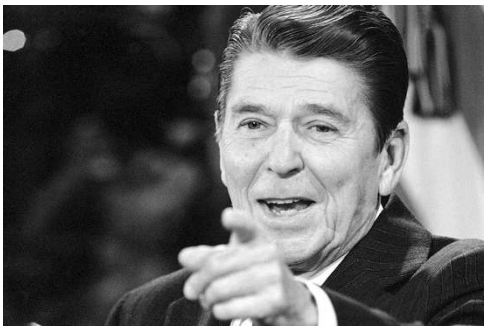
Re: Party Like It's 199A – Regulations Are Coming!

In This Issue:

Quote of the week



To sit back hoping that someday, someway, someone will make things right is to go on feeding the crocodile, hoping he will eat you last – but eat you he will.

.

-Ronald Reagan

On July 23, 2018, the Section 199A Proposed Regulations were submitted to the Office of Management and Budget by the Treasury Department. This provides some guidance on a new area of the tax law which contains numerous questions and open items. It remains to be seen if the Regulations will be finalized, but the proposed Regulations can provide some assistance for clients and their advisors in navigating the new frontier of Section 199A.

We think that we shall never see,

Final Regulations under Section 199A that will make perfect sense to me.

While big companies get a lower tax rate that is automatic,

The Section 199A deduction for small businesses and proprietors will be much more bureaucratic.

Clients with S corporations, partnerships and personally owned businesses and rentals,

Should be aware of the rules that apply, which could drive us all to be mentals.

Many taxpayers, without structuring, will go without the deduction,

Although this could change somewhat after the next “eluction.”

Stay tuned as we analyze this interesting quagmire,

But do pay enough attention so that your taxes may go lower, or at least not higher!

Our article from this morning on the LISI system,

Is set forth below, with considerations where we did list ´em.

New Section 199A Proposed Regulations in Progress

by Alan Gassman, Brandon Ketron & Scott Schenck

Scott Schenck has a Bachelor's Degree from Northeastern University and will attend Duke Law School in August. He has spent his summer at the Gassman, Crotty & Denicolo, P.A. firm studying and writing about Section 199A.

EXECUTIVE SUMMARY

The Tax Cuts and Jobs Act of 2017enacted new Internal Revenue Code Section 199A, which gives a great many taxpayers a 20% deduction on Qualified Business Income, which is categorized and measured pursuant to complicated rules.

While hundreds of thousands of taxpayers and thousands of advisors wish to be sure to qualify for the maximum tax benefits available under these new rules, we are already through almost seven (7) months of 2018, and a great many questions need to be answered in order to facilitate appropriate structuring for individuals, S-corporations, partnerships, and other entities.

On July 23, the Service submitted proposed regulations to the Office of Information and Regulatory Affairs of the Office of Management and Budget ("OMB"), which has no more than ten (10) business days to review these proposed regulations, unless otherwise mutually agreed. The latest day for an expected public release should therefore be Friday, August 3, giving a great many advisors the weekend of August 4 and 5 and the days thereafter to enjoy what is sure to be interesting, complicated and at least somewhat controversial.

FACTS

Internal Revenue Code Section 199A is a complicated and often ambiguous Internal Revenue Code Section that will impact the structuring of thousands of jobs, companies, rental activities, and planning structures.

The basic premise of the statute is that income derived from trades and businesses, which are operated under entities taxed as partnerships, S-corporations, and by Schedule C and E taxpayers can qualify for a 20% deduction if certain requirements are met, and a number of exceptions can be avoided.

Notably, for high-income taxpayers (meaning married joint filers who have more than $415,000 a year of taxable income and single or separate filing individuals who have over $207,500 of income) certain requirements must be met with reference to the income not coming from what is known as a Specified Service Trade or Business, and also a wage and/or qualified property threshold must be met in order to be deductible.

The statute was hastily assembled in only a few weeks' time and changed at the last minute to accommodate legislative deal-making, and therefore has many loose ends, undefined terms, and associated uncertainties.

Prominent examples of this include whether separate operations that may currently be integrated with a Specified Service Trade or Business may be segregated out by having either (1) separate accountings, (2) separate subsidiary entities within the same taxable entity, or (3) separate related entities that would charge for services rendered in order to qualify management, advertising, intellectual property, royalty and other non-Specified Service Trade or Business income for the Section 199A deduction.

In addition, taxpayers in the leasing business need to know what degree of activity will be needed for their activities to be considered a "trade or business," and married couples who are high earners (joint filers who have more than $415,000 a year of taxable income) and operate businesses under disregarded LLCs or individually need to know whether one spouse can own the business, while counting wages paid to the other spouse in order to satisfy the wage and/or qualified property test to qualify for the deduction.

In its submission to the Office of Information and Regulatory Affairs, the IRS has cited to only subsections 199A(f)(4) and Section 199A(h) which is almost assuredly an oversight in the submission process.

Additionally, this filing was described as "Guidance under Section 199A (Computational)," which may limit the scope of guidance even further. For example, advisors may not be receiving their much-desired definition of Specified Service Trade or Business.

Currently, a host of questions remains unanswered, some of which will be listed in the chart below:

General Topic:	Questions:
Aggregation of Qualified Business Income from multiple trades or businesses	• How will aggregation of Qualified Business Income be calculated when a taxpayer has an ownership interest in multiple trades of businesses, and what will happen if some of them are Specified Services?
Employee Leasing/Common Paymaster Scenarios	• Will wages paid to an employee leasing company be counted as wages for the company receiving the services of the leased employees?

	• What about wages paid in common paymaster scenarios?
Loss Carryforwards	• How are loss carryforwards calculated for multiple businesses when some profitable and some are not? • How are losses accounted for with multiple businesses in a single taxable year?
Rental Activities	• What level of activity in leasing is necessary to claim the Section 199A deduction?
Segregating Lines of Business	• Whether income from a management company can be established to provide management services to a Specified Service Trade or Business would be considered as part of, or engaged in, the Specified Service? • What level of separation is necessary to segregate different lines from a Specified Service (e.g. arm's length transactions, different Taxpayer Identification Numbers)?
Tiered Entity Organizations	• Will trades or businesses be able to aggregate wages and Qualified Property of the businesses it owns for the purposes of limitations in Section 199A based on wages and Qualified Property? • Will trades or businesses that own Specified Services and flow-through entities that are not Specified Services be able to separately claim the income derived from each, so that some of the income will not be subject to Specified Service limitations?
Short Taxable Years	• How will wages be allocated when there are varying percentages of ownership during the years for new partners/shareholders during short taxable years?
Application of Section 199A to Charitable Remainder Trusts (CRTs)	• Is the deduction taken at the Charitable Remainder Trust level, or when distributed in a later year? • Does Qualified Business Income create a separate class within the class/category

	system of distributions under Section 664?[1]
ESBT Qualifications	• Will ESBTs be able to qualify for Section 199A? (the Secretary may not have the power to correct this obvious drafting error in the legislation.
Definition of Specified Service Trade or Business	• What is meant by a "business where the principal asset … is the reputation or skill of one or more of its employees?" • Whether the current rulings under Section 448 or Section 1202 will be used when determining if certain services that are incidental to Specified Services are themselves Specified Services (e.g. a janitor for an accounting firm)? • Does licensing, certifications, formal/informal training, or state-imposed professional requirements that are essential for the performance of services affect the determination of whether a trade or business is a Specified Service?

