increase in the amount of UBTI under § 512(a)(7) attributable to nondeductible parking expenses. The guidance in the notice for determining the increase in UBTI mirrors the guidance for determining the nondeductible parking expenses of non-tax-exempt employers summarized earlier in this outline. The notice explains that an increase to UBTI is not required "to the extent the amount paid or incurred is directly connected with an unrelated trade or business that is regularly carried on by the organization" because, in such a case, the expenses for qualified transportation fringes are disallowed by § 274(a)(4) as a deduction in calculating the UBTI of the unrelated trade or business. The notice confirms that the effect of the increase in UBTI can be to require a tax-exempt organization to file Form 990-T, *Exempt Organization Business Income Tax Return*, if the organization's gross income included in computing UBTI is $1,000 or more. The rules for determining the increase in UBTI are illustrated by examples 9 and 10 in the notice.

c. Never had UBTI or paid estimated taxes thereon? Not to worry, says the IRS. Notice 2018-100, 2018-52 I.R.B. 1074 (12/10/18). Prior to the enactment of § 512(a)(7), many if not most § 501(c)(3) organizations had never reported UBTI or paid any unrelated business income tax ("UBIT") thereon. Organizations that owe UBIT are required to pay estimated taxes or suffer penalties. *See* IRC § 6655(c) and (d)(1)(A). Furthermore, because these organizations have never paid UBIT, they would not be eligible for the safe harbor exclusion for estimated taxes under § 6655(d)(1) (estimated payments equal to prior year's UBIT). Accordingly, with new § 512(a)(7) catching most tax-exempt organizations off guard, the Service has decided "in the interest of sound tax administration" (in other words, to prevent another Boston Tea Party) to waive the penalty for failure to make estimated UBIT payments for such exempt organizations. Note, however, the penalty waiver is limited to "tax-exempt organizations that provide qualified transportation fringes (as defined in § 132(f)) and any parking facility used in connection with qualified parking (as defined in §132(f)(5)(C)) to an employee to the extent that the underpayment of estimated income tax results from enactment of [§§ 13304(c) and 13703 of the 2017 Tax Cuts and Jobs Act]." Furthermore, the relief is available only to a tax-exempt organization that was not required to file a Form 990-T (the UBIT form) for the taxable year immediately preceding the organization's first taxable year ending after December 31, 2017. Notice 2018-100 does not address the possibility of estimated UBIT payments attributable to discriminatory on-premises athletic facilities. To avail themselves of the relief granted by the Notice, exempt organizations must write "Notice 2018-100" on the top of the organization's Form 990-T.

B. Charitable Giving

1. This taxpayer took a swing at getting a charitable contribution deduction for a golf course conservation easement, but was distracted by a PLR and whiffed the "extinguishment regulation." PBBM Rose Hill, Ltd. v. Commissioner, 900 F.3d 193 (5th Cir. 9/14/18). The taxpayer, a TEFRA partnership, had paid approximately $2.4 million for 241.48 acres of golf course property in 2002. The property was deed-restricted for use as a golf course, but by 2007 it was clear that operating a golf course on the property was not economically viable. Therefore, in July of 2007, the taxpayer entered into a judicially-approved settlement agreement with certain interested parties, including a neighboring property owner's association ("POA"), that removed the golf course deed restriction over the land. Then, in August of 2007, the taxpayer agreed to sell the land to the POA for $2.3 million. Meanwhile, in December of 2007, the taxpayer granted a conservation easement over approximately 234 acres of the property to the North American Land Trust ("NALT"). Consistent with § 170(h)(4)(a)(i)-(iv), the conservation easement deed required the land to remain undeveloped (i) "for outdoor recreation by, or education of, the general public;" (ii) "as a relatively natural habitat of fish, wildlife, or plants;" (iii) "for open space which provides scenic enjoyment to the general public;" and (iv) "as open space which, if preserved, will advance [government conservation policy] and will yield a significant public benefit." On its 2007 partnership tax return, the taxpayer claimed a charitable contribution deduction for the easement of approximately $15 million. Subsequently, in January of 2008, the taxpayer sold the property to the POA for $2.3 million. The POA then operated the property as a golf course and a park, but limited public access to the property via a gatehouse and "residents only" signs. On audit, the Service disallowed the taxpayer's charitable contribution deduction on two grounds: (1) due to the POA's use of the land as a golf course and park primarily for nearby homeowners and very limited public benefit, the easement failed to meet the "conservation purposes" requirement of § 170(h)(4)(a)(i)-(iv) in execution even if the proper language was in the deed; and (2) the rights reserved to the taxpayer-grantor (and the POA as successor) in the easement deed did not comply with the "extinguishment regulation," thus failing the "protected in perpetuity" requirement of § 170(h)(5)(A). After a five-day trial, the Tax Court upheld the Service's position on both grounds. The Tax Court also held that the taxpayer overvalued the easement and thus was subject to overvaluation penalties. The taxpayer appealed to the Fifth Circuit which (in an written by Judge King) determined that the conservation purposes as expressed in the easement deed were sufficient to meet the "conservation purposes" requirement of § 170(h)(4)(a)(i)-(iv) notwithstanding the actual private use of the property by the POA because the Service could not demonstrate that the taxpayer knew the POA would restrict public access and NALT would fail to object. Nevertheless, the Fifth Circuit agreed with the Tax Court that the "protected in perpetuity" requirement of § 170(h)(5)(A) was not met because the taxpayer's easement deed failed to meet the "extinguishment regulation" (Reg. § 1.170A-14(g)(6)). The extinguishment regulation ensures that conservation easement property is protected in perpetuity because, upon destruction or condemnation of the property and collection of any proceeds, the charitable donee must proportionately benefit. The charitable donee's proportionate benefit is determined by a fraction equal to the value of the easement at the time of the gift as compared to the total value of the property at the time of the gift. This extinguishment language must be in the conservation easement deed. The taxpayer's deed, however, followed Priv. Ltr. Rul. 200836014 (9/5/08) and allowed the taxpayer (or the taxpayer's successor, the POA) to recover the value of any improvements to the property before determining the charitable donee's proportionate benefit. The Fifth Circuit determined that this was not allowed under the plain language of Reg. § 1.170A-14(g)(6) notwithstanding the Service's prior determination to the contrary. The Fifth Circuit further agreed with the Tax Court that overvaluation penalties were appropriately imposed against the taxpayer.

2. In a conservation easement case appealable to the Eleventh Circuit, the Tax Court says again to the Fifth Circuit that we think you got it wrong in BC Ranch II so we're not going to follow your decision, but we are going to follow our Belk decision which was affirmed by the Fourth Circuit. Pine Mountain Preserve, LLLP v. Commissioner, 151 T.C. No. 14 (12/27/18) and Pine Mountain Preserve, LLLP v. Commissioner, T.C. Memo. 2018-214 (12/27/18). In a late-in-the-year development deserving more robust treatment when publication deadlines permit—and when we have the stamina to digest 150+ pages of opinion—the Tax Court disallowed a taxpayer's claimed charitable contribution deduction for a conservation easement. Despite the taxpayer's argument to the contrary, the Tax Court refused to follow the Fifth Circuit's opinion in *B.C. Ranch II, L.P. v. Commissioner*, 867 F.3d 547 (5th Cir. 2017), *vacat'g and remand'g* T.C. Memo. 2015-130, regarding the "protected in perpetuity" requirement for qualified conservation easements. *BC Ranch II* held that the "protected in perpetuity" requirement is not violated if the taxpayer-grantor reserves certain rights to reclaim property subject to a conservation easement while substituting other property therefor. On the other hand, the Tax Court and the Fourth Circuit in *Belk v. Commissioner*, 140 T.C. 1 (2013), *aff'd*, 774 F.3d 221 (4th Cir. 2014), determined that such substitution of property is not permissible under the "protected in perpetuity" requirement.

