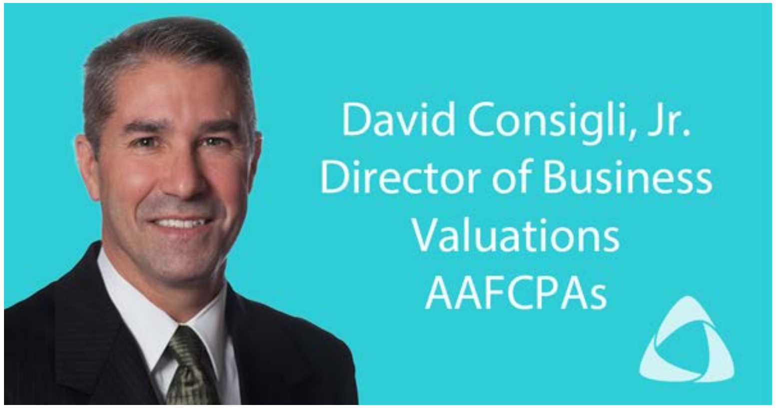
AAFCPAs

great minds | great hearts

Webinar: 2018 Year-End Tax Planning for Privately-Held Companies (Part 2)

Speakers for this session include:



1-CPE Credit Available

- AAFCPAs issues CPE in accordance with NASBA regulations
- To be eligible for CPE you must:
  - Submit answers to all polling questions when they pop up.
  - Complete and submit a written evaluation, which will launch at conclusion.
  - Remain logged in to the webinar for the entirety of the program (or at least 50 minutes).
- We will email CPE certificates within **two weeks** to the email address you provided.

AAFCPAs
great minds | great hearts

Section 199A
Qualified Business Income Deduction

IRC §199A - Overview

Qualified Business Income (QBI) Deduction

- One of the biggest changes included in the TCJA
- Has a big impact on the choice of entity analysis:
  - Allows other entity types to “compete” with the 21% flat tax rate for C corporations

QBI Deduction

What is it?

- Deduction from taxable income (TI)
  - After all other items of income and deduction
  - After computing AGI
  - After taking Standard or Itemized deduction
- The deduction is VERY mathematically intensive and has numerous limitations, phase-ins and phase-outs.

QBI Deduction

What it is not?

- It is neither an above the line deduction for AGI, nor a below the line deduction for TI. It is the last calculation in arriving at final TI.
- It cannot be used to reduce self-employment tax or net investment income tax.

QBI Deduction Line on 2018 Form 1040

Form 1040 (2018) Page **2**

Attach Form(s) W-2. Also attach Form(s) W-2G and 1099-R if tax was withheld.

1 Wages, salaries, tips, etc. Attach Form(s) W-2 . . . 1

2a Tax-exempt interest . . . 2a | b Taxable interest . . . 2b

3a Qualified dividends . . . 3a | b Ordinary dividends . . . 3b

4a IRAs, pensions, and annuities . 4a | b Taxable amount . . . 4b

5a Social security benefits . . 5a | b Taxable amount . . . 5b

6 Total income. Add lines 1 through 5. Add any amount from Schedule 1, line 22 . . . 6

7 Adjusted gross income. If you have no adjustments to income, enter the amount from line 6; otherwise, subtract Schedule 1, line 36, from line 6 . . . 7

Standard Deduction for—

- Single or married filing separately, $12,000
- Married filing jointly or Qualifying widow(er), $24,000
- Head of household, $18,000
- If you checked any box under Standard deduction, see instructions.

8 **Standard deduction or itemized deductions** (from Schedule A) . . . 8

9 Qualified business income deduction (see instructions) . . . 9

10 Taxable income. Subtract lines 8 and 9 from line 7. If zero or less, enter -0- . . . 10

11 **a** Tax (see inst) (check if any from: **1** ☐ Form(s) 8814 **2** ☐ Form 4972 **3** ☐)

b Add any amount from Schedule 2 and check here . . . ▶ ☐ 11

12 **a** Child tax credit/credit for other dependents **b Add** any amount from Schedule 3 and check here ▶ ☐ 12

13 Subtract line 12 from line 11. If zero or less, enter -0- . . . 13

14 Other taxes. Attach Schedule 4 . . . 14

15 Total tax. Add lines 13 and 14 . . . 15

16 Federal income tax withheld from Forms W-2 and 1099 . . . 16

17 Refundable credits: **a** EIC (see inst.) **b** Sch 8812 **c** Form 8863

Add any amount from Schedule 5 . . . 17

18 Add lines 16 and 17. These are your total payments . . . 18

Refund

19 If line 18 is more than line 15, subtract line 15 from line 18. This is the amount you **overpaid** . . . 19

20a Amount of line 19 you want **refunded to you.** If Form 8888 is attached, check here . . . ▶ ☐ 20a

Direct deposit? See instructions. ▶ **b** Routing number ▶ **c** Type: ☐ Checking ☐ Savings

▶ **d** Account number

21 Amount of line 19 you want **applied to your 2019 estimated tax** . . ▶ 21

Amount You Owe 22 **Amount you owe.** Subtract line 18 from line 15. For details on how to pay, see instructions . . . ▶ 22

23 Estimated tax penalty (see instructions) . . . ▶ 23

Go to *www.irs.gov/Form1040* for instructions and the latest information. Form **1040** (2018)

QBI Deduction

Here it is!