At the ABA Section of Taxation's May meeting in Washington D.C., attorney-advisor at the Treasury's Office of Tax Policy Audrey Ellis pointed to old Section 199's regulations when discussing paymaster scenarios under Section 199A, saying that they would be helpful.[2] Earlier in February, at the ABA's San Diego Meeting, Ellis had given indications that the scope of the term "reasonable compensation" would not be expanded.[3] A great many advisors wondered if, and feared that, the term would be applied to all entities beyond its traditional application to S corporations.

It is important to note that Proposed regulations are generally not binding, and the courts have been inconsistent in determining the weight of their authority.[4] However, the Internal Revenue Manual states the following:

[1] The authors would like to thank the AICPA for asking such an insightful question on behalf of Charitable Remainder Trust beneficiaries.

[2] Eric Yauch, *ABA Section of Taxation Meeting: Existing Tax Code Helpful for Addressing Section 199A Issues*, Tax Notes Today (May 28, 2018).

[3] Eric Yauch, *Reasonable Compensation Principles Not Spreading to Partnerships*, Tax Notes Today (May 14, 2018).

[4] In *Natomas N. Am. Inc.*, the Tax Court held that proposed treasury regulations carried no more weight than a legal argument submitted by a taxpayer in a brief. 90 T.C. 710 (1988). In *Garvery, Inc.*, the Court held that reliance on proposed regulations, even if the proposed regulations have been outstanding for a long period of time, was not reasonable and that the IRS does not have an obligation to adopt the proposed regulations. 1 Cl. Ct. 108 (1983). However, in *Rountree Cotton Co.*, the Tax Court held that proposed regulations provided taxpayers and the

> Proposed regulations provide guidance concerning Treasury's interpretation of a Code section. * * * Taxpayers may rely on a proposed regulation, although they are not required to do so. Examiners, however, should follow proposed regulations, unless the proposed regulation is in conflict with an existing final or temporary regulation.[5]

In addition, if Proposed Regulations are followed, the taxpayer's position will not be subject to the negligence penalty under Section 6662(c), as Proposed Regulations provide taxpayers with a reasonable basis and/or substantial authority to take a tax position.[6]

It is also noteworthy that if Temporary regulations are issued under Section 199A that these regulations will be binding on the taxpayer, as Temporary regulations carry the same weight and authority as final regulations until they expire or are withdrawn.[7]

The regulations will be interpretive, meaning that they must be reasonable and cannot be "legislative" or law-changing in nature, except with respect to the following items, which the statute specifically employers the Treasury Department to "legislate":

1. **Short Taxable Years**: Subsection 199A(b)(5) gives the Treasury the ability to create regulations regarding how Qualified Business Income works for short taxable years, where a taxpayer acquires or disposes of a major portion of a trade or business, or where a taxpayer acquires or disposes of a major portion of a separate unit of a trade or business.
2. **Allocation of Items/Wages**: Subsection 199A(f)(4)(A) gives the Treasury the ability to create regulations that require or restrict the allocation of certain items and wages. Additionally, it gives the Secretary the authority to issue regulations determining reporting requirements, and these may resemble the now repealed Section 199 regulations, which stated that a Form W-2 and Form W-3 taken together constituted a proper report filed with the Social Security Administration for the purpose of declaring wages paid.[8]
3. **Tiered Entity Situations**: Tiered entities are arrangements where one entity owns another entity, which may own another entity, in some combination. Subsection 199A(f)(4) gives the Treasury the ability to create regulations to restrict allocations of items under tiered entities. Section 199A(f)(4)(B) by providing that "The [Treasury] Secretary shall prescribe such regulations as are necessary to carry out the purposes of this section, including regulations – … (B) for the application of this section in the case of tiered entities."
4. **Depreciable Periods and 1031 Exchanges**: Subsection 199A(h) gives the Treasury the ability to create anti-abuse rules. Subsection (1) this section requires the Secretary to use rules similar to Section 179(d)(2) to prevent manipulation of depreciable periods, and Subsection (2) empowers the Secretary to create regulations for determining the unadjusted

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Court with guidance regarding the issue in questions and were an effective tool in analyzing the issues of the case. 113 T.C. 422 (1999).

[5] IRM 4.10.7.2.3.3

[6] *See* Reg. §1.6662-3, Reg. §1.6662-4(d)(3).

[7] *See Cinema '84 v. Commissioner*, 294 F.3d 432, 438 (2d Cir. 2002).

[8] Treas. Reg. § 1.199-2(a)(3)(i)

basis of Qualified Property acquired in like-kind exchanges (Section 1031 exchanges) or involuntary conversions.

5. **Agricultural and Horticultural Cooperatives**. In March, Section 199A was updated as part of an omnibus spending bill that provided for technical corrections and fixed what was referred to as the "grain glitch," which would have allowed farmers selling to cooperatives to have unintended benefits.[9] The updated statute gives the Treasury the authority implement the equivalent of a new subsection (g) for agricultural and horticultural cooperatives.

The Code sections that the IRS has authority to produce legislative on can be found in the following chart:

Topic:	Code Section:	Specific Language:
Short Taxable Years	§ 199A(b)(5)	"The Secretary shall provide for the application of this subsection in cases of a short taxable year or where the taxpayer acquires, or disposes of, the major portion of a trade or business or the major portion of a separate unit of a trade or business during the taxable year."
Allocation of Items/Wages	§ 199A(f)(4)(A)	"The Secretary shall prescribe such regulations … for requiring or restricting the allocation of items and wages under this section and such reporting requirements as the Secretary determines appropriate"
Tiered Entity Situations	§ 199A(f)(4)(B)	"The Secretary shall prescribe such regulations … for the application of this section in the case of tiered entities."
Depreciable Periods / 1031 Exchanges	§ 199A(h)	"The Secretary shall— (1) apply rules similar to the rules under section 179(d)(2) in order to prevent the manipulation of the depreciable period of qualified property using transactions between related parties, and (2) prescribe rules for determining the unadjusted basis immediately after acquisition of

[9] See Christine Haughney, *A Tax Law Boon to Farm Co-ops*, Politico (January 10, 2018), https://www.politico.com/newsletters/morning-agriculture/2018/01/10/a-tax-law-boon-to-farm-co-ops-069726. This article does a good job of explaining how the grain glitch might have allowed co-op selling farmers to wipe out their tax burden completely.