X. TAX PROCEDURE

A. Interest, Penalties, and Prosecutions

1. The Service can assess restitution a person has been ordered to pay upon conviction of violating section 7201 when the wrongdoing consisted of aiding and abetting the evasion of payment of a third party's tax liability. Bontrager v. Commissioner, 151 T.C. No. 12 (12/12/18). The taxpayer pleaded guilty to violating § 7201, which criminalizes any willful attempt to evade and defeat tax. The basis for the taxpayer's conviction was that he had aided and abetted his father's evasion of tax. In connection with the criminal proceeding, the U.S. District Court sentenced the taxpayer to one year in prison and three years of supervised release and ordered him to pay criminal restitution in the amount of $72,710. The Service subsequently assessed the restitution pursuant to § 6201(a)(4)(A), which provides—for criminal restitution paid after August 16, 2010—that the Service

> shall assess and collect the amount of restitution under an order pursuant to section 3556 of title 18, United States Code, for failure to pay any tax imposed under this title in the same manner as if such amount were such tax.

The Service subsequently filed a notice of federal tax lien, in response to which the taxpayer requested a collection due process hearing. Among other issues raised by the taxpayer, the settlement officer who conducted the CDP hearing rejected the taxpayer's argument that the Service had no legal authority to assess the restitution. Specifically, the taxpayer argued that assessment of the restitution was not authorized by § 6201(a)(4)(A)—which authorizes assessment of restitution "for failure to pay any tax imposed under this title"—because the restitution was not for *his* failure to pay tax, but rather for his father's failure to pay tax. In reviewing the notice of determination issued following the CDP hearing, the Tax Court (Judge Lauber) held that § 6201(a)(4)(A) authorized assessment of the restitution. The court reasoned that neither § 7201 nor § 6201(a)(4) requires that the tax imposed be a tax imposed on the person ordered to pay the restitution.

> Section 7201 criminalizes any willful attempt to evade payment of "any tax imposed by this title." Section 6201(a)(4) authorizes the assessment of restitution "for failure to pay any tax imposed under this title." Petitioner was ordered to pay restitution for aiding and abetting Winston's failure to pay Federal income tax. That tax was clearly "[a] tax imposed under this title."

The court also rejected the taxpayer's argument that his restitution obligation had been discharged in bankruptcy.

B. Discovery: Summonses and FOIA

C. Litigation Costs

D. Statutory Notice of Deficiency

E. Statute of Limitations

F. Liens and Collections

1. A meeting with an IRS collections officer is not a prior administrative proceeding that precludes a collection issue from being raised in a subsequent CDP hearing. Loveland v. Commissioner, 151 T.C. No. 7 (9/25/18). The taxpayers in this case, a married couple, were a retired boilermaker who left the workforce for health reasons and a retired teacher who survived breast cancer. They had outstanding federal tax liabilities of over $60,000. In response to a final notice of intent to levy, the taxpayers did not request a collection due process hearing, but instead entered into negotiations with a Service collections officer. They submitted an offer-in-compromise on Form 433A (OIC) together with accompanying financial information. They also argued that their health issues combined with the loss of their home to foreclosure constituted special circumstances that limited their ability to pay. The collections officer rejected their offer and concluded that they could pay the full amount of the liability. They initially appealed the decision but withdrew the appeal when they were informed that they could not negotiate an installment agreement if the appeal was pending. While negotiations over the installment agreement were pending, the taxpayers made voluntary payments of $800 per month and sought a mortgage loan on property they owned in order to pay the tax liability.

On the same day they submitted their loan application, the Service filed a notice of federal tax lien, which had the effect of precluding the taxpayers from obtaining the mortgage loan. In response to the notice of federal tax lien, they requested a CDP hearing. They requested that the lien be released and asserted that the lien was causing economic hardship. The Appeals Officer assigned to their matter requested financial information on Form 433-A and supporting documents. In response, the taxpayers sent a letter asking the Appeals Officer to consider their previously rejected offer-in-compromise and attached to the letter their earlier Form 433A (OIC) and accompanying financial information, the letter by which they had initially appealed the earlier decision, and Form 433-D, Installment Agreement, in which they requested payments of $800 per month. The Appeals Officer determined that the taxpayers qualified for an 84-month installment agreement of $853, which would fully pay the liability. However, the Appeals Officer declined to review either the taxpayers' offer-in-compromise (because they had not properly appealed it) or their requested partial-pay installment agreement (because they had not submitted the necessary financial information). In response to an adverse notice of determination, the taxpayers filed a petition in the Tax Court. The Tax Court (Judge Buch) held that the taxpayers were not precluded from requesting an offer-in-compromise in the CDP hearing. Section 6330(c)(4)(A)(i) precludes an issue from being raised in a CDP hearing if "the issue was raised and considered at a previous hearing under section 6320 or in any other previous administrative or judicial proceeding." The court held, however, that prior negotiations with a collections officer outside of a CDP hearing are not a prior administrative hearing for purposes of § 6330(c)(4)(A)(i). Therefore, the taxpayers were able to request an offer-in-compromise in their CDP hearing. The Service's failure to consider it, the court held, was an abuse of discretion. The court also held that it was an abuse of discretion for the Service to decline to review the taxpayers' request for an installment agreement. The stated reason for failing to review the taxpayers' requested installment agreement was not that the financial information they had submitted was out of date, but rather that they had not submitted financial information, which they had. Finally, the court held that it was an abuse of discretion for the Service to consider the taxpayers' claim that full payment of the liability would cause economic hardship. The court remanded to the Appeals Office for further consideration.

2. The taxpayers' attempt to pay their federal tax liability went awry when the Service levied on the bank account on which their check was drawn and applied the proceeds to other tax years. Following a CDP hearing, the appropriate standard of review is for abuse of discretion, says the Tax Court. Melasky v. Commissioner, 151 T.C. No. 8 (10/10/18). The taxpayers hand-delivered to the Service at the Service's office in Houston a check for $18,000 and requested that the check be applied against their 2009 federal income tax liability. The Service accepted the check and initially applied it as the taxpayers had requested. A few days later, however, the Service levied against the bank account on which the check had been drawn and applied the proceeds of the levy to an earlier tax year. The effect of the levy was that the taxpayers' check bounced. The Service therefore reversed the payment against the 2009 liability and charged a $360 penalty for writing a bad check. On the same day as the levy, the Service issued to the taxpayers a final notice of intent to levy with respect to certain years, including 2009. In response, the taxpayers requested a CDP hearing. The Service's settlement officer issued a notice of determination concluding that the proceeds of the levy constituted an involuntary payment, rather than a voluntary payment, and that the Service therefore was free to apply the payment as it wished. In response to the notice of determination, the taxpayers filed a petition in the Tax Court. The Tax Court (Judge Holmes) held that the appropriate standard of review in the Tax Court was for abuse of discretion. In its earlier decision in *Goza v. Commissioner*, 114 T.C. 176 (2000), the court had established that the standard of review in a CDP case is normally for abuse of discretion, but that the standard of review is *de novo* when the underlying tax liability is appropriately before the court. The parties agreed that the standard of review for the 2009 tax year was de novo because the taxpayers contended that they had no tax liability for that year. Nevertheless, the court held that the standard of review was for abuse of discretion because the taxpayers were not challenging the underlying tax liability, but rather were challenging whether the Service properly applied a payment:

> The question for the Melaskys' 2009 tax year is about whether the IRS properly applied a check. A question about whether the IRS properly credited a payment is not a challenge to a tax liability; i.e., the amount of tax *imposed* by the Code for a particular year. It is instead a question of whether the liability remains *unpaid*. Section

6330(c)(2)(A) allows a taxpayer to raise at a CDP hearing "any relevant issue relating to the unpaid tax," whereas section 6330(c)(2)(B) says a taxpayer may challenge "the existence or amount of the *underlying tax liability*" (emphasis added) only if he didn't receive a notice of deficiency or otherwise have an opportunity to do so. See Kovacevich v. Commissioner, T.C. Memo. 2009-160, 2009 WL 1916351, at *6. We therefore hold here that the Melaskys aren't challenging their underlying liability for 2009. See also Chief Counsel Notice CC-2014-002 (May 5, 2014) (announcing similar IRS position).