The deduction is equal to the sum of:

The lesser of:

1. **The combined qualified business income of the taxpayer, or**
2. 20% of the excess of TI over any net capital gains

Plus the lesser of:

1. 20% of qualified cooperative dividends, or
2. TI less net capital gains

Combined Qualified Business Income

It’s actually a deduction!

- THE SUM OF:
  - The LESSER OF:
    - 20% of the taxpayer's **"qualified business income"** or
    - THE GREATER OF:
      - 50% of the W-2 wages with respect to the business, or
      - 25% of the W-2 wages with respect to the business plus 2.5% of the unadjusted basis of all qualified property.
- PLUS:
  - 20% of qualified REIT dividends
  - Qualified publicly-traded partnership income

- REMEMBER – NEVER MORE THAN 20% OF THE TAXPAYER’S TAXABLE INCOME!

QBI Deduction

What qualifies?

- Active trade or business
- Available to both active and passive owners of:
  - Pass-through entities (Partnerships and S-Corps)
  - Sole Proprietors (Schedule C)
  - Disregarded entities (Single Member LLC)
- Domestic activities – must be connected to business within the United States
- Must be from a “qualified business”

QBI Deduction

What is a qualified business?

- Any active trade or business with the exception of a "specified service trade or business"
- Specified Service Trade or Business:
  - Doctors, Attorneys, Accountants, Actuaries, and Consultants
  - Performing artists
  - Paid Athletes
  - Anyone who works in the Financial Services and Brokerage Industry
  - **Any trade or business where the principal asset is the reputation or skill of one or more employees**
  - Engineers and architects are not considered SSTB!

QBI Deduction - SSTB

Can a SSTB owner claim a QBI deduction?

- IT DEPENDS!
- SSTB owners have stricter limitations and additional thresholds
- The deduction is lost if the owner makes too much money!

Combined Qualified Business Income

Phases in at certain income levels

Here it is again.

- THE SUM OF:
  - The LESSER OF:
    - 20% of the taxpayer's "qualified business income" or
    - **THE GREATER OF:**
      - **50% of the W-2 wages with respect to the business, or**
      - **25% of the W-2 wages with respect to the business plus 2.5% of the unadjusted basis of all qualified property.**
- PLUS:
  - 20% of qualified REIT dividends
  - Qualified publicly traded partnership income

- REMEMBER – NEVER MORE THAN 20% OF THE TAXPAYER’S TAXABLE INCOME!

Wage and Property Limits

W-2 Wages

- Wage expense reported on W-2s
- Excludes 1099 contractors and guaranteed payments
- 199A specifies that in order to be a W-2 wage, it must be reported on a payroll tax return.

Qualified Property

- Unadjusted Cost Basis – original purchase price
- Tangible property (no land) subject to depreciation
- Depreciable period cannot end before the close of the tax year
  - Depreciable period – LATER of regular depreciation period or 10 years

Remember…it's your allocable share

Do you qualify for the deduction?

Taxable Income	Non-Specified Service Business (All other businesses)	Specified Services Business
Less than $315,000	YES	YES
$315,000 - $415,000	Wage/Capital Limitation Phases-In	199A Deduction Phases -Out
More than $415,000	Wage/Capital Limitation	NO

Quick Example: Non-Specified Business

Facts

- John is married and runs a waste management business that generates $300,000 of QBI
- John's share of W-2 wages is $100,000 and has qualified property of $500,000
- Taxable income (before QBID) = $355,000

Quick Example: Non-Specified Business

Deduction Calculation

- 20% of QBI = $60,000 ($300,000 x 20%)
- Wage Limit = $50,000 ($100,000 x 50%)
- Capital Limit = $37,500 ($100,000 x 25%) + ($500,000 x 2.5%)
- Because John's TI exceeds the minimum threshold but doesn't exceed the maximum threshold, the wage and capital limitation is phased in:
  - $355,000 TI - $315,000 = $40,000/$100,000 = 40%
- 20% of QBI exceeds the W&C limit by $10,000
- The $60,000 is reduced by 40% of the excess
- QBI Deduction = **$56,000** [$60,000 – ($10,000 x 40%)]

Quick Example: SSTB

Facts

- John is a married self-employed lawyer with TI of $355,000
- His practice nets $300,000 and he pays a paralegal $100,000 and has $500,000 of qualifying property
- John's TI exceeds the $315,000 minimum threshold for a married TP
- Because John is a lawyer, which is a SSTB, his QBID is phased-out by a "specified services applicable percentage"

$$AP = 100\% - 100\% \times \left(\frac{\$355{,}000 - \$315{,}000}{\$100{,}000} \right) = 60\%$$

Quick Example: SSTB

Deduction Calculation

- In calculating his QBI deduction, John can use only the applicable percentage of QBI, Wages, and Capital
- 20% of QBI = $36,000 ($300,000 x 20% x 60%)
- Wage Limit = $30,000 ($100,000 x 50% x 60%)
- Capital Limit = $22,500 ($100,000 x 25% x 60%) + ($500,000 x 2.5% x 60%)
- John’s 20% of QBI exceeds the W&C limitation and his TI exceeds the minimum threshold.