		qualified property acquired in like-kind exchanges or involuntary conversions.
Agricultural and Horticultural Cooperatives	§ 199A(g)(3)(C) & § 199A(g)(6)	"Secretary shall prescribe rules for the proper allocation of items described in subparagraph (A) for purposes of determining qualified production activities income. Such rules shall provide for the proper allocation of items whether or not such items are directly allocable to domestic production gross receipts" & "The Secretary shall prescribe such regulations as are necessary to carry out the purposes of this subsection, including regulations which prevent more than 1 taxpayer from being allowed a deduction under this subsection with respect to any activity described in paragraph (3)(D)(i). Such regulations shall be based on the regulations applicable to cooperatives and their patrons under section 199 (as in effect before its repeal)"

COMMENT

Hold onto your hat! The Service's stance on a great many questions under Section 199A will have a tremendous impact on tax returns, entity structuring, whether individuals should be characterized as independent contractors or employees, whether large bonuses should be paid by year end, what taxpayers or new trusts or other entities formed by them should own interests in business and investment entities, whether aggressive pension (including cross tested defined benefit and cash balance plans, and other income tax planning, including interfamily sales of businesses, and ESOP's (Employee Stock Ownership Plans) should be implemented in order to save tax liability, and what tax liability will be expected to be owed for 2018.

The IRS is not always reasonable with respect to regulations, and may attempt to discourage the use of common and defensible arm's length arrangements between related taxpayers that can significantly reduce tax liability. Sometimes Proposed Regulations are the Service's first offer to taxpayers and advisors, and become more taxpayer friendly after months of

commentary, testimony and lobbying by many special interest groups, and sometimes simply withdrawn, as with the Proposed Regulations that were released under Section 2704(b) in 2016.

The Service misses the boat, resulting in thousands of advisors spending tens of thousands of hours studying and restructuring, only to find that what was allegedly intended by the proposed rules and interpretations were misunderstood or changed midstream. The section 2704(b) regulation experience is a prime example of how the tax profession will impact the regulatory process to protect taxpayers while sacrificing professional and personal time to do so.

CONCLUSION:

The new proposed regulations will answer many questions, while causing at least some degree of controversy, thousands of hours of advisor study, and a good many changes in business and investment structures for thousands of Americans who have to jump through multiple hoops to get the same degree of tax relief that was given to almost all major corporations on a silver platter without requirements or issues. Why we have to go through this for small businesses to qualify for the same relief is a painful policy question. Our duty as advisors to help our clients pay the least possible taxes while complying with the tax system continues to be a difficult challenge, which makes our profession both rewarding and sorely needed

Stay tuned as LISI and its commentators review, summarize, and discuss practical steps that taxpayers will want to take and issues to be considered when these proposed regulations have been released, and keep in mind what the IRS may often forget:

"Anyone may arrange his affairs so that his taxes shall be as low as possible; he is not bound to choose that pattern which best pays the treasury. There is not even a patriotic duty to increase one's taxes. Over and over again the Courts have said that there is nothing sinister in so arranging affairs as to keep taxes as low as possible. Everyone does it, rich and poor alike and all do right, for nobody owes any public duty to pay more than the law demands."

--Judge Learned Hand, *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. 1934), aff'd, 293 U.S. 465 (1935).[10]

Back to top

[10] The court, however, found that (1) where a transaction's only substantial business purpose is avoidance or reduction of Federal tax, the tax law will not regard the transaction, and (2) for Federal tax purposes, where the economic substance of a transaction is different from its legal form, the taxpayer will be bound to its substance.

Trust Administration 101

by Ken Crotty

The administration of a Trust Estate is an involved process that requires determining and collecting the assets, determining and paying any debts, filing appropriate tax returns, and distributing the remaining assets to the named beneficiaries. Trustees are designated to complete this process.

Under Florida law, Trustees are fiduciaries because they are responsible for holding and managing the property of the Trust for the benefit of the Trust's beneficiaries and creditors. As fiduciaries, Trustees are held to a high standard of care. To meet this standard a Trustee must use all available authority to act in the best interest of the Trust Estate's beneficiaries and creditors, and must take all necessary steps to correctly administer and distribute the Trust Estate as quickly and efficiently as possible.

To administer a Trust, Trustees must comply with notice and accounting requirements, and are responsible for identifying creditors, managing the Trust property, filing necessary taxes, and paying expenses incurred during administration.

There are several notices a Trustee is required to give to satisfy the notice requirements. The Trustee must file a Notice of Trust with the Court. The Notice of Trust tells the Court the Trustee's name and that they are responsible for the estate proceedings. The Trustee should also give notice to the Internal Revenue Service that they are acting as a fiduciary by filling out and submitting a Form 56. If the Trustee is hiring a law firm to help with aspects of the Trust Administration, then the Trustee should also submit a Form 2848 to the IRS. This form provides the law firm with a Power of Attorney to discuss the Trust with the IRS.

The Trustee must also give notice to the qualified beneficiaries of the Trust. A qualified beneficiary is a beneficiary who is: (1) receives or may receive distributions of income or principal from the Trust; (2) would receive distributions of income or principal if a beneficiary's (who is described in (1)) interest in the Trust ended without causing the Trust to terminate; or (3) would receive distributions of income or principal if the Trust terminated. Sufficient notice to the beneficiaries requires: (1) disclosure of the Trust's existence, the beneficiaries' right to a copy of the Trust instrument, the beneficiaries' right to accountings, and identity of the grantor; (2) notice of accepting the position of Trustee; the Trustee's full name and mailing address; and (3) notice that a fiduciary lawyer-client privilege applies to any attorney employed by the Trustee.

The Trustee must be able to provide the beneficiaries with accountings of the Trust. It is best if the Trustee maintains proper accountings from the beginning of the administration process. Maintaining proper accountings also helps coordinate and track the inventory, receipts, and disbursements that a Trustee is required to make. While a Trustee can handle this process individually, they can also hire a professional to assist with this. Hiring a professional to handle all accounting measures often is expensive. To avoid this expense, beneficiaries can waive their right to accountings, but a Trustee should still prepare a schedule that shows how the assets that are available for distribution were calculated and how they will be distributed. Any such waiver is valid for future periods until it is rescinded by the beneficiary.

In order to give notice to creditors, the Trustee is required to identify all potential creditors of the Estate. Common creditors include: credit card companies, doctors and hospital charges, and funeral expenses. There is no formal process during Trust administration to identify creditors. Creditors have generally 2 years from the date of death to file claims against the Trust. To limit this period, Trustees may want to consider initiating a probate proceeding and filing a Notice to Creditors. By doing this, the 2 year deadline for claims is reduced to 3 months, and creditors only have 30 days from when they receive the notice to file their claims. If a creditor does not file a claim within this period then they are barred from filing a claim or demanding payment from the Trust indefinitely.

The Trustee is responsible for managing the Trust property. This entails identifying, collecting, doing inventory on, and determining value of the Trust Estate's assets. To access account records, a Trustee must present certified copies of the death certificate to the banks and entities holding the assets to prove they are a Trustee and authorized to administer the Trust assets. If the banks and entities do not have a copy of the Trust, then the Trustee may need to provide one. Formal appraisal is used to determine the value of the assets as of the date of death. After taking possession of all of the property and determining its value, the Trustee is responsible for arranging for the assets' preservation and safekeeping.