a. A dishonored check is not a voluntary payment of tax and therefore the Service need not apply the tendered check as directed by the taxpayer, even when the check is dishonored because an IRS levy depleted the funds in the bank account. Melasky v. Commissioner, 151 T.C. No. 9 (10/10/18). In this separate, reviewed opinion (9-2-2) by Judge Thornton involving the same facts as *Melasky v. Commissioner*, 151 T.C. No. 8 (10/10/18), the Tax Court considered whether it was an abuse of discretion for the Service to decide: (1) not to apply against the taxpayers' 2009 income tax liability the proceeds of the levy on their bank account, and (2) to reject the taxpayers' proposed installment agreement. With respect to application of the levy proceeds, the court noted that the Service's policy is to apply voluntary payments as directed by the taxpayer, but that involuntary payments generally may be applied against whatever unpaid tax liabilities the Service chooses. The court rejected the taxpayers' argument that the check for $18,000 they hand-deliverd to the Service's office in Houston should be treated as a voluntary payment and therefore applied to 2009 as the taxpayers had directed. A payment by check, the court reasoned, is a conditional payment and is subject to the condition subsequent that the check be paid when presented to the drawee (the bank). If the condition subsequent is fulfilled, the court explained, "the payment generally becomes absolute and is deemed to relate back to the time when the check was provided." According to the court, acceptance of a check is not an absoulte payment in the absence of an agreement that the check will be treated as an absolute payment. In this case, because the check was not honored, and there was no agreement that acceptance of the check would be teated as an absolute payment, the check was not a voluntary payment. The court rejected the taxpayers' argument that, because the Service's levy on the bank account led to the check being dishonored, a different result was warranted. It was not unreasonable or inappropriate, the court stated, for the Service to levy after approximately fifteen years of collection activity. The proceeds of the levy were an involuntary payment that the Service could apply as it chose. With respect to the second issue, the court held that it was not an abuse of discretion for the Service to reject the taxpayers' proposed partial-pay installment agreement.

- A concurring opinion by Judge Lauber (joined by Judges Thornton, Marvel, Gustafson, Kerrigan, Buch, Nega, Pugh, and Ashford) is highly critical of and responds to certain arguments in the dissenting opinion by Judge Holmes. Generally, the concurring opinion takes the position that the taxpayers did not raise in the CDP hearing the argument that the $18,000 check, although dishonored, should be treated as a voluntary payment, and therefore "[t]he SO did not commit legal error by failing to address an argument petitioners did not make."

- A concurring opinion by Judges Buch and Pugh (joined by Judges Gustafson and Paris) notes that Rev. Proc. 2002-26 requires the Service to apply a voluntary payment as directed by the taxpayer, and that the court's opinion does not "foreclose finding an abuse of discretion if evidence were to show that, through negligence or malfeasance, the Commissioner circumvented his own revenue procedure for designating payments."

- Judge Holmes wrote a lengthy dissenting opinion that was joined by Judge Morrison. Judge Holmes agreed that the settlement officer did not abuse his discretion in rejecting the taxpayers' proposed installment agreement, although for different reasons than those set forth in the court's opinion. Judge Holmes dissented with respect to the treatment of the $18,000 dishonored check. According to the dissenting opinion, the check was a voluntary payment that the Service should have applied as directed by the taxpayers.

G. Innocent Spouse

H. Miscellaneous

XI. <u>WITHHOLDING AND EXCISE TAXES</u>

XII. <u>TAX LEGISLATION</u>

XIII. <u>TRUSTS, ESTATES & GIFTS</u>

Recent Developments in Federal Income Taxation

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State Bar of Texas Tax Section
First Wednesday Tax Update
April 3, 2019

To obtain today's outline and slides:
https://tinyurl.com/outline0419

https://tinyurl.com/slides0419

Gaylor v. Mnuchin,
___ F.3d ___ (7th Cir. 3/15/19)
Outline: item A.1, page 2

- Holds the parsonage allowance exclusion of 107(2) to be constitutional.

Deduction of State and Local Taxes
Outline: item D.1, page 3

- TCJA: An individual's itemized deductions on Schedule A for state taxes cannot exceed $10,000.
  - Applies to aggregate of property taxes, and sales or income taxes.
  - Limit applies both to single individuals and married individuals filing jointly
  - Applies 2018 through 2025
- Some states have adopted workarounds, e.g., New Jersey gives a credit against property taxes for contributions to certain charitable funds designated by the state.
- <u>Notice 2018-54 (5/23/18)</u>: proposed regulations will "make clear that the requirements of the Internal Revenue Code, informed by substance-over-form principles, govern the federal income tax treatment of such transfers."

Deduction of State and Local Taxes
Outline: item D.1.b, page 4

- Proposed regulations: 83 Fed. Reg. 43,563 (8/27/18).
  - Apply to contributions *after* 8/27/18.
- The proposed regulations:
  - Generally require taxpayers to reduce the amount of any federal income tax *charitable contribution deduction* by the amount of any corresponding state or local tax *credit*.
    - Provide an exception: a taxpayer's federal charitable contribution deduction is *not* reduced if the corresponding state or local credit does not exceed 15 percent of the taxpayer's federal deduction.
    - Example: T contributes $1,000 to state charity and gets 10% state tax credit.
  - Provide that a *state or local tax deduction* normally will *not* reduce a taxpayer's federal *deduction* (provided the state and local deduction does not exceed the taxpayer's federal deduction).

5

Deduction of State and Local Taxes
IRS News Release IR-2018-178 (9/5/18)
Rev. Proc. 2019-12, 2019-04 I.R.B. 401 (12/29/18)
Outline: item D.1.c-d, page 5

- This News Release provides:
  - If a payment to a government agency or charity qualifies as an ordinary and necessary business expense under § 162(a), it is not subject to disallowance in the manner in which deductions under § 170 are subject to disallowance.
  - This is true regardless of whether the taxpayer is doing business as a sole proprietor, partnership or corporation.
- Rev. Proc. 2019-12:
  - Sets forth safe harbors for C corporations and "specified passthrough entities."
  - General principle: the taxpayer's federal charitable contribution deduction is reduced by any state tax credit, but the balance of the payment can be a business expense deduction under § 162 if the payment is made with a business purpose.

6

Deduction of State and Local Taxes
Rev. Rul. 2019-11, 2019-__ I.R.B. ___ (3/29/19)
Outline: item D.1.e, page 6

- Addresses application of the tax benefit rule to those whose deductions for state and local taxes have been limited to $10,000.
- The tax benefit rule has long required taxpayers to include in gross income amounts deducted in a prior tax year that are recovered in the current tax year.
- However, under § 111(a), the amount so includible in gross income is limited to the amount deducted that resulted in a reduction of the taxpayer's tax liability for the prior year.
- In other words, the inclusion in gross income of the amount recovered is limited to the "tax benefit" of the amount previously deducted.

Deduction of State and Local Taxes
Rev. Rul. 2019-11, 2019-__ I.R.B. ___ (3/29/19)
Outline: item D.1.e, page 6

- *Situation 1 (State income tax refund fully includable).*
- *Facts:* Taxpayer A paid local real property taxes of $4,000 and state income taxes of $5,000 in 2018. A's state and local tax deduction was not limited by section 164(b)(6) because it was below $10,000. Including other allowable itemized deductions, A claimed a total of $14,000 in itemized deductions on A's 2018 federal income tax return. In 2019, A received a $1,500 state income tax refund due to A's overpayment of state income taxes in 2018.
- *Held:* In 2019, A received a $1,500 refund of state income taxes paid in 2018. Had A paid only the proper amount of state income tax in 2018, A's state and local tax deduction would have been reduced from $9,000 to $7,500 and as a result, A's itemized deductions would have been reduced from $14,000 to $12,500, a difference of $1,500. A received a tax benefit from the overpayment of $1,500 in state income tax in 2018. Thus, A is required to include the entire $1,500 state income tax refund in A's gross income in 2019.