Not only is his deduction phased-out, now the W&C limit gets phased-in as well!

Quick Example: SSTB

Deduction Calculation

- 20% of QBI = $36,000 ($300,000 x 20% x 60%)
- Wage Limit = $30,000 ($100,000 x 50% x 60%)
- Capital Limit = $22,500 ($100,000 x 25% x 60%) + ($500,000 x 2.5% x 60%)
- Phase-in % calculation
  - $355,000 TI - $315,000 = $40,000/$100,000 = 40%
- 20% of QBI ($36,000) exceeds the W&C limit ($30,000) by $6,000
- The $36,000 is reduced by 40% of the excess
- QBI Deduction = **$33,600** [$36,000 – ($6,000 x 40%)]

Takeaway: Non-SSTB vs. SSTB

John’s non-SSTB deduction = $56,000

John’s SSTB deduction = $33,600

That’s a $22,400 reduction in his deduction just by being a lawyer!

POLL (1 of 3)

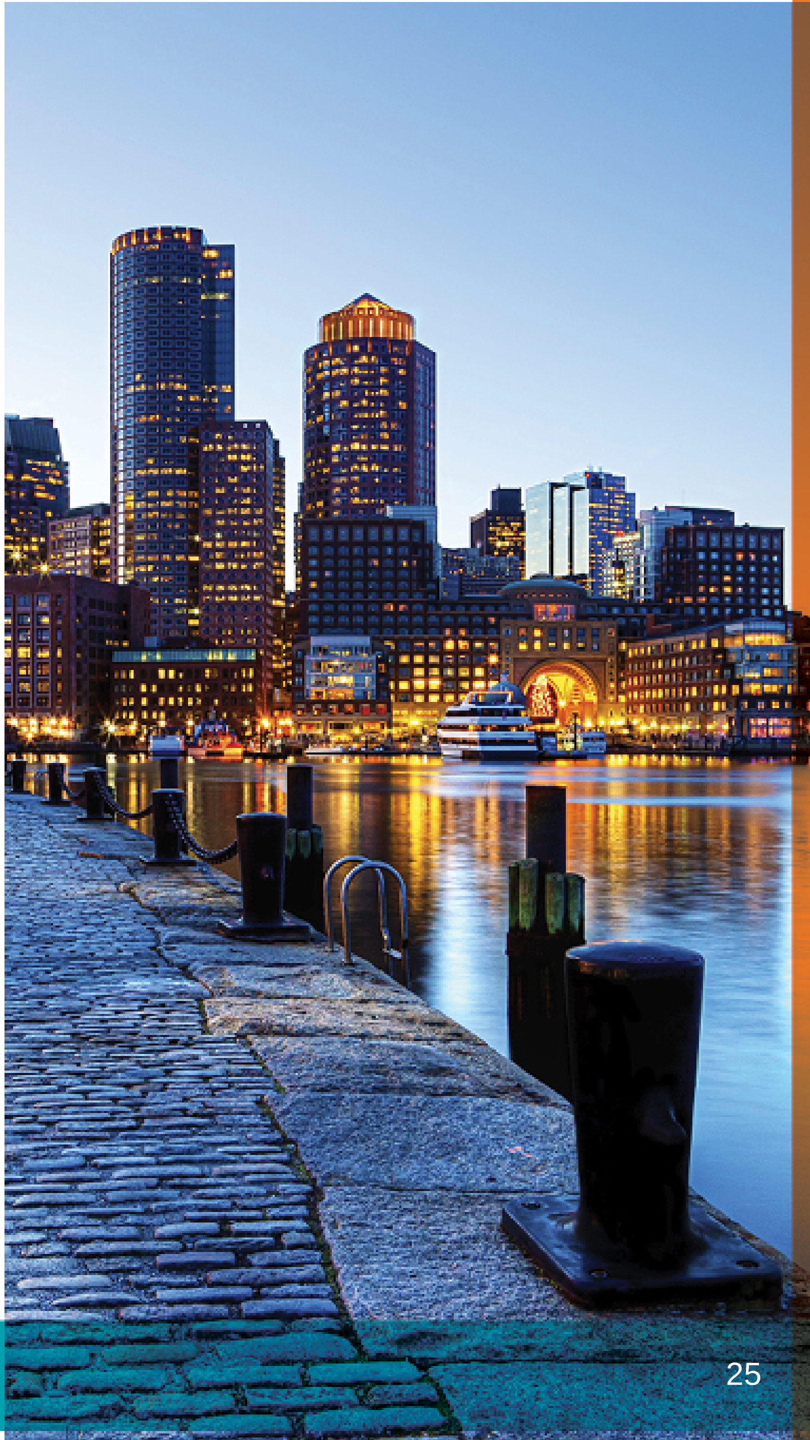
Which of the following would be considered a specified service trade or business (SSTB)?

AAFCPAs issues CPE in accordance with NASBA regulations.