As part of preservation and safekeeping, it is important to ensure that there is adequate insurance coverage for any tangible personal property or improved real estate. This requires confirming existing coverage is still valid, as many policies become invalid upon death, and obtaining new coverage if necessary. Confirmation of existing policies should be done with both the agent and the applicable carrier. To prepare the inventory, the Trustee will have to determine the title and location of all assets held in the Grantor's name alone, held jointly by the Grantor and someone else, and any assets the Grantor may have been entitled to, such as life insurance policy proceeds.

The Trustee is also responsible for Taxes regarding the Trust. Florida law does not have an estate tax, but does require filing Form DR-312 of DR-313. Income taxes are due on any income that the Trust Estate generates during administration exceeding $600. This income is reported by filing on behalf of the Trust a Form 1041, which is a fiduciary income tax return. The Trustee may also be required to ensure prior taxes were timely filed and paid, so a Trustee should generally review the tax returns for the previous three years. Reviewing the taxes can also reveal assets or sources of income that were previously unknown. Trustees should work with a CPA to ensure income tax requirements are satisfied and to minimize taxes associated with the Trust Estate assets.

The Trustee is required to pay for any expenses incurred during administration of the Trust Estate. Expenses include paying creditors, paying taxes, and general administration costs. These expenses are paid out of the Trust's assets. To make payments, the Trustee can choose to either use the existing Trust account or to open a new Trust checking account. If the Trustee chooses to open a new checking account, they should deposit all funds into it and make all payments from that account. If the Trust account has available cash, the Trustee is required to determine if the cash is sufficient to meet the Trust Expenses. If more cash is available than needed, the Trustee should determine if some form of prudent investment is required. If there is not enough cash available to cover expenses then the Trustee may have to sell assets or borrow money on behalf of the Trust Estate.

Each Trust is different, and the obligations and powers given to the Trustee can vary. The above items are basic duties and responsibilities that generally apply to Trustees.

Back to top

Florida Doctor's Guide to Section 199A: Tax and Business Planning Consideration *Part 3 of 3.*

By Alan Gassman and Brandon Ketron

SECTION 4. Other Rules/Traps for the Unwary.

There are also some additional rules that can significantly impact tax planning:

1. Under the "Guaranteed Payment" rules, partnerships cannot pay W-2 wages to a partner. If an individual or married couple is a direct partner in a medical practice or other entity taxed as a partnership, they may want to transfer their ownership interest so that they are not personally partners, and then receive wages as appropriate to meet the wage test if it applies.

2. It does not appear to be possible for a Schedule C or Schedule E individually-owned business to pay a wage to the owner/taxpayer, although it appears possible that one spouse can own a proprietorship or disregarded LLC reported on a joint tax return, while paying the other spouse W-2 wages. As a result, a high-income taxpayer owning a Schedule C business that does not pay sufficient wages to those other than the owner/taxpayer may consider transferring the business to an S corporation so the owner can receive wages.

3. "Trade or business" means a United States trade or business. Any part of a trade or business that occurs or is located outside of the United States, including territories with the exception of Puerto Rico, cannot be counted as trade or business income for 199A. Businesses that outsource billing, IT, customer service, and other items may want to separate these to avoid confusion.

4. To assure that real estate rental activities can be considered a "trade or business," it may be necessary for the landlord to provide significant services for the tenant, such as maintenance, management of landscaping, and other functions. The statute does not define "trade or business," but the definition of "trade or business" generally has been interpreted to mean an activity engaged in with continuity and regularity and the primary purpose of which must be for income or profit.[11] The AICPA submission to the IRS requests that all rental activities should qualify, but it is unknown whether the IRS will agree.

5. Many professionals will increase the rent paid in order to reduce the income of the practice and increase the income of the rental entity, which may qualify for the 199A deduction, but this may

[11] *Commissioner v. Groetzinger*, 480 U.S. 23 (1987). Justice Blackmun noted the term trade or business is not defined in the Internal Revenue Code. "We accept the fact that to be engaged in a trade or business, the taxpayer must be involved in the activity with continuity and regularity and that the taxpayer's primary purpose for engaging in the activity must be for income or profit."

cause imposition of higher sales tax if rent is actually paid to the rental entity.[12]

6. Rental payments, management fees, or other income paid to related entities must be considered reasonable and commensurate with other arm's-length arrangements, or income may be reallocated to the business under Internal Revenue Code Section 482.

7. All legal practice entities must be owned by lawyers, or professional entities that are owned by lawyers. In Florida these entities must be the individual lawyer, a general partnership of lawyers (which is never recommended), and professional corporations. Almost all other professions (other than optometrists and dentists) can operate under entities that can be owned by spouses, children, and trusts for spouses and children that would be able to receive up to $157,500 each of income that could qualify for the section 199A deduction. This eliminates an important planning opportunity for lawyers, but maybe not for medical practices.

The Florida Board of Dentistry, the Florida Board of Medicine, and other boards throughout the country have approved having the "goodwill" of a dental or medical practice owned by a non-physician or dentist under a "management company," which may receive a significant portion of the revenues or otherwise applicable net income as management fees to reflect the value for the use of intellectual property, practice assets, and management and oversight services.

One author was involved in a Florida Board of Dentistry petition where the Board informally determined that paying 54% of revenues to a dental practice management company, that had paid hundreds of thousands of dollars to an orthodontist in exchange for the goodwill of his practice, did not violate the Dental Practice of Medicine prohibition. The management company could not control the actual judgment of the dentist or the supervision of dental employees, and was not directly paid to provide patients or referrals to the practice. The arm's-length nature of the arrangement included a 5-year employment agreement at a fair market value salary and a non-competition agreement. The Board of Medicine in the state of Florida has made similar determinations.[13]