Deduction of State and Local Taxes
Rev. Rul. 2019-11, 2019-__ I.R.B. ___ (3/29/19)
Outline: item D.1.e, page 6

- *Situation 2 (State income tax refund not includable)*
- *Facts:* Taxpayer B paid local real property taxes of $5,000 and state income taxes of $7,000 in 2018. Section 164(b)(6) limited B's state and local tax deduction on B's 2018 federal income tax return to $10,000, so B could not deduct $2,000 of the $12,000 state and local taxes paid. Including other allowable itemized deductions, B claimed a total of $15,000 in itemized deductions on B's 2018 federal income tax return. In 2019, B received a $750 state income tax refund due to B's overpayment of state income taxes in 2018.
- *Held:* In 2019, B received a $750 refund of state income taxes paid in 2018. Had B paid only the proper amount of state income tax in 2018, B's state and local tax deduction would have remained the same ($10,000) and B's itemized deductions would have remained the same ($15,000). B received no tax benefit from the overpayment of $750 in state income tax in 2018. Thus, B is not required to include the $750 state income tax refund in B's gross income in 2019.

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Deduction of State and Local Taxes
Rev. Rul. 2019-11, 2019-__ I.R.B. ___ (3/29/19)
Outline: item D.1.e, page 6

- *Situation 3 (State income tax refund partially includable)*
- *Facts:* Taxpayer C paid local real property taxes of $5,000 and state income taxes of $6,000 in 2018. Section 164(b)(6) limited C's state and local tax deduction on C's 2018 federal income tax return to $10,000, so C could not deduct $1,000 of the $11,000 state and local taxes paid. Including other allowable itemized deductions, C claimed a total of $15,000 in itemized deductions on C's 2018 federal income tax return. In 2019, C received a $1,500 state income tax refund due to C's overpayment of state income taxes in 2018.
- *Held:* In 2019, C received a $1,500 refund of state income taxes paid in 2018. Had C paid only the proper amount of state income tax in 2018, C's state and local tax deduction would have been reduced from $10,000 to $9,500 and as a result, C's itemized deductions would have been reduced from $15,000 to $14,500, a difference of $500. C received a tax benefit from $500 of the overpayment of state income tax in 2018. Thus, C is required to include $500 of C's state income tax refund in C's gross income in 2019.

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Deduction of State and Local Taxes
Rev. Rul. 2019-11, 2019-__ I.R.B. ___ (3/29/19)
Outline: item D.1.e, page 6

- *Situation 4 (Standard deduction)*
- *Facts:* Taxpayer D paid local real property taxes of $4,250 and state income taxes of $6,000 in 2018. Section 164(b)(6) limited D's state and local tax deduction on D's 2018 federal income tax return to $10,000, so D could not deduct $250 of the $10,250 state and local taxes paid. Including other allowable itemized deductions, D claimed a total of $12,500 in itemized deductions on D's 2018 federal income tax return. In 2019, D received a $1,000 state income tax refund due to D's overpayment of state income taxes in 2018.
- *Held:* In 2019, D received a $1,000 refund of state income taxes paid in 2018. Had D paid only the proper amount of state income tax in 2018, D's state and local tax deduction would have been reduced from $10,000 to $9,250, and, as a result, D's itemized deductions would have been reduced from $12,500 to $11,750, which is less than the standard deduction of $12,000 that D would have taken in 2018. The difference between D's claimed itemized deductions ($12,500) and the standard deduction D could have taken ($12,000) is $500. D received a tax benefit from $500 of the overpayment of state income tax in 2018. Thus, D is required to include $500 of D's state income tax refund in D's gross income in 2019.

11

Johnson v. Commissioner,
152 T.C. No. 6 (3/11/19)
Outline: item D.2, page 8

- Addresses receipt of lump sum Social Security benefits and the determination of modified adjusted gross income for purposes of eligibility for the § 36B premium tax credit

12

Notice 2019-20
2019-14 I.R.B. 927 (3/7/19)
Outline: item G.1, page 9

- Provides penalty relief for failure of partnerships to report negative tax capital account information on Schedule K-1

13

Walquist v. Commissioner,
152 T.C. No. 3 (2/25/19)
Outline: item A.1, page 10

- Holds that accuracy-related penalties determined by the IRS's Automated Correspondence Exam System are "automatically calculated through electronic means."
- Therefore, they are exempt from the section 6751(b) supervisory approval requirement.

14

Palmolive Building Investors, LLC v. Commissioner, 152 T.C. No. 4 (2/28/19)
Outline: item A.2, page 10

- Holds section 6751(b) supervisory approval requirement does not require that all penalties be determined at the same time.

15

ATL & Sons Holdings, Inc. v. Commissioner, 152 T.C. No. 8 (3/13/19)
Outline: item A.3, page 11

- Holds that filing an extension request for an individual S corporation shareholder's return does not extend the time to file the S corporation's return.

16

Gregory v. Commissioner, 152 T.C. No. 7 (3/13/19)
Outline: item D.1, page 12

- Holds that filing a power of attorney on Form 2848 does not provide the IRS with clear and concise notification of the taxpayer's new address.

Campbell v. Commissioner, T.C. Memo. 2019-4 (2/4/19)
Outline: item F.1, page 13

- Holds that IRS abused its discretion in the context of a CDP hearing.

IS THAT REALLY THE LAW: NEWEST ERISA RULES

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- Co-Chair of the Employee Benefits Committee of the Tax Section of the State Bar of Texas
- Board Chair of KCBI radio FM 90.9 and other civic and charitable organizations
- Leadership Dallas
- SMU Dedman School of Law
- Texas Tech University
- Married to Sheila

E. R. I. S. A.

- E mployee
- R etirement
- I ncome
- S ecurity
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- Of
- 1974