U.S. Supreme Court's Wayfair Decision
State and Local Tax Strategies

What we will cover…

- Sales Tax Overview
- Prior Supreme Court Cases
- Notice and Report States
- South Dakota v. Wayfair
- Economic Nexus – Factor-Based Thresholds
- Implementation Dates and Procedures
- Sales Tax Compliance
- Streamlined Sales and Use Tax Agreement
- Strategic Resolution and Planning
- Questions

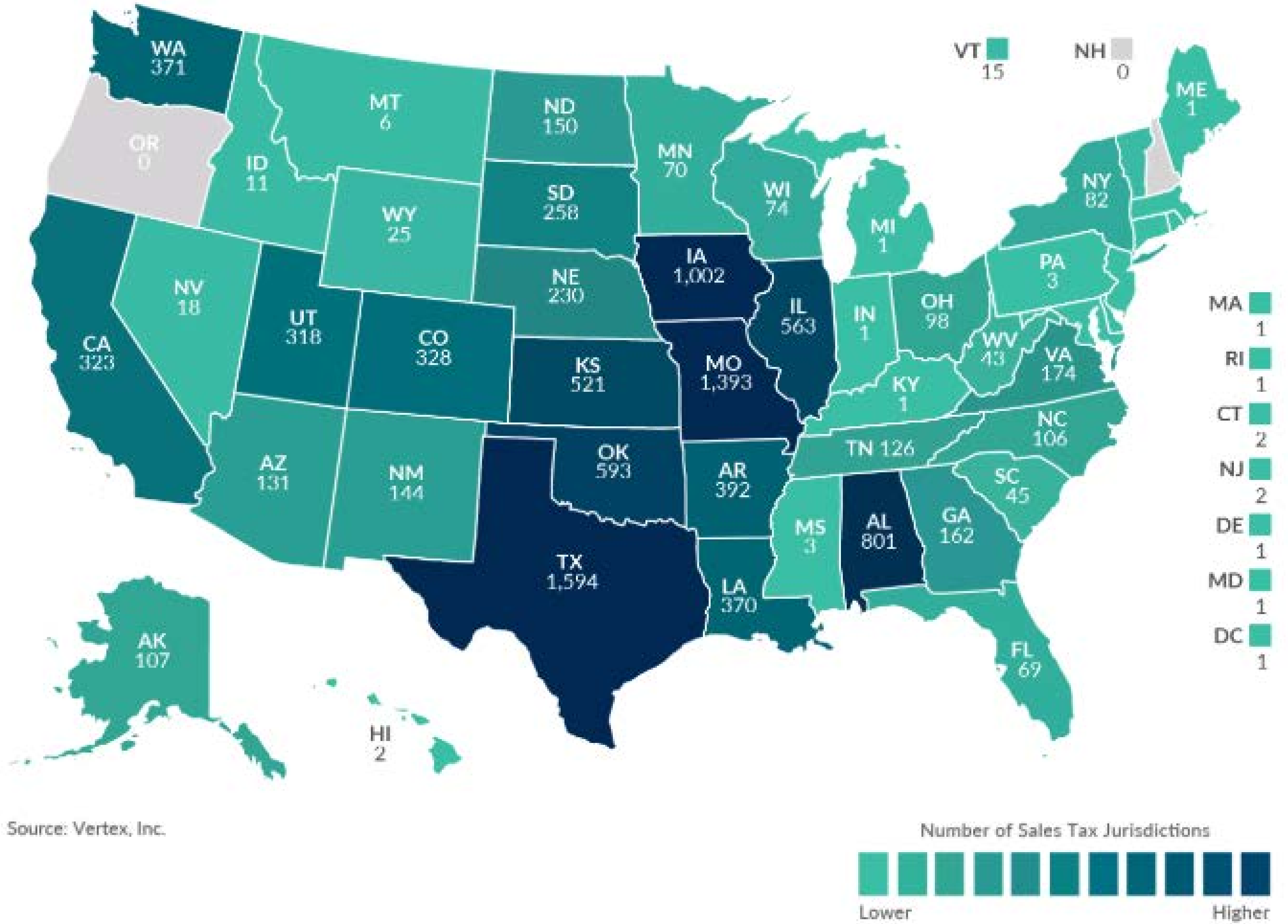


Sales Tax Overview

- Mississippi 1939
- Vermont 1969
- 5 States have no state-wide sales tax system
    - New Hampshire
    - Oregon
    - Montana*
    - Alaska*
    - Delaware
- There are approximately 11,000 state and local tax jurisdictions in the United States

How Many Sales Tax Jurisdictions Does Your State Have?