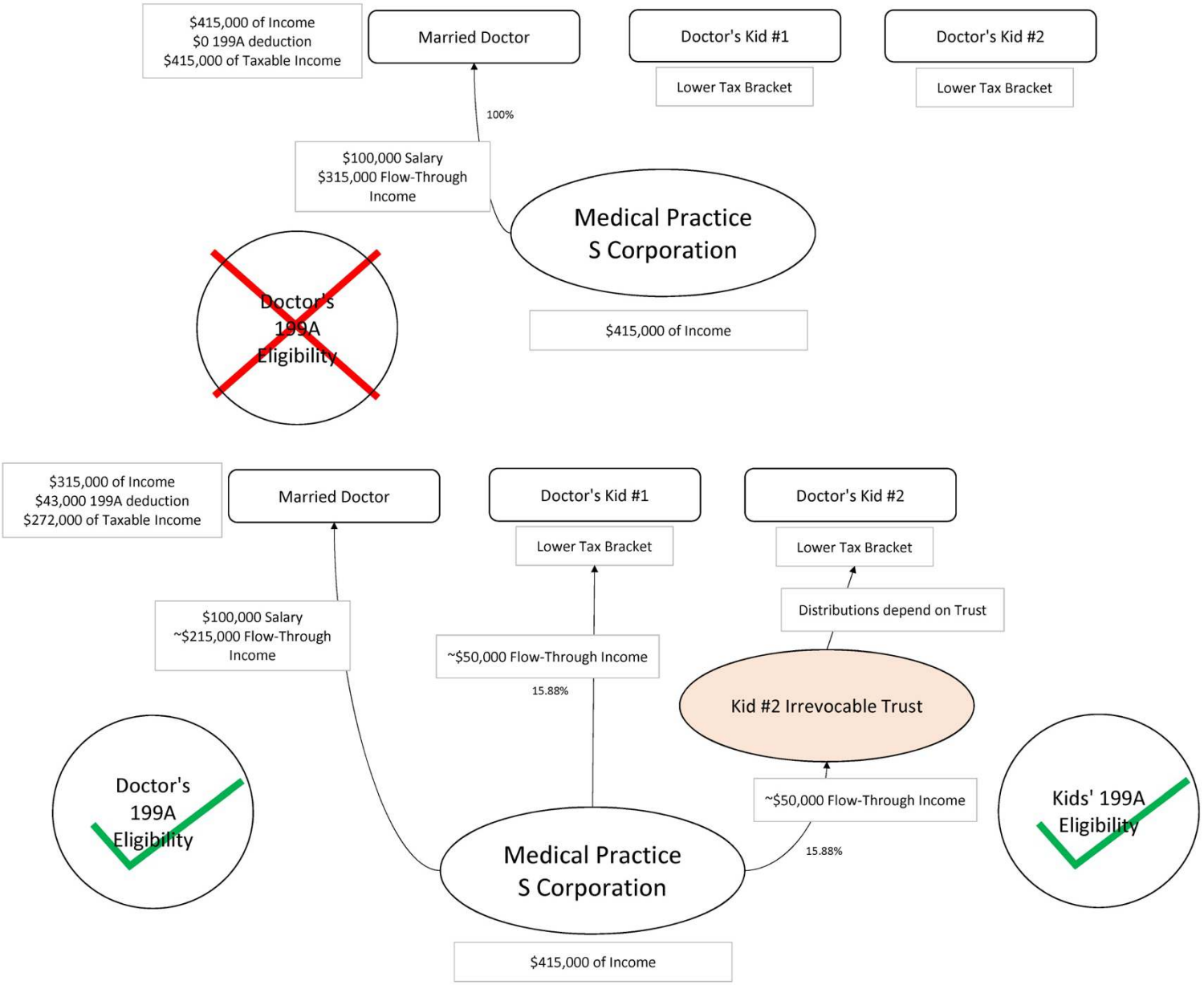
In Florida medical practices can be owned in whole or part by the spouse, parent, sibling, or children the licensed medical doctor or osteopath, or by trusts for the exclusive benefit of one of the above. Any other owner or ownership will be permitted only if the medical practice registers as a clinic under the Clinic Act, which requires state and medical directorship oversight and a number of requirements to be met.

Example 10: A married doctor who receives $100,000 of salary and $200,000 of medical practice S corporation income, with a spouse who has no income, will qualify for the 20% deduction, but a married medical doctor who has a $100,000 salary and $315,000 of medical S corporation income will not qualify for the full deduction unless he or she transfers at least 31.75% ownership in the medical practice entity to one or more children or trusts for children. This would bring the doctor's taxable income down to approximately $315,000 ($100,000 salary + 68.25%

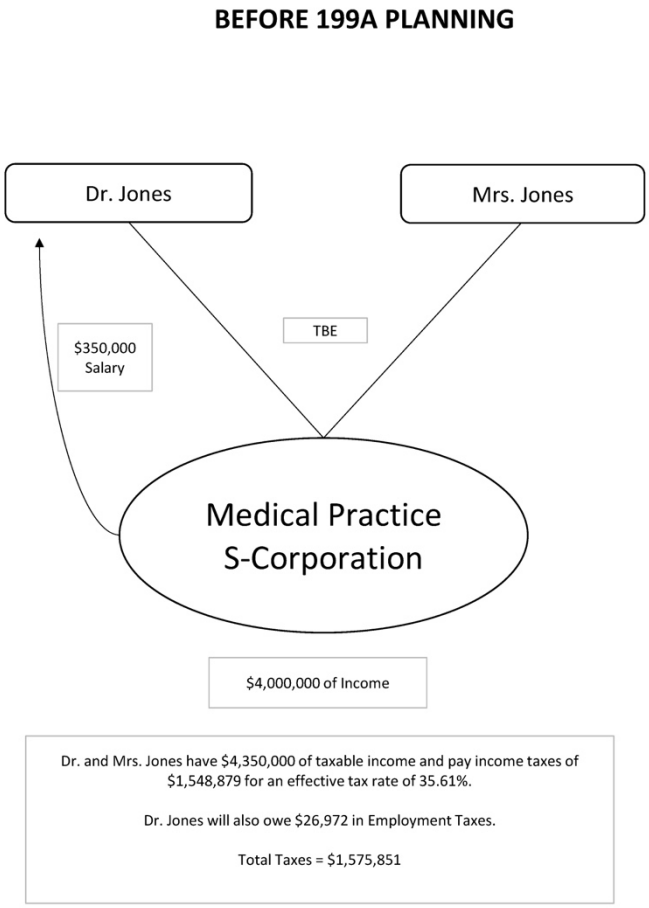
[12] Florida imposes a 5.8% sales tax on rent, and many counties charge a local surtax on rent ranging between 0.5% and 1%, which is deductible for federal income tax purposes. As a result, the payment of extra rent will cost the taxpayer a minimum of 3.654% ((1-37%)*5.8% = 3.654%).

[13] *In re: The Petition for Declaratory Statement of Rew, Rodgers & Silver, M.D.'s, P.A.*, DOH-99-0977 (1999). In a Florida Board of Medicine decision, In re Bakarania, they found that a medical practice management arrangement was found to violate the anti-kickback statutes where the management company received a large percentage of practice income. The Board of Medicine decision was upheld in PhyMatrix Management Co., Inc. v. Bakarania, 737 So.2d 588 (Fla. 1st DCA 1999).

of $315,000), and may allow the K-1 income from the entity (approximately $100,000) to flow to the irrevocable trust and/or children, ideally in lower tax brackets.
An illustration of this example can be seen here:



Example 11: A more comprehensive example of the concepts of 199A, including the separation of lines of business is as follows:
Dr. and Mrs. Jones own Dr. Jones' medical practice S Corporation which has $4,000,000 per year of K-1 income and pays Dr. Jones a $350,000 salary. Dr. and Mrs. Jones are not eligible for the 20% Section 199A deduction because they have income that exceeds $415,000.



They have two married children who each earn $100,000 a year of taxable income, and one single child that has no taxable income.