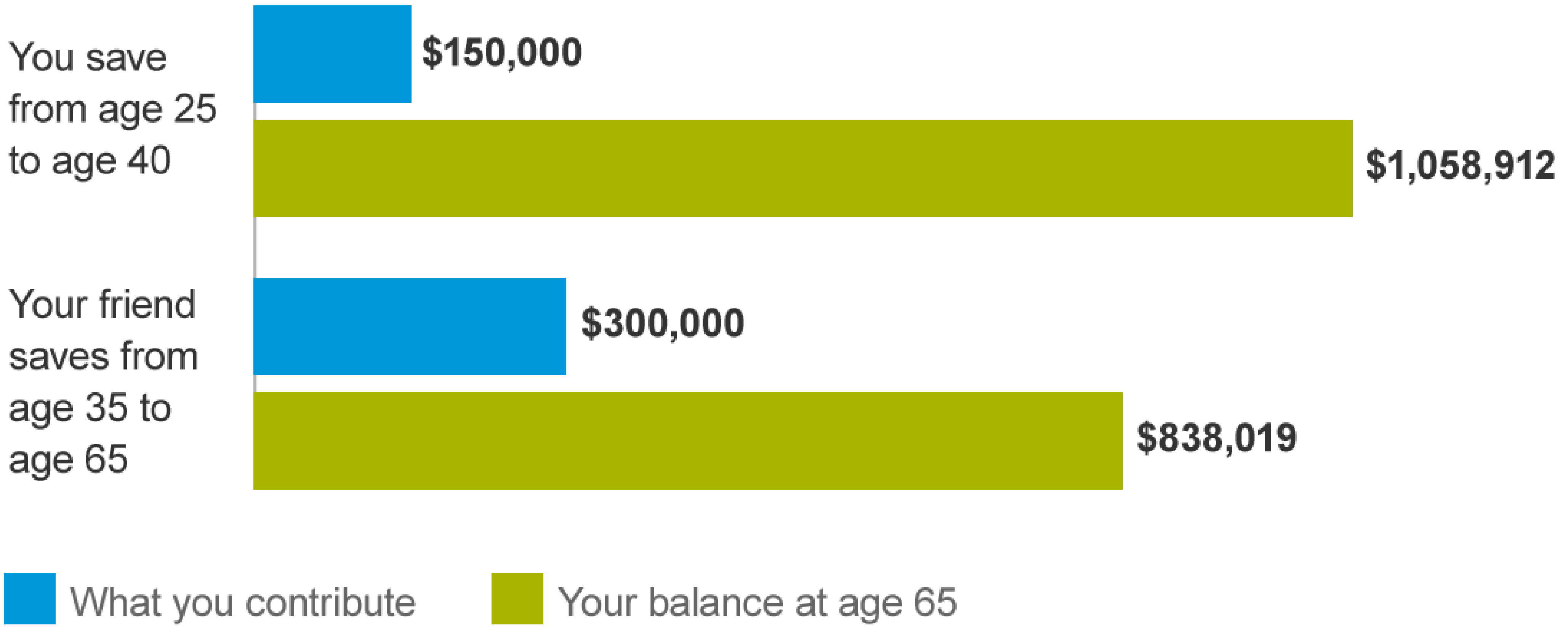
Topics

- Some Really New Things
- 401(k) Matching Contributions for Student Loan Repayments
- The Coaches Tax (Oops)
- Newest Kind of Stock Options
- Nonprofit Parking Tax

401(k) Matching Contributions for Student Loan Repayments—The Problem

- No more pension plans
- 401(k)/403(b) plans
  - Employees have to buy the free money
- Other Priorities
  - Debt
  - Other obligations

401(k) Matching Contributions for Student Loan Repayments—The Problem



401(k) Matching Contributions for Student Loan Repayments—The Problem

- Why Employers Should Care
  - Recruiting
  - Retention
  - Socially responsible
  - Competitive
  - Burn out
  - Employee morale

401(k) Matching Contributions for Student Loan Repayments--Solutions

- How Employers Can Help
  - Debt consolidation and refinancing
  - Direct pay
    - Bonus
  - 401(k) benefits

401(k) Matching Contributions for Student Loan Repayments—Abbott Laboratories

- "Matching" contribution
  - Inside the 401(k) plan
  - Tied to an employee's student loan repayments outside the 401(k) plan
- Contingent benefit rule
  - Employer cannot give employees a $50 cash bonus as an incentive to sign up for, and contribute to, the 401(k) plan.
- Private Letter Ruling 201833012

401(k) Matching Contributions for Student Loan Repayments—What's Next

- Legislation
- What About 401(k) Incentives for Other Behavior
  - Buy new house or car
  - Have or adopt a child
  - Make a charitable contribution or pledge

The Coaches Tax (Oops)

- Trump Tax bill added Section 4960 to the Internal Revenue Code to penalize non-profit employers (i. e. charities) for paying excessive compensation.
- 21% penalty tax imposed on the non-profit employer.
- Effective for taxable years beginning after December 31, 2017.

The Coaches Tax (Oops)

- Tax applies to:
  - Remuneration over $1 million paid to a covered employee and
  - Excess parachute payments paid to a covered employee.
- IRS Notice 2019-09

The Coaches Tax (Oops)

- Applicable Tax-Exempt Organizations (“ATEO”)
  - Charities--Section 501(a)
  - Farmers’ cooperative--Section 521(b)
  - Governmental entity--Section 115(1)
  - Political organizations--Section 527
- What about state colleges and universities?

The Coaches Tax (Oops)

- Covered Employee
  - 5 highest paid employees in any year after 2016.
- Remuneration
  - Excludes amounts paid to a licensed medical professional for medical services.

The Coaches Tax (Oops)

- Tax On Severance Pay
  - Involuntary termination only
  - Excess parachute payments

Newest Kind of Stock Options

- Qualified Equity Grant
- Section 83(i)
  - 5 year income deferral
- Applies after December 31, 2017

Qualified Stock

- Received by the employee upon:
  - Exercise of a stock option
  - Settlement of a restricted stock unit (RSU)
- Private employers only; not a publicly traded corporation
- 80% participation

Excluded Employees

- An excluded employee is an individual who:
  - 1% owner
  - CEO or CFO or their family members
    - spouse, children, grandchildren, and parents
  - Top 4 highest paid officers

Nonprofit Parking Tax--Overview

- Tax-exempt employers must treat as unrelated business taxable income the cost of providing parking to their employees
  - Churches and other 501(c)(3) charities
- 21% tax on the charity; not the employee
- Applies starting in 2018

Non Profit Parking Tax—An Escape Hatch

- IRS Notice 2018-99 issued on December 10, 2018
- Charities that are excluded from the new tax
  - Charity has no reserved employee parking spaces
  - The charity’s parking facility is not used primarily by employees
- It is not an escape hatch that the charity (and thus the parking) is located in a rural area where there is lots of wide open space.

Non Profit Parking Tax—Another Escape Hatch

- A charity is not subject to the parking tax if the sum of the following items is less than $1,000:
  - Parking expenses allocable to reserved employee parking
  - Taxable amount from unreserved parking spaces
  - Gross revenue from any actual unrelated business activites

Non Profit Parking Tax—A Few Details

- Tax is based on the expense of providing parking for employees.
- “Parking facilities” include garages and parking lots.
- Applies to each geographic location of the employer.
- Method:
    - Determine total parking expenses, and then
    - Determine what portion of the total expenses is allocable to employee parking.

Non Profit Parking Tax—A Few Details

- Total Parking Expenses: The portion of the following expenses allocable to the organization's parking facilities and paid during the tax year:
  - Rent or lease payments
  - Interest
  - Repairs
  - Maintenance
  - Utility expenses
  - Insurance
  - Property taxes

  Leaf removal
  Trash removal
  Cleaning
  Landscape expenses
  Parking lot attendant
  Security
  Snow and ice removal

Non Profit Parking Tax—A Few Details

- Amounts paid by charity to a 3rd party for parking spaces
  - Total cost is subject to the tax
- Charity owns or leases all or a portion of one or more parking facilities where its employees park.
  - Reserved Space—a portion of the Total Parking Expenses must be allocated to reserved parking spaces
    - Reserved means exclusively reserved for employee use.
    - March 31, 2019 deadline to abandon reserved parking

Non Profit Parking Tax—A Few Details

- Determine total number of all parking spaces, including reserved parking
- Determine total number of parking spaces reserved for employee use.
- Determine the taxable portion of total parking expenses attributable to:
  - Reserved spaces
  - Employee use of nonreserved spaces
    - No amount attributable to nonreserved spaces is taxable if the nonreserved spaces are primarily (more than 50%) used to provide parking to the general public.

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THE GIFT TAX EXEMPTION COAST IS CLEAR

Time to go back into the water?

Authors
Charlie Ratner, Senior Director, Washington National Tax
Carol Warley, Partner, Private Client Services
Rebecca Warren, Senior Manager, Washington National Tax

In our Dec. 6, 2018 Tax Alert, The IRS says, “Yes, there is no clawback,” we noted that IRS issued proposed regulations that would effectively ensure that where a taxpayer made gifts of their entire exemption between 2018 and 2025 when the exemption was $11 million (indexed), and then passed away after 2025 when the exemption dropped to $5 million (indexed), the benefit of the higher exemption would not be retroactively eliminated.

Taxpayers who have identified opportunities to take advantage of the increased exemption before 2026 (or sooner if the political winds suggest a mid-course correction) but have been hesitant to do so because of the risk of clawback now find themselves on firmer ground for moving forward with those plans. However, with all of the ways and means of using the exemption, what should they do…and why?

Perhaps the first place to look for uses for the exemption is to fix problems with existing planning, especially if those problems are now straining the individual's cash flow or will cause unwanted or unproductive use of exemption down the road. Here are some situations that might call for application of exemption.