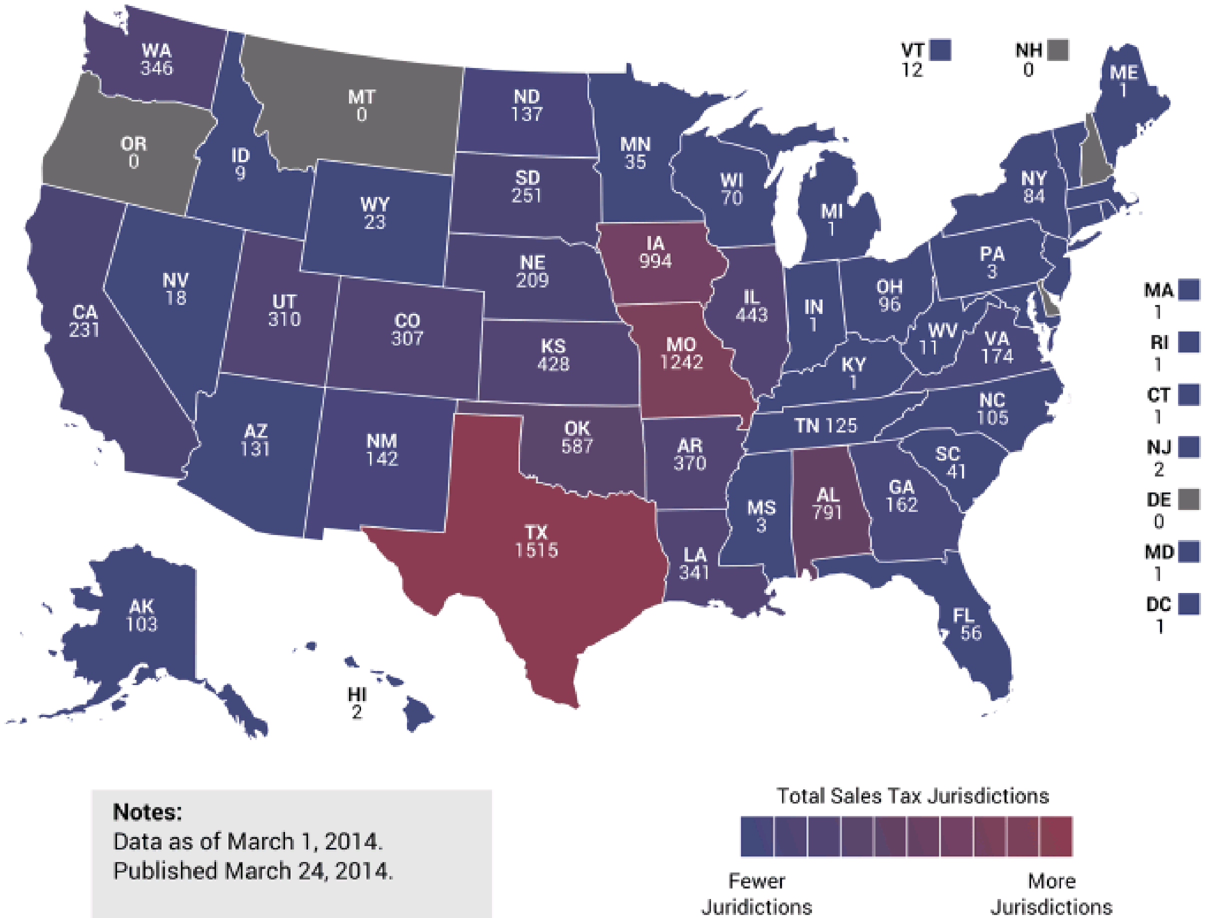
Total Sales Tax Jurisdictions by State, 2018



Source: Vertex, Inc.

TAX FOUNDATION @TaxFoundation

Total Sales Tax Jurisdictions by State in 2014



Notes:
Data as of March 1, 2014.
Published March 24, 2014.

Source:
Vertex, Inc.

taxfoundation.org/maps

Prior Supreme Court Cases

- Quill Corp v. North Dakota, 1992
  - North Dakota DOR required Quill to collect/remit sales tax
  - North Dakota Supreme Court ruled in favor of state
  - SCOTUS ruled in favor of Quill, partially overturning Bellas Hess
  - Due process clause doesn't require physical presence, but Dormant Commerce Clause always requires physical presence
  - Physical Presence Standard still there
  - Must have a building or employees or some other physical presence

Notice & Report States

- States are beginning to require that out of state sellers notify their residents that transactions in which sales tax wasn't collected may be subject to Use Tax

- States are also requiring the out of state sellers to notify the state of who their customers are

- Reporting requirements vary by state:
  - CO $100,000 or 200 transactions
  - OK, PA, WA $10,000

South Dakota v. Wayfair

- Case decided by SCOTUS on June 21, 2018, 5-4 vote
- South Dakota passed an economic nexus law that would require sellers with more than $100,000 or 200 separate transactions to collect and remit sales tax
- Wayfair sued South Dakota in state court and the South Dakota Supreme Court ruled in favor Wayfair, saying that this law violated the standard set in the Quill decision
- SCOTUS ruled 5-4 in favor of SD, although all 9 justices agreed Quill was wrong, they differed in how to address it
- Essentially abandons Physical Presence in favor of Economic Nexus

Economic Nexus by State

State	Total Sales	Transactions
AZ (Effective since 1990; no updated guidance since Wayfair)	$100,000	
CO, HI, IL, IN, IA, KY, LA, ME, MD, MI, NE, NV, NJ, NC, ND, RI, SD, UT, VT, WI, WA, WV, WY	$100,000	or 200 separate transactions
CT	$250,000	and 200 transactions during the 12 month period ending on 9/30/xx
AL, MS	$250,000	
MA	$500,000	and >100 transactions, based on PY
OK, PA	$10,000 (based on prior 12m period)	