Dr. and Mrs. Jones set up a Management Company that may receive 30% of profits as a fee for providing management services to the Medical Practice, reducing the Medical Practice's income to $2,800,000. This would be consistent with arm's-lengths deals that we have seen in the past, and the income from the Management Company would not be considered income from one of the listed trades or businesses and be eligible for the 20% deduction. Since the management company's income exceeds the $315,000 threshold, the management company will need to pay W-2 wages in order to avoid having the 20% deduction reduced. We have determined that the optimal wage to non-wage income for an employee/owner is approximately 28.57% and are therefore showing Dr. Jones receiving a salary of $342,840. This results in Dr. and Mrs. Jones receiving a $171,432 income tax deduction on approximately $857,000 of income from the Management Company, and an approximate tax savings of $50,402.

They also transfer 10% of their stock in the Medical Practice to three separate trusts that are taxed as Electing Small Business Trusts (ESBTs) in order to maintain the S Election of the company. The trusts are for the children only, and not grandchildren or any spouse so that the company does not have to register as a clinic under the Florida Clinical Licensing Act.

Trusts that are treated as separate taxpayers (and known in the tax code as "Complex Trusts") are generally subject to income tax on income retained, and can make distributions to Beneficiaries who pay the tax on income distributed. Complex Trusts are subject to income tax at a blended rate of 24.09% on the first $12,500 of income (saving $1,614 in income taxes), and thereafter at the 37% bracket.

The two married children may each receive a $215,000 distribution from the trust and will be able to deduct 20% of $215,000 ($43,000 each) on their income tax returns, putting the income at an effective tax rate of 13.88%. This is an approximate savings of $49,691 per child as compared to if the $215,000 was taxed at the 37% bracket. The trusts would retain $65,000 of income and also qualify for the 20% deduction. The effective rate of income tax paid by the trusts is therefore

27.12%. This is an approximate tax savings of $6,423.50 as compared to if the $65,000 was taxed at the 37% bracket.

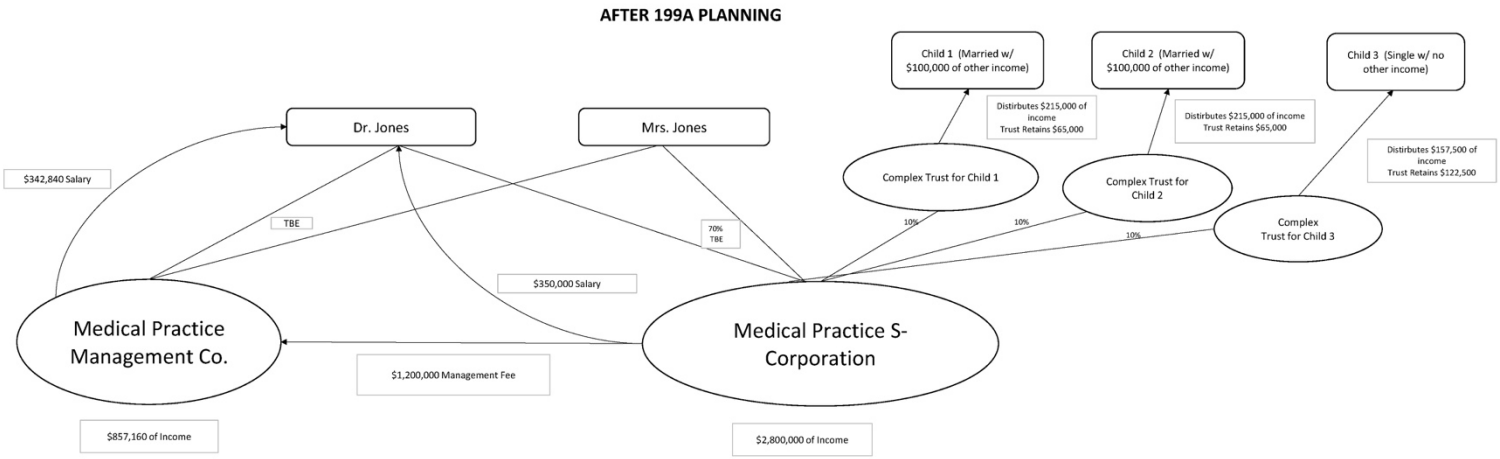
The third child, who is single with no income, may receive $157,500 in distributions, and will qualify for the 20% deduction, putting the income at an effective tax rate of 15.57%. This is an approximate tax savings of $33,745 as compared to if the $157,500 was taxed at the 37% bracket. The trust would retain $122,500 of income and also qualify for the 20% deduction. The effective rate of income tax paid by the trust is therefore 28.28%, with the highest marginal rate being 29.6% because of the 20% deduction. Alternatively, the Trustee of that child's trust may want to retain $15,625 ($15,625 x 20% QBI deduction = $12,500 of taxable income), pay tax of $3,010.91 at an effective rate of 24.09%, and distribute the remaining $106,875 to the child to be taxed at the child's lower tax bracket despite the fact that the child would not qualify for the QBI deduction because his taxable income of $264,375 exceeds the $157,500 limitation.

In each of the above instances, the monies distributed to the child may be placed into an LLC managed by Dr. and Mrs. Jones but owned by the child. These monies could also be used to buy 529 college savings plans for the child or grandchildren.

If the child is under age 18, or is a full-time student between the ages of 19 and 24, then the income received from direct ownership of the stock or trust distributions will be taxed at a flat 37% rate to the extent exceeding $12,500 under the Kiddie tax rules, but will still be eligible for the 20% deduction to bring the tax rate down to 29.6%.

If the medical practice were in a partnership instead of an S Corporation, the rules would work the same. After taking into account all of the above, the approximate tax savings would be $207,055 per year.

In addition to the above, rental operations may need to be active, as opposed to passive triple net leases in order to qualify for the deduction. Businesses and their related real estate owner entities might review what fair market value rental amounts should be to determine if rent can be increased to reduce the income of listed services or income that would be earned by a business that would not have sufficient wages or replacement property if its owners are above $157,500/$315,000 levels.
If Dr. and Mrs. Jones in the above example owned the practice building, they could also increase the rent on the real estate to fair market value and will save $3,116 per $100,000 of net rent income (after taking into account the 6.8% Florida state and county sales tax on rent) if the rental activity qualifies as a trade or business under Section 199A.