Forgiving debts from the children

Children borrowed from the 'Bank of Mom and Dad' to buy a home. The parents made sure that the transaction was documented properly, secured the loan with a mortgage on the home and have, in fact, made sure that the children paid the mortgage in accordance with its terms. The children, it seems, have read about the increased exemption and, after checking with their planner, have suggested that Mom and Dad's forgiveness of the balance due on the mortgage would be a smart tax planning move. Yes, the forgiveness would be a gift, but with the increased exemption, there would be no gift tax due. Mom and Dad are happy to oblige their obligors. They also mention, albeit in a stage whisper, that with the mortgage out of the way, the children will no longer need Mom and Dad's help on funding the grandchildren's education.

Shoring up 'underfunded' irrevocable life insurance trusts and split-dollar plans

Many individuals established irrevocable life insurance trusts (ILITs) to own policies earmarked for various financial and estate planning uses. The ILITs will keep the proceeds of the policies out of the individuals' taxable estates, but the ILITs have to be funded by gifts from the individuals. Those gifts may be covered by annual exclusions by way of a *Crummey* power. However, the premiums on large policies often exceed the available annual exclusions by a wide margin. Many of those who established ILITs expected that they would have to make gifts, annual exclusion or otherwise, for a certain number of years. They recognized (or were certainly told) that unless the premium was guaranteed, the expectation of the policy's being self-sufficient after a certain numbers of years was just that, an expectation, not a guarantee. Fast forward to today, and many of these individuals are looking at paying premiums for perhaps twice the number of years that they originally expected. To make matters worse, some of those policies were funded by split-dollar arrangements that were calibrated to 'roll out', meaning have enough cash value to enable the ILIT to repay the party advancing the premiums under the plan and be self-sufficient thereafter, after a certain number of years. Unfortunately, the rollout was utterly dependent on the performance of the policies and, with interest rates at historic lows for so many years now, the policies are a shadow of what they were projected to be when they were put in force (at higher rates). Here again, the individuals who established these arrangements are looking at many, many more years of absorbing the income and gift tax cost of supporting the arrangement.

Individuals who find themselves in these situations can consider using the increased exemption to fund their ILITs with income–producing (and hopefully discountable) assets such as S corporation stock or interests in family partnerships or limited liability companies. While this funding will use exemption, it will give the ILITs the means to service the policies and take over the payment of the economic benefit in the split-dollar arrangements, thereby saving the individuals significant future gifts.

A subset of the ILIT issue involves revisiting (and rewiring) the individual's life insurance program, which may now involve more insurance than they need for estate taxes. Even if the coverage is needed, it could make sense to see if the premiums could be reduced because the coverage is not going to be needed for as many years as originally anticipated.

Shoring up 'underperforming' or under-capitalized intentional defective grantor trusts

Many individuals sold assets to their intentionally defective grantor trusts in exchange for installment notes from the intentionally defective grantor trusts (IDGTs). For a host of technical reasons, the individuals 'seeded' their IDGTs with a certain amount of cash or other property to give the transaction at least the appearance of commercial viability. In some case, seeding was not possible at all or in the amount required, so the individuals' children, perhaps, guaranteed the notes.

Again, fast forward to today, some of these arrangements are not working out so well, either because the transferred asset isn't generating the cash flow to service the notes, there is a concern that the seeding was not quite enough to pass muster or the guarantors are getting nervous. Even if things are proceeding nicely, there is a concern that the tax implications of the individual's dying before the note has been repaid are still unclear and could be problematic, though not necessarily for the individual. Therefore, the individual could consider using exemption to forgive all or a portion of the balance due on the note. Even the partial forgiveness could alleviate pressure on the economics of the transaction going forward and maybe even allow for the release of the guarantors.

Many of these transactions were done with generation-skipping trusts. In those cases, the individuals allocated generation skipping tax (GST) exemption to the seed gift. With the concurrent increase in the GST exemption, the shoring-up of the IDGT should have no GST tax implications.

Doing late allocations of GST exemption

There are a host of reasons and situations where someone 'missed' a timely allocation of GST exemption. There are also situations where the allocation wasn't missed; not allocating was informed and intentional. However, maybe now the landscape had changed and an allocation is called for or is otherwise prudent.

Pro-active planning, sometimes with income tax basis in mind

Establishing spousal lifetime access trusts

It is common for parents to be interested in using their gift tax exemptions to save eventual estate tax on what they will leave to their children. However, it is also common for those same parents to be reluctant to give up control of and the income from significant holdings. These individuals may be able to achieve their estate tax objective while retaining much of the economic benefits of the assets by using a spousal lifetime access trust (SLAT).

A SLAT is an irrevocable trust set up by one spouse for the benefit of the other spouse. Let's assume that the husband creates a SLAT for his wife's benefit and funds it with part of his $11.4 million gift tax exemption. During his wife's lifetime, the trustee (which may be the wife) can distribute income and principal as needed to her for her health, education, maintenance and support. She can also have a ‘5x5’ power and a testamentary limited power of appointment. Thus, assuming the husband remains on good terms with his wife, he will have ‘indirect’ access to the trust's income and principal. When his wife passes away, the trust property will pass estate tax free to the children.

Another perspective on the use of the SLAT is that it can function as an ILIT. This use of the SLAT may appeal to individuals who find the loss of control of a (valuable) policy associated with the traditional ILIT a bridge too far. So, the SLAT would be the applicant, owner and beneficiary of a policy on the husband. The SLAT would use the funding it received from the husband to pay the premiums. Once cash value develops, the trustee can access the policy by way of withdrawals and loans. Of course, the trust should not give the husband/insured any incidents of ownership in the policy for purposes of section 2042.

The SLAT will be a grantor trust during the lifetime of the grantor spouse, here the husband. That's probably fine with him since the asset never left home anyway, as it were. However, the mood can darken quickly if the wife dies first or the couple gets divorced. The obvious concern is that the husband would lose even his indirect assess to the trust's income and principal. To make matters worse, the husband could find that the trust remains a grantor trust even after the divorce, meaning that he loses access but keeps the tax bill! There may be ways to draft around these concerns, but the more comfortable the husband is with the trust's 'contingency provisions', the more risk there will be that the IRS will consider him as the outright owner of the trust's assets for estate tax purposes.

Where the SLAT is attractive to a couple, the planner should anticipate their question about doing one for each other, kind of, reciprocally. They can indeed get there from here, but will have to do things *Grace*-fully, as the case law requires that the trusts have sufficiently different provisions to not make them the mirror image of one another. As with other areas of tax planning for spouses, planners who try to create non-reciprocal, 'dueling' SLATs for a couple need to be aware of the potential conflicts of interest inherent in consulting for both spouses and document the file accordingly.

Upstream planning

Let's assume that an individual owns a highly appreciated asset with a seriously low basis. She would like to sell the asset and diversify the holding, but is reluctant to trigger the significant capital gains tax plus the 3.8 percent tip on net investment income. Her mother does not have a taxable estate. Working with her advisors, the individual transfers the asset to a trust for the benefit of her mother. The trust provides her mother with a general power of appointment that will cause the trust's assets to be includible in the mother's estate for estate tax purposes. Assuming her mother does not exercise the power in an unanticipated fashion, the trust's assets will pass back to the individual, to her own children or to a trust for family members. Because the mother does not have a taxable estate, there will be no estate tax and no generation-skipping tax. However, because the trust's assets will be included in her estate for estate tax purposes, the assets will receive a step-up in basis at the mother's death.

Exercising 'swap' powers in an IDGT to bring low basis assets back into the estate

Particularly back in the waning days of 2012 and, no doubt, thereafter, many individuals sold highly appreciated, low basis assets to intentionally defective grantor trusts. Their objective was to convert an appreciating asset into a fixed promissory note, thereby saving estate tax on the future appreciation of the asset above the interest rate on the note. One downside of the technique if done with an asset with these characteristics is that the trust will carry over the individual's low basis, so that if the trust sells the asset, it will trigger a substantial capital gains tax. If the trust gives the individual (grantor) the right to substitute an asset of equal value in the trust, the individual can use this 'swap' power to transfer a high basis asset to the trust in exchange for the low basis asset. The low basis asset will now be included in the individual's estate, thereby giving it a step-up in basis when the individual dies.