Economic Nexus by State

State	Total Sales	Transactions
GA	$250,000	Or 200 separate transactions
MN	$100,000	Or 100 separate transactions
NY	$300,000	And 100 separate transactions
SC	$100,000	
OH, TN	$500,000	

- Most states have implementation dates between fall of 2018 and Jan 2019
- Some states base threshold on PY sales, others prior 12 months, and others CY sales

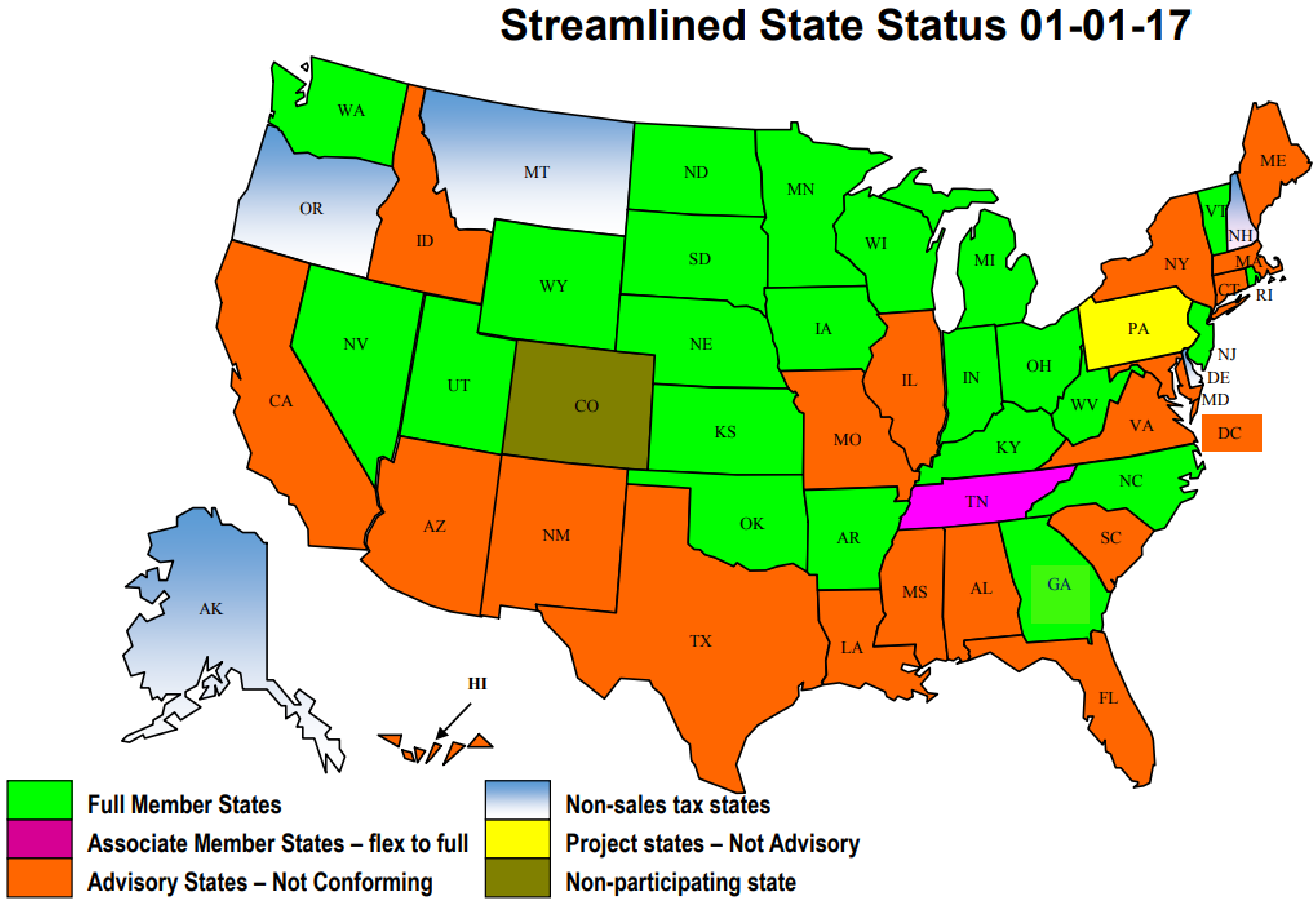
Impact of Wayfair Decision

- Increased State Tax Revenues from Out of State Sellers
- Increased Costs to Small Businesses
- Online Retailers Lose Advantage of No Tax?
  - Overstock
  - Wayfair
  - Etsy
  - Amazon 3rd Party Vendors

Streamlined Sales and Use Tax Agreement

- Streamlined Sales Tax Governing Board began in March 2000 with a goal to find solutions for the complexity in state sales tax systems.
- Part of the effort behind finding solutions was aimed at solving the issues that caused the SCOTUS to reach the decisions they did in Quill and Bellas Hess
- The Governing Board filed an amicus brief in support of South Dakota
- 24 States are Members
  - Massachusetts is not a full member
- Some Goals of the Agreement
  - Uniformity in state and local tax base
  - Uniformity on major tax base definitions
  - Simplification of rates
  - Central registry for all member states
  - Simplified administration of exemptions
  - Simplified tax returns