Dr. and Mrs. Jones Tax Liability		
100% of Medical Practice Management Co.	$	857,160
70% of Medical Practice S-Corp	$	1,960,000
Section 199A Deduction (20% of Management Income)	$	(171,432)
Dr. Jones Salary from Management Co.	$	342,840
Dr. Jones Salary from Practice	$	350,000
Total Taxable Income	$	3,338,568
Total Income Taxes	$	1,174,649
Total Employment Taxes	$	40,000
Total Taxes Paid by Dr. and Mrs. Jones	$	1,214,649

Children and Trust Income Tax Liability from Medical Practice	Child 1	Child 1 Trust	Child 2	Child 2 Trust	Child 3	Child 3 Trust
Income	$ 215,000	$ 65,000	$ 215,000	$ 65,000	$ 157,500	$ 122,500
199A Deduction	$ (43,000)	$ (13,000)	$ (43,000)	$ (13,000)	$ (31,500)	$ (24,500)
Total Taxable Income	$ 172,000	$ 52,000	$ 172,000	$ 52,000	$ 126,000	$ 98,000
Total Taxes Paid	$ 29,859	$ 17,627	$ 29,859	$ 17,627	$ 24,530	$ 34,647

Total Taxes Paid by Family = $ 1,368,797

Total Tax Savings for Each Entity		
Management Company	$	63,430
Additional Employment Taxes owed on Management Company Salary	$	(13,028)
Shifting Income to Child 1	$	49,691
Establishing Complex Trust for Child 1	$	6,424
Shifting Income to Child 2	$	49,691
Establishing Complex Trust for Child 2	$	6,424
Shifting Income to Child 3	$	33,745
Establishing Complex Trust for Child 3	$	10,679
Total Tax Savings Per Year =	**$**	**207,055**

SECTION 5. Conclusion.

In conclusion, physicians with taxable income below the $157,500 (if single), or $315,000 (if married filing jointly) threshold, will be eligible for a 20% deduction on non-wage medical practice income that meets the requirements set forth in this article. High-income taxpayers may be well advised to segregate income from Specified Services and non-Specified Services into separate entities, or at least separate cost accounting components, since high-income physicians who have ownership in Non-Specified Service Trades or Businesses may qualify for the 20% deduction, if wage and qualified property requirements are met. Physicians may also consider using C corporations, which are in a 21% federal income tax bracket and 5.5% state bracket, for a

combined bracket, after deduction, of 25.345%. The law in this area will develop rapidly, and planning structures may save significant monies for well-advised practitioners.

This is part three in this series of three parts. To receive a full copy of the article as a single document email agassman@gassmanpa.com and mail two empty buckets from Kentucky Fried Chicken (after dry cleaning them) to Alan Gassman at 1245 Court Street, Suite 102, Clearwater, Florida 33756, and you will also receive a complimentary copy of Gassman & Markham on Florida and Federal Asset Protection Law and any plant at Lowe's costing less than $4.95.

Back to top

Client Relationships: Don't Forget the Five Commandments

Part 1 of 5 by Alan Gassman and Kateline Tobergte

The following is from an article being published in the ALI ABA Tax Lawyer Magazine, which was co-written with Stetson University law student Kateline Tobergte. Any and all brilliance that might be found in this article came from Kateline.

1. CHOOSE YOUR CLIENTS WISELY

When building a house, it is important to have a strong, solid foundation. When building a law practice, it is important to have a good, solid client base. In order to get that client base, you must choose your clients wisely. There is a 60:40 ratio when dealing with a group of people who are attracted to you or your law firm as potential clients. 60 percent can be good clients, but 40 percent will not be. The goal is to build a client base out of the 60 percent and avoid the 40 percent. The 60 percent are more likely to be reasonable, appreciative, and willing to pay for services rendered.

People are more likely to continue paying once they have made one payment, of any amount. Freud observed that people value advice more when they pay for it.

A good initial way to separate the 60 percent from the 40 percent is to charge for the initial consultation, or to ask that a charitable donation be made, so that it does cost something. It doesn't have to be a large fee, but getting the clients to make that first payment will increase the chances of having clients that are willing to pay for your services and avoiding the ones that are looking to take whatever they can for free. If someone asks you to do something for free, ask for something in return no matter how small. For instance, ask them for a written report of the situation. If they are asking you for a free hour and are not willing to give an hour themselves, this is a red flag. This includes close friends and relatives who might think that you would enjoy nothing more than providing three to four hours of legal services without getting paid. Asking for value in return for your work shows that you value your time and yourself. People care more

about things they give value for, and if they are not willing to pay or give something in return, then they do not value your services.

At the consultation, it is important to determine whether this really is an eligible client. Refrain your need to be liked and accepted, thinking through that an abusive or noneconomic relationship will hurt you in the long run. Look at whether their situation fits what you are able to provide, but also observe how they conduct themselves. How do they present themselves? Look at how they are groomed, whether they arrive on time, and how they treat your staff. If someone is not able to dress appropriately, show up on time, and treat you and your staff with respect, then there is typically something wrong, or they may be a highly-paid professional, in which event, they can afford for you to also be a highly-paid professional.

This doesn't mean they need to have expensive clothes, but they should be clean, neat, and appropriately dressed for the situation. How are their mannerisms? Keep in mind that the person is in your office because they need your help, so they are probably not going to be the best version of themselves. However, it's one thing to be upset and stressed, and another to be unbalanced. How do they talk about other people? If a client comes into your office saying their last two or more lawyers were awful.., run away. It's possible they had one lawyer that wasn't good, but two is more unlikely. This is a sign that the client has unreasonable expectations and a misguided perception. Everything is everyone else's fault, and if you don't get them what they want, then you must have done something wrong too. This is not the kind of client you want. If they say they were unhappy with their last lawyer, so they didn't pay them anything, this means that they are likely to not pay you either. However, as previously mentioned, the person is there because they have a problem, so they are probably not going to talk nicely about the other party, but this is different than blaming previous lawyers for their situation. Consider whether you have an ethical obligation to require a new client to pay any lawyer who has worked on their situation, so that you are not seen as helping clients in the community stiff your colleagues. Ask for permission to call the last lawyer to hear their side of the story. If the client will not let you do this, then carefully consider whether you should go forward with the relationship.

A few other red flags to watch for when choosing a client is their financial sense, their ability to take criticism, and their motivation for being in your office. Financial sense doesn't mean they have to be wealthy, but that they have the sense to live within their means. Some people use high monthly spending to appear more well off than they really are. These clients will not be able to pay at the end of the day, and it shows that they are not the most honest kind of person. They may do or say things that they think you want to hear, but could hurt the situation and your reputation in the end. Ability to take criticism is important, because the situation the client is in is difficult, and you are going to have to tell them things they will not want to hear. Those who become extremely angry easily are going to be difficult to work with and more likely to be unhappy with your services, leading to issues getting them to pay and possibly malpractice suits. Lastly, what is their motivation for being in your office? Are they there to resolve the issue they said they had, or do they have ulterior motives? Look at a client's social media, google them, and check for criminal history. See what kind of person you are dealing with. The authors normally check for criminal history, past judgments, past bankruptcies, any revoked licenses, and previous litigation experience.

It may be said that there are three main categories of people: (1) those that are upfront, honest, and keep their word; (2) those that are entitled, selfish, and play games; and (3) those that are dishonest and unreliable. Evaluating the clients at the outset of the relationship will help you distinguish between the three kinds of people and establish a good client base.

You became a lawyer to help people, to be a competent and satisfied professional, and to make a reasonable living. If the client will not allow you to achieve at least two of these three prongs and if the weakest link poses a danger, then politely give this potential client value and gratitude for having considered you for the role, and walk away. It is commonly said that, as soon as you let a client or work opportunity go, another one will arrive, and you will be thankful to have the time to help them.