But, wait a minute…

Before we close, however, we should point out that there will be situations where, for income tax reasons, the family is best served by the individual's retaining an asset until death rather than transferring it during lifetime. A lifetime gift of an asset will remove any post-gift appreciation in the value of the asset from the taxable estate. However, the donee of that gift will take the individual/donor's basis in the asset. If the individual holds the asset for the rest of his or her life, it will get a stepped-up basis.

The question will be whether, all income and estate tax things considered, it would make more sense not to make the gift and to hold the asset for a stepped-up basis. With a 40 percent estate tax rate and a 23.8 percent top federal capital gains rate, a transferred asset that has a carry-over basis would have to appreciate substantially for the estate tax savings on the removed appreciation to offset the loss of a basis step-up. In some cases, perhaps involving a 'legacy asset' such as a beach house that will remain in the family for generations, the estate tax side of the argument could prevail and the individual will make the gift. However, if the children will sell the asset proximately, the math could favor retaining it in the estate for the step-up.

The coast may be clear, but the decisions remain challenging

It could go without saying that determining whether and how to use the exemption is not an easy task. Each and every application that we have described calls for careful consideration of myriad personal, economic and tax factors. Individuals should ask their advisors to explain how those factors come into play and coalesce in the context of each application of the exemption. Only then will individuals be able to make informed decisions about steps that will generally be irrevocable.

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TAX SECTION OF
THE STATE BAR OF TEXAS

2018 – 2019 CALENDAR

June 2018	
Thur - Fri 06/21/18 – 06/22/18	**SBOT Annual Meeting** Marriott Marquis Hotel 1777 Walker Street Houston, Texas 77010 (713) 654-1777
Thursday 06/21/18	**Tax Section Council Planning Retreat** Marriott Marquis Houston, Texas 1:00 p.m. - 4:00 p.m.
Thursday 06/21/18	**2018 Tax Section Annual Meeting Speaker's Dinner** Grappino's 2817 W. Dallas Street Houston, Texas (713) 528-7002
Thursday 06/21/18	**Presentation of Outstanding Texas Tax Lawyer** Award Presentation at State Bar Annual Meeting, Speakers' Dinner Grappino's 2817 W. Dallas Street Houston, Texas (713) 528-7002
Friday 06/22/18	**2018 Tax Section Annual Meeting Program** Marriott Marquis Hotel 1777 Walker Street Houston, Texas 77010 (713) 654-1777
Friday 06/22/18	**Presentation of 2018 Tax Legend Award** Award Presentation During Tax Section Annual Meeting Program Marriott Marquis Hotel 1777 Walker Street Houston, Texas 77010 (713) 654-1777
July 2018	
Wednesday 07/04/18	**July 4th Holiday**
Fri - Sun 07/13/18 - 07/15/18	**Officer's Retreat** Granbury, Texas 76048

Tuesday 07/17/18	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Thur - Sat 07/19/18 – 07/21/18	**Texas Bar College** Summer School Moody Gardens Hotel, Spa & Convention Center Seven Hope Boulevard Galveston, TX 77554
?	**Tax Section Budget Deadline** (Budget must be submitted to State Bar of Texas)
Monday 07/23/18	**SBOT Chair and Treasurer Training** Texas Law Center 1414 Colorado St. Austin, TX 78701 10:30 a.m. – 2:30 p.m.
August 2018	
Thur – Tues 08/02/18 – 08/07/18	**American Bar Association Annual Meeting** Hyatt Regency Chicago, Chicago, Illinois
Tuesday 08/07/18	**Officer's Call** 4:00 p.m.
Thur – Fri 08/09/18 – 08/10/18	**Advanced Tax Law Course** Cityplace Events, Dallas, Texas
Tuesday 08/21/18	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Friday 08/24/18	**Meeting of Council, Committee Chairs, and Committee Vice Chairs** Norton Rose Fulbright US LLP 1301 McKinney, Suite 5100 Houston, Texas 77010 (48^{th} Floor) 10:30 a.m. – 12:30 p.m. w/lunch Dial In: 866-203-7023 Conference Code: 713-651-5591# Security Passcode: None – at the prompt press *
Sept 2018	
?	**Deadline for Submissions to State Bar of Texas Board of Directors Meeting Agenda**

Monday 09/03/18	**Labor Day Holiday**
Tuesday 09/04/18	**Officer's Call** 4:00 p.m.
Sun - Tues 09/09/18 – 09/11/18	**Rosh Hashanah (Religious Holiday)**
Friday 09/14/18	**Submission Deadline – Texas Tax Lawyer (Fall Edition)** Submit to TTL Editor: Michelle Spiegel michelle.spiegel@nortonrosefulbright.com
Monday 09/17/18	**Tax Court Pro Bono Calendar Call-Lubbock**
Monday 09/17/18	**Outreach to Law Schools/Texas Tech School of Law**
Tuesday 09/18/18	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Tues - Weds 09/18/18 – 09/19/18	**Yom Kippur (Religious Holiday)**
Thursday 09/20/18	**Deadline for Appointment of Tax Section Nominating Committee**
Sun - Sun 09/23/18 – 09/30/18	**Sukkot (Religious Holiday)**
Oct 2018	
Monday 10/01/18	**Tax Court Pro Bono Calendar Call - Dallas & San Antonio**
Tuesday 10/02/18	**Officer's Call** 4:00 p.m.
Thurs - Sat 10/4/18 – 10/6/18	**American Bar Association Section of Taxation Joint Fall CLE Meeting** Hyatt Regency, Atlanta, Georgia
Monday 10/08/18	**Columbus Day Holiday**
Monday 10/15/18	**Tax Court Pro Bono Calendar Call - Houston**

Tuesday 10/16/18	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Tues - Fri 10/23/18 – 10/26/18	**Council on State Taxation (COST) 49th Annual Meeting** Arizona Grand Resort & Spa, Phoenix, Arizona
Friday 10/26/18	**Council of Chairs Meeting** Texas Law Center 1414 Colorado St. Austin, TX 78701 10:30 a.m. – 2:30 p.m.
Thurs - Fri 10/25/18 – 10/26/18	**National Association of State Bar Tax Sections ("NASBTS") Annual Meeting**
Tuesday 10/30/18	**COST Regional Meeting** Austin, Texas
Wednesday 10/31/18	**Insurance Renewal is Due** **Note Premium Paid by Big Bar!**
Nov 2018	
Monday 11/05/18	**Tax Court Pro Bono Calendar Call-Dallas**
Tuesday 11/06/18	**Officer's Call** 4:00 p.m.
Thurs - Fri 11/08/18 – 11/09/18	**20th Annual International Tax Symposium** Crowne Plaza Houston River Oaks 2712 Southwest Freeway Houston, TX 77098
Thurs - Fri 11/08/18 – 11/09/18	**Austin Chapter CPA Annual Tax Conference** Norris Conference Center, Austin, Texas
Friday 11/09/18	**Meeting of Council** Norton Rose Fulbright US LLP 1301 McKinney, Suite 5100 Houston, Texas 77010 (48th Floor) 10:30 a.m. – 12:30 p.m. w/lunch Dial In: 866-203-7023 Conference Code: 713-651-5591# Security Passcode: None – at the prompt press *

Monday 11/12/18	**Veterans Day Holiday**
Monday 11/12/18	**Annual Meeting Deadline for submitting to SBOT date and time preferences for CLE programs, section meetings, council meetings, socials and special events**
Tuesday 11/13/18	**Comptroller Annual Meeting Briefing**
Wed - Thurs 11/14/18 – 11/15/18	**UT Law 66th Annual Taxation Conference** AT&T Conference Center, Austin, Texas
Tuesday 11/20/18	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Thursday 11/22/18	**Thanksgiving Day Holiday**
Dec. 2018	
Sun - Mon 12/02/18 – 12/10/18	**Hanukkah (Other Holiday)**
Tuesday 12/04/18	**Officer's Call** 4:00 p.m.
Monday 12/10/18	**Tax Court Pro Bono Calendar Call-Dallas**
Monday 12/17/18	**Tax Court Pro Bono Calendar Call-Houston**
Tuesday 12/18/18	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Tuesday 12/25/18	**Christmas (Other Holiday)**
Jan. 2019	
Tuesday 01/01/19	**New Year's Day Holiday**