Streamlined States



Strategic Resolution and Planning

- Voluntary Disclosure Agreements
  - Negotiated with the state(s)
  - Back tax is collected/paid to the state(s)
  - Late penalties are reduced/eliminated
  - Win/Win for state and business

- Amnesty Periods
  - Many states will offer limited amnesty periods for businesses to clear up past due liabilities
  - States have strict rules/guidelines for eligibility

- Multistate Tax Analysis
  - AAFCPAs can perform an analysis of multistate operations to determine potential exposure in all areas of state taxation: income, sales & use, payroll, and property tax
  - Business is considering adding employees in a new state, relocating operations, etc.

POLL (2 of 3)

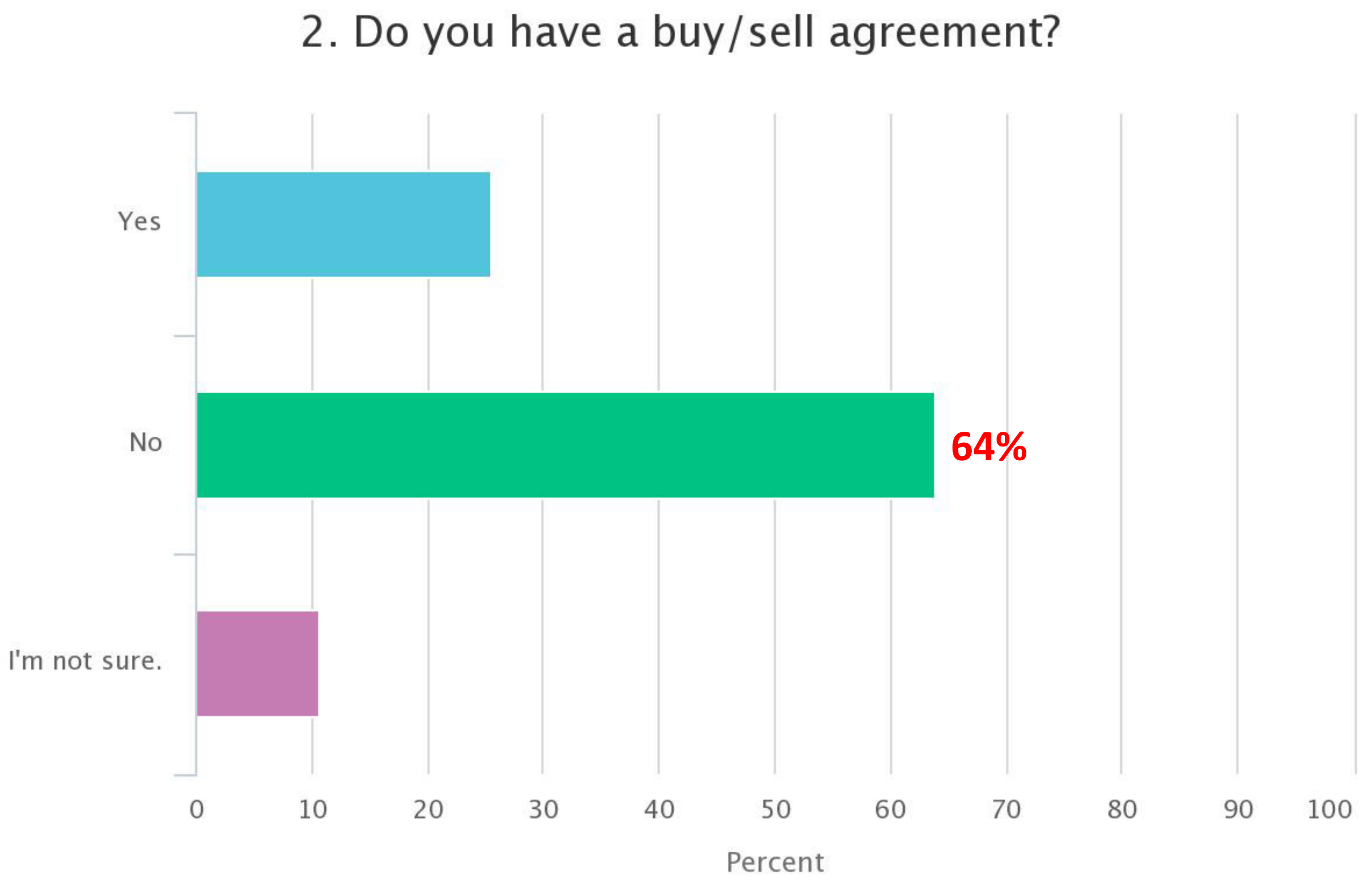
Are you confident you have addressed your state and local tax exposure risks?

AAFCPAs issues CPE in accordance with NASBA regulations.