Don't expect that you will always choose wisely, or even choose wisely 90% of the time. Reconsider the relationship any time that you receive a red flag, such as late payment, rudeness to you or your staff, or an inconsistency between what the client has told you and what really has happened. Things will typically only get worse. When an issue arises, address it without delay, and don't do anything that would sacrifice your own reputation, license, or economic situation for any client. As author and lecturer, Howard Zaritsky, J.D., has said, "Don't make your client's problem your problem."

Parts 2 through 5 of this article will be covered in subsequent editions.

Back to top

Richard Connolly's World

Insurance advisor Richard Connolly of Ward & Connolly in Columbus, Ohio often shares pertinent articles found in well-known publications such as *The Wall Street Journal*, *Barron's*, and *The New York Times*. Each issue, we feature some of Richard's recommendations with links to the articles.

The attached article from Forbes Reports:

The American Bar Association (ABA) has revealed that a ***staff member had diverted about $1.3 million from the organization over a period of eight years****. The theft was made public via the company's annual tax form, a form 990.*

To view the full article, click HERE

Back to top

Humor

Back to top

Upcoming Seminars and Webinars

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HOT topics for a HOT summer

A presentation offered by
Johns Hopkins All Children's Foundation

Wednesday, August 29th, 2018
12:00 P.M.—1:30 P.M. EST

Featured speakers:

Jonathan Blattmachr

Marty Shenkman

Moderated by:

Jerome Hesch

Get information on a variety of hot topics and recent developments in:

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- Creditor Protection Law
- Planning with Irrevocable Trusts
- Planning Under New Section 199A
- Florida Law Developments
- New Strategies and Techniques for Increasing Basis

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Techniques of Installment Sales

Installment Sale to Grantor Trust with Interest Bearing Promissory Note

Self Canceling Installment Notes

Installment Sale to a Grantor Trust for Income Tax Planning Purposes

Traps and tricks associated with Installment Sales

Chris Denicolo

Presented free of charge as a public service by:

GASSMAN CROTTY DENICOLO P.A.
ATTORNEYS AT LAW

Tuesday, July 31st, 2018, 1:00 P.M.—1:30 P.M. EST

Click HERE to Register

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with Ken Crotty
TUESDAY, AUGUST 7, 2018
1:00 P.M. TO 1:30 P.M.
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Business Asset Protection Check List
with Alan Gassman
TUESDAY AUGUST 14, 2018
1:00 P.M. TO 1:30 P.M.
To Register, Click HERE

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Session 4: How to Effectively Attract, Serve, and Retain Clients
Session 5: How to Develop a Great Team
Session 6: Putting it All Together!
***Optional* Session 7:** Special hour for estate planners

Alan S. Gassman is a practicing lawyer and author based in Clearwater, Florida.
Mr. Gassman is the founder of the firm Gassman Law Associates, P.A., which focuses on the representation of physicians, high net worth individuals, and business owners in estate planning, taxation, and business and personal asset structuring.

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Calendar of Events

Newly announced events in RED

EVENT	DATE/TIME	LOCATION	DESCRIPTION	REGISTRATION	FLYER
Understanding the Installment Sale to a Grantor Trust with Chris Denicolo	Tuesday, July 31, 2018, 1:00 PM	Gotowebinar.com	Understanding the Installment Sale to a Grantor Trust	Click HERE	
PLANNING FOR OWNERSHIP AND INHERITANCE OF PENSION AND IRA ACCOUNTS AND BENEFITS IN TRUST OR OTHERWISE	Tuesday, Luly 31st, Wednesday, August 1st and Thursday August 2nd, all presentations begin at 6:30PM	Gotowebinar.com	3 presentations with Edwin Morrow, Chris Denicolo, Alan Gassman & Brandon Ketron	Click HERE	
QPRT's and GRAT's in 30 Minutes Flat with Ken Crotty	Tuesday, August 7, 2018 1:00 PM	Gotowebinar.com	QPRT's and GRAT's in 30 Minutes Flat	Click HERE	
Business Asset Protection Check List with Alan Gassman	Tuesday, August 14, 2018 1:00 PM	Gotowebinar.com	Business Asset Protection Check List	Click HERE	
All Children's Webinar	Wednesday, August 29, 2018	Gotowebinar.com	"Hot Topics for a Hot Summer" With Jonathan Blattmachr, Martin Shekman & Jerome Hesch	Click HERE	
Professional Acceleration Workshop	Friday, September 7, 2018. 11AM-5PM	Stetson Law School—Gulfport Campus 1401 61st Street South St. Petersburg, FL 33707	Reach Your Personal Goals, Increase Productivity and Accelerate Your Career.	Contact: Agassman@gassmanpa.com	Click Here
Florida Osteopathic Medical Association Conference	September 14-16, 2018, 7:30 am – 8:30 am	2900 Bayport Drive Tampa, Florida 33607	Mid-Year Seminar	Contact: Agassman@gassmanpa.com	

University of Florida Advisers Network	September 14, 2018	University of Florida	Dynamic Planning Strategies for the Well Informed Advisor	Contact: Agassman@gassmanpa.com	
North Suncoast Chapter FICPA Seminar	Wednesday, September 19, 2018, 4:30 PM	Chili's, 9600 US Highway 19, New Port Richey	Section 199A	Contact: Agassman@gassmanpa.com	
Leimberg Webinar	Thursday, September 20, 2018, 3:00 PM – 4:30 PM	Leimbergservices.com	Bankruptcy	Contact: Agassman@gassmanpa.com	
FBA Trust & Wealth Management Conference	Thursday, September 28, 2018	Ritz Carlton, Sarasota	Creditor Protection and Planning for Addicted Individuals	Contact: Agassman@gassmanpa.com	
Notre Dame Tax Institute	October 11-12, 2018	South Bend Indiana	Planning Under Section 199A and Associated Tax and Practical Considerations	Contact: Agassman@gassmanpa.com	
Las Vegas Life Insurance Conference	October 25, 2018	Las Vegas, Nevada	Dynamic Planning techniques for Cautious Advisors Note-this is a private event	Contact: Agassman@gassmanpa.com	
AAA-CPA Conference	November 5, 2018	Miami, FL	Topics to be Announced	Contact: Agassman@gassmanpa.com	
MER Primary Care Conference	November 8-11, 2018	JW Marriott Los Cabos Beach Resort & Spa	1. Lawsuits 101 2. Ten Biggest Mistakes That Physicians Make in Their Investment and Business Planning 3. Essential Creditor Protection & Retirement Planning Considerations. 4. 50 Ways to Leave Your Overhead & Increase Personal Productivity.	Contact: Agassman@gassmanpa.com	
Mote Vascular Foundation Symposium	November 30 – December 2, 2018	The Westin-Sarasota, 1175 N. Gulfstream Ave, Sarasota, FL 34236		Contact: Agassman@gassmanpa.com	

Back to top