?	**Nomination Period Opens for 2019 Outstanding Texas Tax Lawyer Award** • Nominations due April 1, 2019 • Nomination forms to be posted on website • Submit nomination forms to Tax Section Secretary: Christi Mondrik
Wednesday 01/02/19	**Officer's Call** 4:00 p.m.
?	**Deadline for receipt of information for SBOT Board of Director's Meeting Agenda**
Monday 01/07/19	**Annual Meeting Deadline: Submit programming for the registration brochure, CLE topics, speakers, and speaker contact information and firms**
Monday 01/7/19	**Pro Bono Tax Court Calendar Calls – San Antonio**
Friday 01/11/19	**Meeting of Council, Committee Chairs, and Committee Vice Chairs** Norton Rose Fulbright US LLP 1301 McKinney, Suite 5100 Houston, Texas 77010 (50th Floor) 10:30 a.m. – 12:30 p.m. w/lunch Dial In: 866-203-7023 Conference Code: 713-651-5591# Security Passcode: None – at the prompt press *
Friday 01/11/19	**Leadership Academy application due for the 2019-2020 class**
Tuesday 01/15/19	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Tuesday 01/15/19	**Application Period Opens for Law Student Scholarship Program**
Thur - Sat 01/17/19 – 01/19/19	**American Bar Association Section of Taxation Midyear Meeting** Hyatt New Orleans, New Orleans LA
Monday 01/21/19	**Martin Luther King Jr. Day (Holiday)**
Friday 01/25/19	**Submission Deadline – Texas Tax Lawyer (Winter Edition)** Submit to TTL Editor: Michelle Spiegel michelle.spiegel@nortonrosefulbright.com
Friday 01/25/19	**Tax Law in a Day CLE**

Monday 01/28/2018	**Pro Bono Tax Court Calendar Calls – El Paso**
Thursday 01/31/2019	**Pro Bono Tax Court Calendar Calls – Lubbock**
Feb. 2019	
Friday 02/01/19	**Register and make guest room reservations for Annual Meeting (www.texasbar.com/annualmeeting)**
?	**Leadership Academy Class of 2019-2020 Announced**
Monday 02/4/19	**Pro Bono Tax Court Calendar Call – Houston**
Tuesday 02/05/19	**Officer's Call** 4:00 p.m.
Monday 02/18/19	**George Washington's Birthday (Holiday)**
Tuesday 02/19/19	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Thur - Fri 02/21/19 – 02/22/19	**International Fiscal Association Annual Conference** The Ritz-Carlton Washington, D.C.
Friday 02/22/19	**Council of Chairs Meeting and Section Representative Election** Texas Law Center 1414 Colorado St. Austin, TX 78701 10:30 a.m. – 2:30 p.m.
Monday 02/25/2019	**Pro Bono Tax Court Calendar Calls – Dallas**
March 2019	
Friday 03/01/19	**Nomination Deadline for Chair-Elect, Secretary, Treasurer, and 3 Elected Council Members**
Monday 03/04/19	**Annual Meeting Deadline: Order special awards, council and chair plaques, food and beverage and audio visuals**
Tuesday 03/05/19	**Officer's Call** 4:00 p.m.

Monday 03/18/19	**Pro Bono Tax Court Calendar Calls – Dallas**
Tuesday 03/19/19	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera; 9:00 a.m.
Thur - Fri 03/21/19 – 03/22/19	**Leadership Academy Dallas Session**
Friday 03/22/19	**SBOT Tax Section Deep Dive Tax Workshop – Dallas** Belo Mansion 2101 Ross Ave Dallas, TX 75201
Sun - Wed 03/24/19 – 03/27/19	**Annual Meeting of Unclaimed Property Professionals Organization (UPPO)** Tampa, Florida
Monday 03/25/19	**Pro Bono Tax Court Calendar Calls – Houston**
Friday 03/29/2019	**2019 State Bar of Texas Property Tax Committee Meeting & Legal Seminar** Thompson Conference Center - UT Campus 2405 Robert Dedman Dr. Austin, Texas 78712
April 2019	
Monday 04/01/19	**Nominations for Outstanding Texas Tax Lawyer Due to Christi Mondrik** Email**:** (cmondrik@mondriklaw.com)
Monday 04/01/19	**Nominating Committee Report Due to Council**
Wednesday 04/02/19	**Officer's Call** 4:00 p.m.
Friday 04/05/19	**Meeting of Council** Norton Rose Fulbright US LLP 1301 McKinney, Suite 5100 Houston, Texas 77010 (48th Floor) 10:30 a.m. – 12:30 p.m. w/lunch Dial In: 866-203-7023 Conference code: 713-651-5591# Security passcode: None - at the prompt press * **Note: Council Vote and Selection of Recipient of 2019 Outstanding Texas Tax Lawyer Award**

Saturday 04/06/2019	**Law Student Scholarship Application Deadline**
Friday 04/12/19	**Submission Deadline – Texas Tax Lawyer (Spring Edition)** Submit to TTL Editor: Michelle Spiegel michelle.spiegel@nortonrosefulbright.com
?	**Tax Court Pro Bono Calendar Call**
Tuesday 04/16/19	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Fri – Sun 04/19/19 – 04/21/19	**Good Friday, Passover, Easter Sunday (Religious Holiday)**
Monday 04/15/19	**Annual Meeting Deadline: course materials for app; CLE articles, PowerPoints, speaker bios and photos**
Monday 04/22/19	**Annual Meeting Deadline: submit any final programming changes for onsite event guide; CLE topic titles, speakers, speaker contact information and firm**
May 2019	
Tuesday 05/07/19	**Officer's Call** 4:00 p.m.
Thur - Sat 05/09/19 – 05/11/19	**American Bar Association Section of Taxation May Meeting** Grand Hyatt, Washington, DC
Monday 05/13/19	**Last Day of Early Bird Registration for Annual Meeting**
Monday 05/20/19	**Deadline to make guest room reservations for Annual Meeting at discounted rate (www.texasbar.com/annualmeeting)**
Tuesday 05/21/19	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.
Monday 05/27/19	**Memorial Day Holiday**
June 2019	
Tuesday 06/04/19	**Officer's Call** 4:00 p.m.

Wed – Fri 06/12/19 – 06/14/19	**Annual Texas Federal Tax Institute** La Cantera Resort, San Antonio, Texas
Wed - Fri 06/12/19 – 06/14/19	**Leadership Academy Austin Session (with Annual Meeting)**
Thur – Fri 06/13/19 – 06/14/19	**SBOT Annual Meeting** JW Marriot, Austin, Texas
Thursday 06/13/19	**Tax Section Council Planning Retreat** JW Marriott Austin, Texas
Thursday 06/13/19	**2019 Tax Section Annual Meeting Speaker's Dinner**
Thursday 06/13/19	**Presentation of Outstanding Texas Tax Lawyer** Award Presentation at State Bar Annual Meeting, Speakers' Dinner
Friday 06/14/19	**2019 Tax Section Annual Meeting Program**
Friday 06/14/19	**Award Presentation to Council and Chairs During Tax Section Annual Meeting Program**
Tuesday 06/18/19	**Government Submissions (COGS) Call with Committee Chairs** Dial-in: 800-525-8970; Conference Code: 2143975538# Henry Talavera 9:00 a.m.

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2018-2019

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2018-2019

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***New Committee – Amendment to Bylaws in process to add Law School Outreach and Scholarship Committee.**