AAFCPAs
great minds | great hearts

Buy/Sell Agreements
How the new tax law may affect your current Agreement

Poll results from Part 1 Webinar:



Overview of the Buy/Sell

- Agreement between shareholders
- Based on a future event
  - Death
  - Disability
  - Firings
  - Divorce
  - Exit
- Establishes a process for how the price will be determined

The Valuation Process Agreements

- Determine the standard of value, and purpose of valuation
  - Fair market value
    - Marketability discounts
    - Minority discounts
    - Key man discounts
  - Fair value

The Valuation Process Agreements
(Continued)

- The valuation calculation
  - The difference in value between a flow through entity, Sub Chapter S Corporations, Partnerships and Limited Liability Companies vs. C Corp gap is narrowing.
  - Corporate tax rates for a C Corp
    - Flat 21%
    - Double taxation, dividend rate at 20%

The Valuation Process Agreements
(Continued)

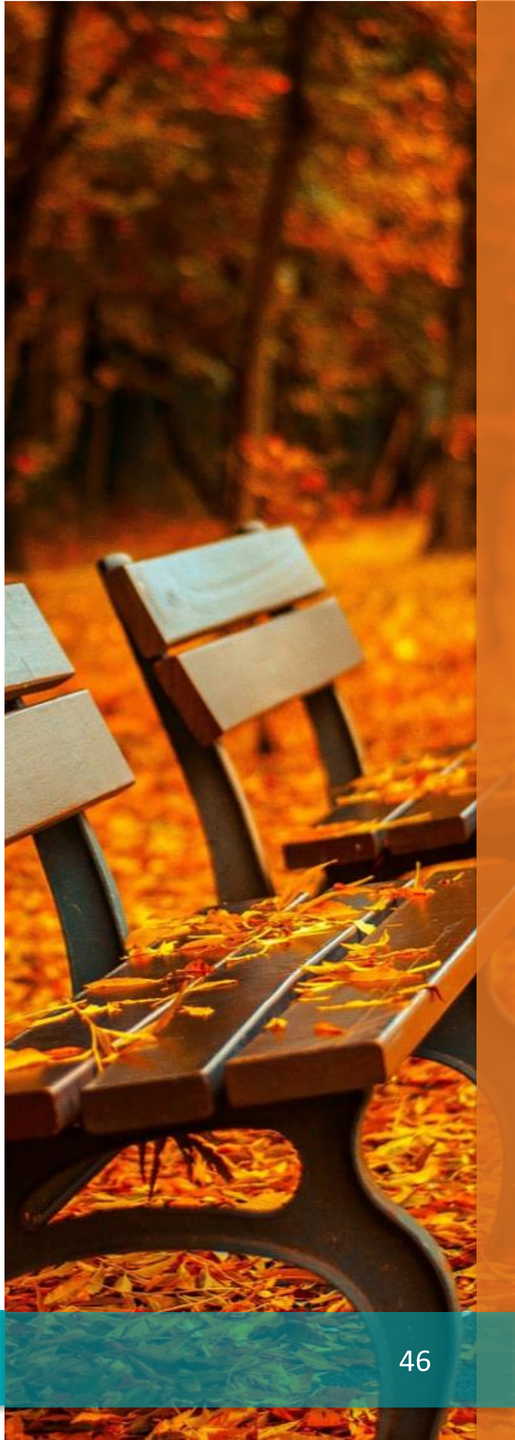
- S Corporation
  - Qualified Business Income Deduction - does the business qualify
  - Interest deduction
  - Depreciation deduction limit $1,000,000; bonus depreciation 100%
- Expiring provisions: Is it necessary to forecast out until 2025 to predict future cash flow?
- Are S Corporations and C Corporations now worth the same?

The Valuation Process Agreements
(Continued)

- Life insurance
  - Who is the beneficiary; is there a tax consequence?
  - Does the tax consequence consideration need to be re-visited due to current change in tax rates?

Moving Forward

- Every Business is unique
  - Select one appraiser now
  - Determine value
  - Update regularly



POLL (3 of 3)

- Do you have any concerns that business shares could end up in the hand of someone other than who you intend?

AAFCPAs issues CPE in accordance with NASBA regulations.

Questions?

Julie Chevalier, CPA
Tax Partner
774.512.4037
jchevalier@aafcpa.com

Richard Weiner, CPA, MST
Tax Partner
774.512.4078
rweiner@aafcpa.com

David Consigli, Jr., CPA, ABV, CPVA, CDFA
Director, Business Valuations
774.512.4005
dconsigli@aafcpa.com

David Gravel, CPA
Tax Manager
774.512.4008
dgravel@aafcpa.com

AAFCPAs' 2018 3-Part Tax Planning Webinar Series

Learn more and register: https://info.aafcpa.com/webinar-tcja

AAFCPAs' 2018 Year-End Tax Planning Webinar for **Privately-Held Companies** PART 1	AAFCPAs' 2018 Year-End Tax Planning Webinar for **Privately-Held Companies** PART 2	AAFCPAs' 2018 Year-End Tax Planning Webinar for **Individuals & Families**
October 17	October 23	October 25
Now Available OnDemand	Available Next Week OnDemand	Thursday, October 25, 2018 9-10am

Thank You